



**NEW FLYER**

**NEW FLYER INDUSTRIES INC.**

**Annual Information Form**

**March 24, 2014**

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## NEW FLYER INDUSTRIES INC.

### GENERAL

The information, including any financial information, disclosed in this Annual Information Form is stated as at December 29, 2013 or for the year ended December 29, 2013, as applicable, unless otherwise indicated. Unless otherwise indicated, all dollar amounts are expressed in U.S. dollars and references to “\$”, “US\$” and “U.S. dollars” are to the lawful currency of the United States. References to C\$ are to the lawful currency of Canada. References in this Annual Information Form to “we”, “us”, “our” or the “Company” refer to New Flyer Industries Inc. (“NFI”) and all of its direct or indirect subsidiaries, including New Flyer Industries Canada ULC (“NFI ULC”), New Flyer of America Inc. (“NFAI”), NABI Bus, LLC (“NABI Bus”) and NABI Parts, LLC (“NABI Parts”) and references to “NFI” or the “Issuer” refer to New Flyer Industries Inc. References to “New Flyer” refer just to NFI ULC and NFAI. References to “NABI” refer to NABI Bus and NABI Parts. References in this Annual Information Form to “management” are to management of the Company.

Certain statements in this Annual Information Form are “forward-looking statements”, which reflect the expectations of management regarding the Company’s future growth, results of operations, performance and business prospects and opportunities. The words “believes”, “anticipates”, “plans”, “expects”, “intends”, “projects”, “estimates” and similar expressions are intended to identify forward-looking statements. These forward-looking statements reflect management’s current expectations regarding future events and operating performance and speak only as of the date of this Annual Information Form. Forward-looking statements involve significant risks and uncertainties, should not be read as guarantees of future performance or results, and will not necessarily be accurate indications of whether or not or the times at or by which such performance or results will be achieved. A number of factors could cause actual results to differ materially from the results discussed in the forward-looking statements, including, but not limited to, the factors discussed under “Risk Factors”. Although the forward-looking statements contained in this Annual Information Form are based upon what management believes to be reasonable assumptions, investors cannot be assured that actual results will be consistent with these forward-looking statements, and the differences may be material. These forward-looking statements are made as of the date of this Annual Information Form and the Company assumes no obligation to update or revise them to reflect new events or circumstances, except as required by applicable securities law.

All of the data presented in this Annual Information Form with respect to market share, the number of heavy-duty transit buses in service and the number of heavy-duty transit buses delivered is measured in, or based on, “equivalent units”. One equivalent unit represents one 30-foot, 35-foot or 40-foot heavy-duty transit bus. One articulated bus represents two equivalent units. An articulated bus is an extra-long bus (55-feet to 60-feet in length), composed of two passenger compartments connected by a joint mechanism. The joint mechanism allows the vehicle to bend when the bus turns a corner, yet have a continuous interior.

Throughout this Annual Information Form, unless otherwise indicated, all references to “IFRS” are to International Financial Reporting Standards.

### **Definitions of EBITDA and Adjusted EBITDA**

References to “EBITDA” are to earnings before interest expense, income taxes, depreciation and amortization; losses or gains on disposal of property, plant and equipment; unrealized foreign exchange losses or gains on non-current monetary items and forward foreign exchange contracts and fair value adjustment to embedded derivatives. References to “Adjusted EBITDA” are to EBITDA after adjusting for: the effects of certain non-recurring and/or non-operations related items that have impacted the

business and are not expected to recur, including non-recurring transitional costs relating to business acquisitions, loss on debt repurchase, loss on exercise of redemption right, past service pension costs, realized and unrealized investment tax credits (“ITCs”), stock-based compensation and costs associated with assessing strategic and corporate initiatives.

Management believes EBITDA and Adjusted EBITDA are useful measures in evaluating the performance of the Company. However, EBITDA and Adjusted EBITDA are not recognized earnings measures under IFRS and do not have standardized meanings prescribed by IFRS. Readers of this Annual Information Form are cautioned that EBITDA and Adjusted EBITDA should not be construed as an alternative to net earnings or loss determined in accordance with IFRS as an indicator of NFI’s and/or the Company’s performance or to cash flows from operating, investing and financing activities determined in accordance with IFRS as a measure of liquidity and cash flows.

NFI’s method of calculating EBITDA and Adjusted EBITDA may differ materially from the methods used by other issuers and, accordingly, may not be comparable to similarly titled measures used by other issuers. Dividends are not assured, and the actual amount of dividends received by holders of common shares of NFI (the “Shares”) will depend on, among other things, the Company’s financial performance, debt covenants and obligations, working capital requirements and future capital requirements, all of which are susceptible to a number of risks. See “Risk Factors”.

### **Use of Market and Industry Data**

This Annual Information Form includes market and industry data that has been obtained from third party sources, including industry publications and industry associations, as well as industry data prepared by management on the basis of its knowledge of and experience in the industry in which the Company operates (including management’s estimates and assumptions relating to the industry based on that knowledge). Management’s knowledge of the industry has been developed through its experience and lengthy participation in the industry. Management believes that its industry data is accurate and that its estimates and assumptions are reasonable, but there can be no assurance as to the accuracy or completeness of this data. Third party sources generally state that the information contained therein has been obtained from sources believed to be reliable, but there can be no assurance as to the accuracy or completeness of included information. Although management believes it to be reliable, neither the Issuer nor management have independently verified any of the data from third party sources referred to in this Annual Information Form or ascertained the underlying economic assumptions relied upon by such sources.

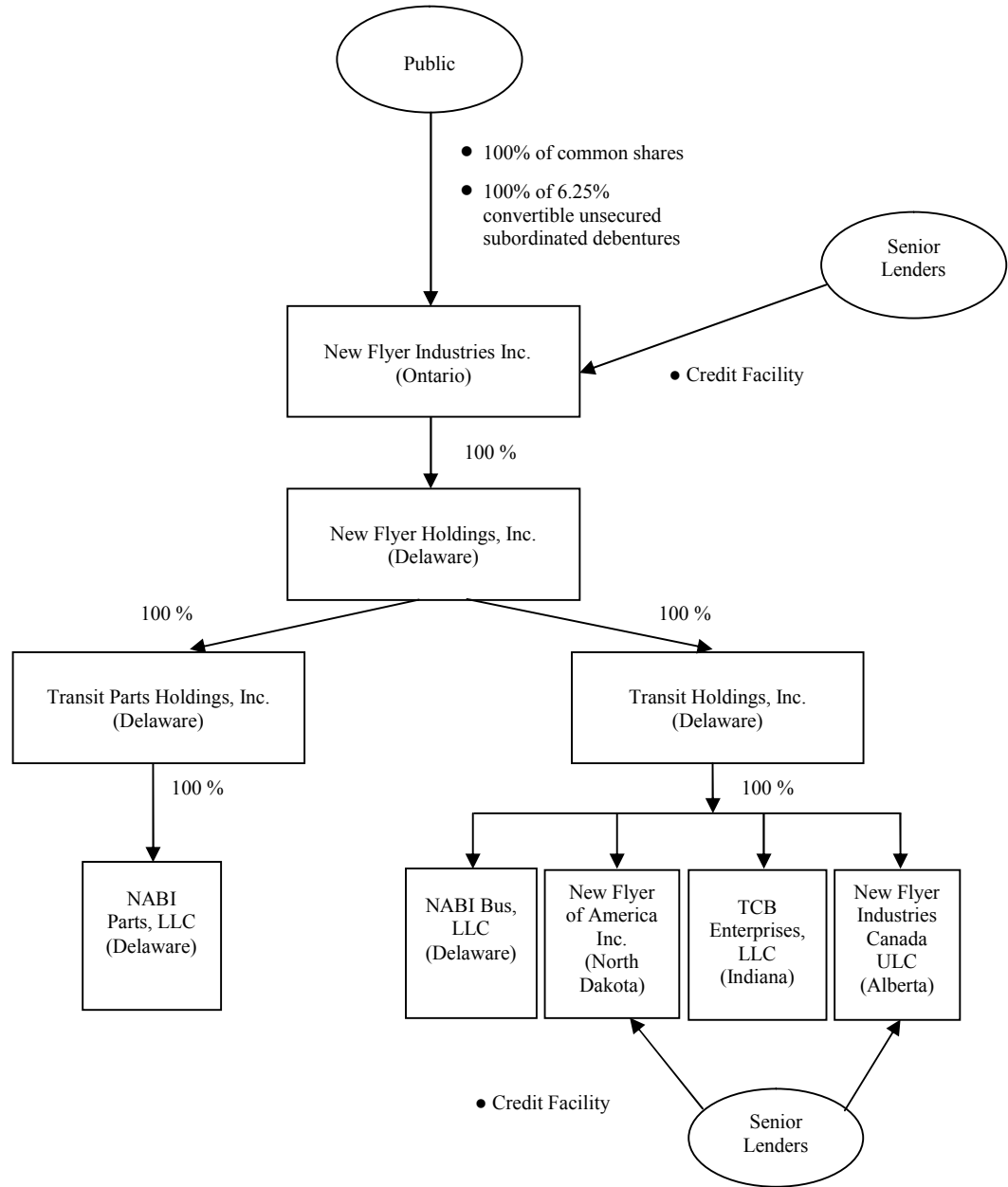
## CORPORATE STRUCTURE

### The Issuer

NFI is a corporation established under the *Business Corporations Act* (Ontario) on June 16, 2005. The registered office of NFI is located at Suite 3000, 79 Wellington Street West, Toronto, Ontario, M5K 1N2.

### Ownership Structure

The following chart shows the Issuer and its principal subsidiaries:



## GENERAL DEVELOPMENT OF THE BUSINESS

### Recent Developments

#### *Fiscal 2011*

New Flyer completed its initial public offering of income deposit securities (“IDS”) on August 19, 2005. Each IDS consisted of one Share and C\$5.53 principal amount of 14.0% subordinated notes of New Flyer Industries Canada ULC (“NFI ULC”) (the “Subordinated Notes”). In 2011, NFI completed a non-cash rights offering (the “Rights Offering”) to facilitate New Flyer’s conversion from an IDS structure to a traditional common share structure (the “Common Share Conversion”). Pursuant to the Rights Offering, each shareholder was issued one right (a “Right”) for each Share held, which entitled such shareholder to subscribe for nine additional Shares in exchange for C\$5.53 principal amount of Subordinated Notes (being the principal amount of Subordinated Notes represented by each IDS at that time) prior to August 18, 2011, the expiry date for the Rights Offering. Shareholders exercised approximately 89% of the Rights issued by tendering approximately C\$242.3 million principal amount of Subordinated Notes in exchange for 394,315,425 Shares. Immediately following the closing of the Rights Offering, the Shares (including Shares formerly represented by IDSs) were listed and posted for trading on the Toronto Stock Exchange (the “TSX”) under the symbol “NFI”.

In connection with the Rights Offering, effective with the July 2011 distribution, payable on August 15, 2011 to IDS holders of record on July 29, 2011, the Company decreased its IDS distributions from C\$1.17 per annum to C\$0.86 per annum, consisting of an annual dividend payment of C\$0.086 per pre-Consolidation Share (compared to the previous annual dividend level of C\$0.396 per pre-Consolidation Share) and an annual interest payment of C\$0.774 per C\$5.53 principal amount of Subordinated Note. Following the Consolidation (described below), the dividend rate was adjusted accordingly and NFI began paying annual dividends of C\$0.86 per Share. The board of directors of NFI (the “Board”) maintained this dividend rate on a monthly basis until August 2012 when the remaining Subordinated Notes were redeemed. Following the redemption of the remaining Subordinated Notes, the Board approved a new annual dividend rate of C\$0.585 per Share.

On July 26, 2011, NFI ULC and New Flyer of America Inc. (“NFAI”) entered into a second amended and restated senior credit facility agreement with a syndicate of financial institutions in the amount of \$195 million, which was further amended and restated on June 25, 2012, amended again on March 1, 2013 and amended and restated on June 21, 2013 (the “Credit Facility”). The Credit Facility currently consists of a \$142 million secured term loan facility and a revolving credit facility of up to \$115 million (including a \$55 million letter of credit sub-facility). The Credit Facility also includes an accordion feature of \$75 million for future investment or acquisition opportunities. The Credit Facility matures on April 24, 2017. See “Description of Capital Structure – Credit Facility”.

On August 29, 2011, the Board adopted a shareholder rights plan (the “SRP”). The SRP was ratified by NFI’s shareholders at its special meeting of shareholders held on September 30, 2011 (the “Special Meeting”). The primary objectives of the SRP are (i) to provide the Board with sufficient time to explore and develop alternatives for maximizing shareholder value if an unsolicited take-over bid is made for NFI, (ii) to provide all shareholders with an equal opportunity to participate in such a bid, and (iii) to ensure, to the extent possible, that all shareholders are treated fairly in connection with any take-over bid. The SRP was not adopted in response to any specific proposal to acquire control of NFI. Additional details regarding the SRP are described below under the heading “Description of Capital Structure – Share Capital of NFI” and in NFI’s management information circular for the Special Meeting dated August 29, 2011 (the “Circular”). Copies of the Circular and the SRP are available on SEDAR at [www.sedar.com](http://www.sedar.com).

Pursuant to articles of amendment dated September 30, 2011, NFI consolidated its Shares (the “Consolidation”), pursuant to which one post-Consolidation Share was exchanged for every ten pre-Consolidation Shares, such that the number of outstanding Shares was reduced from 443,790,704 pre-Consolidation Shares to 44,379,070 post-Consolidation Shares (including Shares held in the form of an IDS). In connection with the Consolidation, the ratio of Shares and Subordinated Notes represented by each IDS was automatically adjusted such that each post-Consolidation IDS represented one Share and C\$55.30 principal amount of Subordinated Notes. The Consolidation was approved by NFI’s shareholders at the Special Meeting. Additional details regarding the Consolidation are described in the Circular, a copy of which is available on SEDAR at [www.sedar.com](http://www.sedar.com).

On December 9, 2011, NFI ULC announced the repurchase and cancellation of approximately C\$15.7 million aggregate principal amount of Subordinated Notes for a purchase price of approximately 107% of the principal amount. The repurchase and related costs were financed by utilizing approximately \$17 million of the \$75 million accordion term loan feature available under the Credit Facility.

### ***Fiscal 2012***

On March 21, 2012, NFI announced that it had entered into an agreement (the “Coliseum Agreement”) with Coliseum Capital Management, LLC (“Coliseum”), which, as at December 29, 2013, exercised control or direction over approximately 10.14% of the outstanding Shares, pursuant to which NFI agreed to include Adam Gray, a managing partner of Coliseum, as its nominee on the slate of directors proposed for election at NFI’s 2012 annual meeting of shareholders (the “Meeting”) and support Mr. Gray’s election as a director at the Meeting and at any meeting of shareholders in respect of the election (or removal) of directors held prior to the 2013 annual meeting of shareholders. Pursuant to the Coliseum Agreement, Coliseum agreed to vote its Shares in favour of management’s slate of directors during that same period. Mr. Gray was elected by shareholders to serve as a director at the Meeting. The Coliseum Agreement also provides that (i) Coliseum will not, subject to certain exceptions, acquire 20% or more of NFI’s outstanding Shares or take certain actions in relation to the solicitation of proxies, in each case until the later of six months following Coliseum ceasing to have a representative on the Board and 12 months following the date of the Meeting, and (ii) Coliseum will have a pre-emptive right to purchase Shares in certain circumstances to maintain its proportionate interest in NFI during that same period. A copy of the Coliseum Agreement can be found on SEDAR at [www.sedar.com](http://www.sedar.com).

On May 7, 2012, NFI entered into a long-term joint venture with Alexander Dennis Limited (“Alexander Dennis”), the United Kingdom’s largest manufacturer of single-deck and double-deck transit buses and coaches, pursuant to which the two companies agreed to collaborate to introduce a mid-sized low-floor bus for sale in Canada and the United States, which has subsequently been branded as the MiDi<sup>®</sup>. Under the arrangements of the joint venture, New Flyer is responsible for sales, marketing, manufacturing and aftermarket support with Alexander Dennis performing design, engineering, test and prototype development activities.

On June 5, 2012, NFI completed an offering of US\$65,000,000 aggregate principal amount of 6.25% convertible unsecured subordinated debentures (the “Debentures”). The net proceeds of the offering of the Debentures (the “Debenture Offering”) were used to redeem the outstanding Subordinated Notes (described below) and for general corporate purposes. The Debentures were posted for trading on the TSX under the trading symbol “NFI.DB.U”. See “Description of Capital Structure – Description of Debentures.”

On June 25, 2012, NFI ULC and NFAI entered into a third amended and restated senior credit facility agreement with a syndicate of financial institutions, which amended certain of the covenants effective on the redemption of the Subordinated Notes (described below). The changes to the covenants in the Credit Facility were intended to reflect the Company’s new capital structure following the redemption. The

Credit Facility was again amended on March 1, 2013 and further amended and restated on June 21, 2013. See “Description of Capital Structure – Credit Facility”.

On August 20, 2012, NFI ULC completed the redemption of all of its outstanding Subordinated Notes, including those held separately and those held in the form of IDSs. The redemption was financed with the net proceeds of the Debenture Offering. The Subordinated Notes were redeemed for a total price of C\$58.4812 per C\$55.30 principal amount of Subordinated Notes, representing a redemption price of C\$58.065 per C\$55.30 principal amount of Subordinated Notes (or 105% of principal), plus accrued and unpaid interest to and including the redemption date. On the redemption date, the IDSs were de-listed from the TSX and the Shares forming part of an IDS commenced trading separately under the trading symbol “NFI”. Following the redemption of the Subordinated Notes, on September 19, 2012, NFI ULC ceased to be a reporting issuer in all provinces and territories of Canada.

### ***Fiscal 2013***

On January 23, 2013, NFI announced that Marcopolo S.A. (“Marcopolo”), one of the world’s largest bus builders, agreed to make a strategic investment of C\$116 million to acquire 11,087,834 newly issued Shares, representing a 19.99% stake in NFI. In accordance with the investment agreement entered into by NFI and Marcopolo (the “Investment Agreement”), each Share was to be issued at a price of C\$10.50 per Share, or an approximate 20% premium to the 30 day volume-weighted average trading price of the shares on the TSX for the period ending January 23, 2013. 4,925,530 Shares were issued to a wholly-owned Canadian subsidiary of Marcopolo on February 15, 2013 for aggregate consideration of C\$52 million and the remainder of the shares (being 6,162,304 Shares) were issued to the same wholly-owned subsidiary of Marcopolo on June 21, 2013 for aggregate consideration of C\$65 million. NFI and Marcopolo also signed a Memorandum of Understanding to explore opportunities to cooperate on engineering, technical, purchasing and operational matters, with a focus on reducing New Flyer’s bus manufacturing and aftermarket part costs and enhancing New Flyer’s competitiveness. The companies further agreed to assess Marcopolo’s technology and products for possible introduction into the Canadian and US markets through New Flyer as well as New Flyer’s technology and products for potential distribution into global markets.

Under the Investment Agreement Marcopolo was granted the right to nominate a member to the Board for so long as it holds at least 10% of the outstanding Shares and was granted pre-emptive rights to purchase additional securities in certain circumstances to maintain its proportionate interest in NFI. Marcopolo also agreed to certain disposition and standstill restrictions including a requirement to hold its Shares for a period of at least two years and a restriction on acquisitions of additional NFI securities and certain other actions for a period of at least two years. The Investment Agreement also provides that if New Flyer in the future enters into an agreement with a third party providing for the acquisition of all of the Shares or assets of New Flyer, then Marcopolo will, subject to certain exceptions, agree to vote in favor of and to sell its Shares as part of the transaction unless Marcopolo has made an alternative proposal that the Board believes is superior or that the shareholders have determined to accept. A copy of the Investment Agreement can be found on SEDAR at [www.sedar.com](http://www.sedar.com).

On March 1, 2013, NFI ULC acquired certain assets from Daimler Buses North America (“DBNA”) relating to its Orion aftermarket parts business which supported the nearly 10,000 Orion heavy-duty buses then in operation in Canada and the United States with aftermarket parts. Under the terms of the transaction with DBNA, NFI ULC (i) acquired DBNA’s Orion aftermarket parts inventory, accounts receivable and assumed certain obligations under its parts contracts with transit customers, (ii) acquired an exclusive license to use the Orion proprietary parts designs in connection with New Flyer’s aftermarket parts business, and (iii) entered into an agreement under which New Flyer will be the exclusive supplier of parts to DBNA for its customer warranty obligations under Orion bus purchase contracts and pre-closing parts contracts. The companies also entered into a transition services agreement

for an interim period following the purchase, during which time the business was to be prudently and efficiently integrated into New Flyer's business. A copy of the purchase and sale agreement can be found on SEDAR at [www.sedar.com](http://www.sedar.com).

On June 21, 2013 NFI announced the acquisition of North American Bus Industries, Inc. from an affiliate of Cerberus Capital Management, L.P. ("Cerberus") for cash consideration of approximately \$80 million, virtually all for the satisfaction of affiliate debt. The acquisition excluded discontinued operations in Hungary and substantially all related assets and liabilities. With bus manufacturing operations in Anniston, AL, a parts distribution center in Delaware, OH, and a service center in Jurupa Valley, CA, NABI Bus is an innovative manufacturer of urban transit buses for U.S. customers. NABI Parts operates one of the transit industry's most sophisticated aftermarket parts organizations. The transaction, including related expenses, was funded using approximately C\$65 million in proceeds from the issuance of the second and final tranche of the strategic equity investment in New Flyer by Marcopolo. An additional \$20 million was drawn from the Company's Credit Facility.

Concurrent with the acquisition of North American Bus Industries, the Company completed the amendment and extension of the Credit Facility. Certain financial covenants and definitions in the Credit Facility were adjusted to reflect the acquisition of North American Bus Industries. The Credit Facility also includes an accordion feature of \$75 million for future investment or acquisition opportunities.

Copies of the North American Bus Industries purchase agreement and the Credit Facility can be found on SEDAR at [www.sedar.com](http://www.sedar.com).

In December 2013, the Company commenced production of the New Flyer MiDi<sup>®</sup> in its St. Cloud, Minnesota facility. The first purchase order for the mid-sized, low floor bus was received from a Canadian customer on November 7, 2013 and the first delivery of a MiDi<sup>®</sup> to a customer is expected to occur in the first half of 2014.

#### ***Fiscal 2014 Year-to-Date***

In February 2014, New Flyer entered into an agreement with ABC Companies, Inc. ("ABC") to serve as the exclusive distributor of New Flyer's MiDi<sup>®</sup> and Xcelsior<sup>®</sup> models to private bus and shuttle operators in the United States. ABC will market, sell and provide after-sales services through its established sales and services locations and through select independent dealerships. ABC is a leading provider of transit products including new and pre-owned highway coach vehicles, mid-size shuttle transport vehicles and advanced design heavy-duty transit equipment.

On March 4, 2014, the Company amended its agreement with A. Girardin Inc. ("Girardin") to include the MiDi<sup>®</sup> in addition to the Xcelsior<sup>®</sup> heavy-duty transit bus. New Flyer and Girardin first entered into a distributor's agreement in April 2011, to distribute the Xcelsior<sup>®</sup> heavy duty transit bus. Girardin will serve as the exclusive distributor of MiDi<sup>®</sup> and Xcelsior<sup>®</sup> transit bus models for all public and private customers in Quebec and private operators in Ontario and the Atlantic provinces. Under the terms of the agreement, Girardin will market, sell and provide after sales service for the MiDi<sup>®</sup> and Xcelsior<sup>®</sup> transit buses through its established service locations.

## **DESCRIPTION OF THE BUSINESS**

### **Business of the Company**

NFI was established to acquire an interest in New Flyer Holdings, Inc. ("NF Holdings"). NFI, NF Holdings and Transit Holdings, Inc. ("Transit Holdings") do not have any ongoing business operations of their own. NF Holdings depends on the operations and assets of its indirect wholly-owned operating

subsidiaries, TCB Enterprises, LLC (“TCB”), NFI ULC, NFAI and since June 21, 2013, NABI Bus and NABI Parts for cash distributions. NFI, in turn, depends on NF Holdings for cash distributions and interest payments from NFI ULC on intercorporate debt to pay dividends on its Shares and to make interest payments on the Debentures.

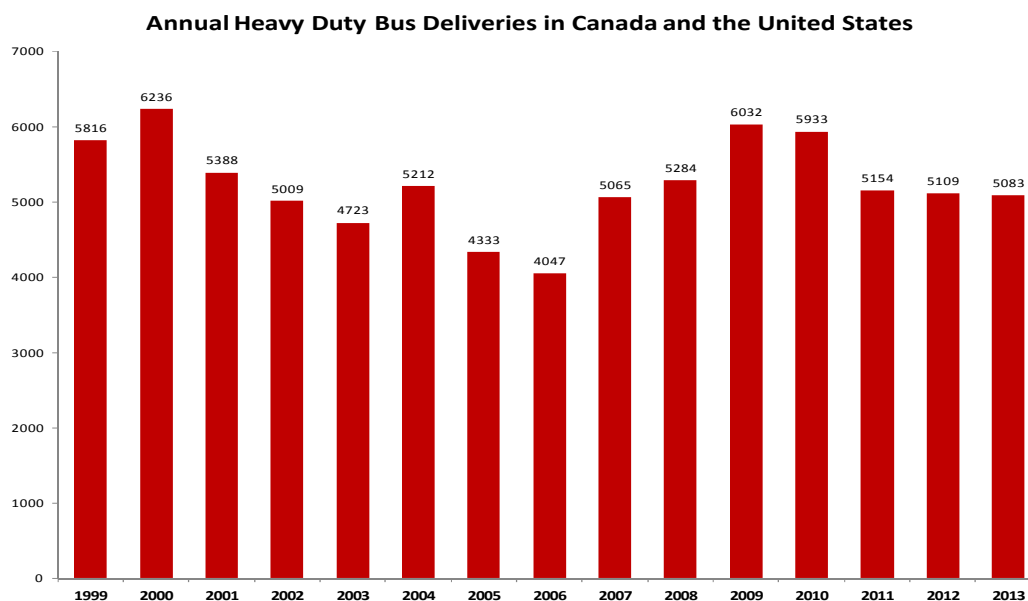
The Shares and Debentures are listed and posted for trading on the TSX under the symbols “NFI” and “NFI.DB.U”, respectively. The Shares are included by the TSX in the S&P/TSX SmallCap Index.

## Industry Overview

The Company is the leading manufacturer of heavy-duty transit buses in the United States and Canada and a leading provider of aftermarket parts and support. Heavy-duty transit buses are the backbone of intra-city urban public transportation systems throughout the United States and Canada. They consist of vehicles that are generally between 30 and 60 feet with seating capacity for up to 65 passengers. These buses operate in arduous stop and go conditions, often for up to 16 hours a day, seven days a week. Heavy-duty transit buses use a variety of propulsion systems in addition to diesel, including diesel-electric hybrid systems, compressed natural gas (“CNG”) systems, zero emission electric trolleys, select hydrogen fuel cell systems and now all-electric battery systems. Municipal and other local transit authorities are the principal purchasers of heavy-duty transit buses.

The broader heavy-duty bus manufacturing industry includes transit buses and motor coaches. The Company currently does not manufacture motor coaches (often referred to as highway coaches). There are well-established US federal funding programs for transit fleet replacements in place. However, most federal funding programs require a local contribution component, typically twenty percent of the total amount of the customer’s purchase requirements, and there has been pressure on local funding over the last several years due to the impact of the US recession on local tax revenues. There continues to be a trend based on environmental concerns for the expansion of transit services and for the exploitation of new technologies to enhance transit’s “green” potential.

Management’s estimates of total deliveries of equivalent units to customers in the United States and Canada over the period from 1999 to 2013 are shown in the chart below.



Source: Management estimates.

Notes: Deliveries indicated in number of equivalent units.

Although no reliable public data source exists regarding industry deliveries in Canada and the United States, management continues to try to refine its estimates and believes the heavy-duty transit bus industry absorbed approximately 5,100 equivalent units in 2013, approximately the same number of equivalent units delivered in 2011 and 2012. Management anticipates that for 2014, the market will increase slightly.

Transit ridership in both Canada and the United States has improved. At December 31, 2013, the American Public Transportation Association's ("APTA") ridership report indicated an increase in ridership of 1.09% in 2013 as compared to 2012, with bus ridership down 0.10% during the same period. However, U.S. transit ridership during the fourth quarter of 2013 increased 3.75% in all modes of public transportation compared with the previous year's fourth quarter, and specific bus ridership increased by 0.60% during the same period. According to APTA, the demand for public transportation rose last year as Americans took 10.6 billion trips from January through December 2013, which is the highest annual public transit ridership number in 57 years. The same report indicates Canadian ridership decreased by 1.14% in all modes of transit ridership during the fourth quarter of 2013, and decreased 0.07% year-to-date as compared to the previous year.

## **Company Overview**

New Flyer, together with its subsidiaries, NABI Bus and NABI Parts, is the leading manufacturer of heavy-duty transit buses in the United States and Canada and a leading provider of aftermarket parts and support. Management estimates that in 2013, New Flyer had an approximate 43% market share of the combined United States and Canadian heavy-duty transit bus industry based on deliveries of equivalent units in 2013. From its production facilities in Winnipeg, Manitoba and Crookston and St. Cloud, Minnesota, New Flyer has the broadest and most advanced product offering in the industry. NABI Bus operates from its production facilities in Anniston, Alabama.

The Company designs and manufactures a variety of heavy-duty transit buses from 30-feet to 60-feet in length and with diverse propulsion systems, including diesel, diesel-electric hybrid systems, CNG systems and zero emission electric trolleys. New Flyer has also developed a 40-foot hydrogen fuel cell bus and a 40-foot battery-electric propulsion bus. In addition to its engineering and manufacturing capabilities, the Company maintains one of the industry's leading aftermarket parts organizations, which is responsible for supporting an extensive range of post-sale activities, including parts distribution, support documentation and training.

For the fiscal year ended December 29, 2013, the Company generated revenue and Adjusted EBITDA of approximately \$1,199.4 million and \$94.7 million, respectively.

## **New Flyer History**

New Flyer's predecessor was founded in 1930 as a manufacturer of motor coaches and school buses. The name Flyer Industries Limited was adopted in 1971, at which time the company began to focus exclusively on heavy-duty urban transit buses. With its acquisition in 1986 by Den Oudsten, B.V. ("Den Oudsten"), Holland's largest bus manufacturer, the company became New Flyer Industries Limited. Den Oudsten was an innovation leader in the European bus manufacturing industry, having been the first manufacturer to introduce the low floor bus concept. Den Oudsten brought the low floor bus to North America through New Flyer in 1988 and it eventually became the industry standard in the United States and Canada.

As part of New Flyer's growth in the United States market, in 1990 a final assembly plant was established in Grand Forks, North Dakota to complete bus shells manufactured in Winnipeg. In 1996, final assembly was moved from that facility to the current facility in Crookston, Minnesota. In late 1999,

in response to “Buy-America” legislation and continuing market share growth, New Flyer constructed a third state-of-the-art assembly plant with fully integrated production capabilities in St. Cloud, Minnesota.

With this increase in manufacturing capacity, New Flyer focused on expanding its customer base and successfully grew its market share. However, engineering capacity constraints in a period of rapid expansion, poor supply management and manufacturing and quality control issues led to production bottlenecks and delayed deliveries. This resulted in significant increases in work-in-progress inventory, which in turn created liquidity issues in the form of higher working capital requirements. As a result, in 2001, New Flyer was unable to secure surety bonding facilities, which limited the company’s ability to take new orders. New Flyer temporarily suspended production of new orders and reallocated the workforce to complete its work-in-progress for delivery and final acceptance. In March 2002, a private investor group acquired a controlling interest in New Flyer, allowing the Company to secure new surety bonding facilities and address its production and operational challenges.

In February 2004, New Flyer was acquired by a new private equity ownership group. In August 2005, NFI and NFI ULC completed their initial public offering (the “IPO”). Between July 2007 and June 2010, NFI and NFI ULC completed three additional public IDS offerings.

### **NABI History**

North American Bus Industries’ origins are in bus engineering and manufacturing in Budapest, Hungary—once home of Ikarus Body and Coach Works, then one of the world’s largest manufacturers of full-sized buses. The company was originally incorporated in 1992 in Alabama as American Ikarus, Inc. by an investment fund and was licensed to produce full-size, heavy-duty buses designed by Ikarus in Hungary. Throughout its early years, North American Bus Industries used engineering and manufacturing resources in Hungary, due to its wealth of available technical talent.

In 1996, the company changed its name from American Ikarus, Inc. to North American Bus Industries, Inc. and began an aggressive expansion of its aftermarket parts division, which initially supplied service parts only for the company’s products. In conjunction with this expansion, North American Bus Industries hired several experienced individuals previously employed within the aftermarket parts organization of Flxible Corporation, a large US transit bus manufacturer, which has since discontinued transit bus manufacturing and aftermarket parts operations.

In 2006, an affiliate of Cerberus acquired all of the shares of North American Bus Industries. A few months later, the company acquired Optima Bus Corporation, a Wichita, KS producer of mid-sized buses. In 2007, Optima’s operations in Wichita were moved to the company’s Anniston, Alabama plant and the Wichita plant closed. Prior to New Flyer purchasing North American Bus Industries in 2013, the company completed the move of its shell manufacturing operations from Hungary to Anniston, AL. The discontinued Hungarian operations of North American Bus Industries and substantially all of its related assets and liabilities were retained by Cerberus.

### **Business Strengths**

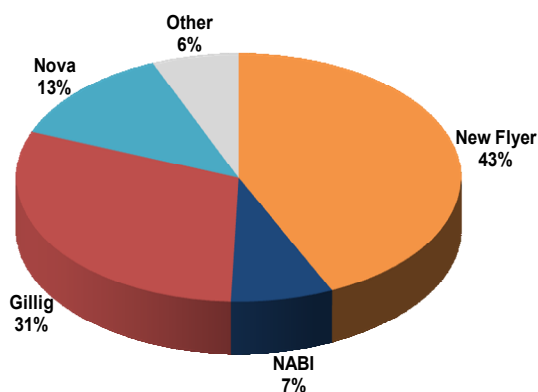
Management believes that the Company possesses the following key business strengths that allow it to maintain its strong competitive position in its industry.

#### ***Leading Market Position***

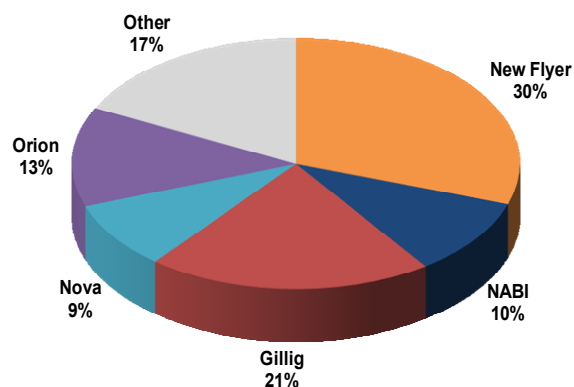
The Company has built its leading market position through its broad product offering, product innovation, extensive in-house engineering capabilities, delivery of buses to specifications, product reliability and aftermarket parts and support capabilities. Management estimates that in 2013, New Flyer

had an approximate 43% market share of the combined United States and Canadian heavy-duty transit bus manufacturing industry based on the number of equivalent unit deliveries in 2013.<sup>1</sup> Although the Company’s market share may fluctuate year-to-year, management believes that since 1999 the Company has consistently maintained the leading market share of the combined United States and Canadian heavy-duty transit bus market. Management estimates there are approximately 24,000 New Flyer buses (of the approximately 34,000 buses New Flyer has delivered) and approximately 8,000 NABI buses (of the approximately 10,000 buses NABI has delivered) currently in service in the United States and Canada. This represents approximately 40% of the estimated 80,000 active heavy-duty transit buses in the United States and Canada.

**2013 Heavy Duty Transit Bus Market Share**



**Active Buses by Manufacturer**



Source: Management estimates.

***Broadest Product Portfolio and Innovation Leader***

The Company has the broadest product and most advanced propulsion systems offering in the industry with the engineering capabilities to meet the diverse needs of its customers. The Company produces heavy-duty transit buses with a range of standard and alternative fuel propulsion systems and is recognized in the industry for product innovation and has consistently been at the forefront of developing and integrating new technologies. Examples of the Company’s product innovation include products such as the low floor bus, which has become the industry standard, on-board electronics, bus styling, hybrid drive systems and articulated buses. The Company’s leadership in innovation is a result of its extensive in-house engineering capabilities that involve many disciplines, such as structural design, powertrain, hydraulic, electrical and HVAC systems. The Company’s breadth of product offering and its demonstrated product development capability allow it to bid on almost any heavy-duty transit bus contract in the United States and Canada.

In October 2008, New Flyer introduced Xcelsior<sup>®</sup>, the customer-centric evolution of its proven standard low-floor transit bus. Its many product improvements make Xcelsior<sup>®</sup>, a “best-in-class” vehicle. From 29 Xcelsior<sup>®</sup> buses delivered in 2010, Xcelsior<sup>®</sup> now represents 100% of New Flyer’s heavy-duty transit bus production. See “Description of the Business – Product Development and Innovation”.

<sup>1</sup> Based on New Flyer deliveries made in 2013, plus NABI deliveries made on or after June 21, 2013. The NABI share indicated in the chart below is based on deliveries made by NABI in 2013 prior to June 21, 2013.

In May, 2012, New Flyer announced a joint venture with Alexander Dennis Limited as part of its strategy to pursue growth and diversification. Alexander Dennis is the United Kingdom's largest manufacturer of single-deck and double-deck transit buses and coaches. The two companies have collaborated to introduce the New Flyer MiDi<sup>®</sup>, a mid-sized low-floor bus that management anticipates will address the demand in North America public and private markets for vehicles having a seven to 12 year operating life. This strategic partnership builds upon New Flyer's North American market leading position, manufacturing expertise and extensive aftermarket support network, with Alexander Dennis bringing demonstrated design expertise of quality mid-sized buses, having delivered over 16,000 of this class of bus to customers throughout the UK, Hong Kong, New Zealand and Australia. Under the arrangements of the joint venture, New Flyer is responsible for sales, marketing, manufacturing and aftermarket support with Alexander Dennis performing design, engineering, test and prototype development activities. Prototypes of the New Flyer MiDi<sup>®</sup> for North America were deployed in 2013 for a market launch and test program. The bus is offered to both public transit and private operators with a clean diesel propulsion system, which the Company plans to expand potentially to electric hybrid and compressed natural gas propulsion systems.

### ***Employee Focused***

In 2013, for the ninth consecutive year in a row, the Company was selected by Mediacorp Canada Inc., as one of Manitoba's Top 25 Employers. This special designation recognizes Manitoba employers who lead their respective industries by offering exceptional places to work. New Flyer's programs and initiatives are key components in making New Flyer a "Great Place to Work". The evaluation process was based on eight key areas: physical workplace; work atmosphere and social activities; health, financial and family benefits; vacation and time off; employee communications; performance management; training and skills development; and community involvement.

In May 2013, New Flyer received the Organizational Development and Strategic Initiative Award from the Human Resource Management Association of Manitoba. This award recognizes organizations that have developed initiatives and programs which have enhanced or changed organization-wide strategic thinking in the field of Human Resources.

### ***High Quality and Diversified Customer Base***

*Established, Long-Term Relationships with Diverse Customer Base.* Twenty-four out of the 25 largest transit authorities in the United States and Canada (based on the number of buses in service in 2013), operate either New Flyer or NABI buses, or both. The Company has active business relationships (which includes the sale of parts) with approximately 270 transit authorities in Canada and the United States. It is estimated by management that these 270 transit authorities operated approximately 75% of the total heavy-duty transit buses in Canada and the United States in 2013. The average tenure of the Company's relationships with its ten largest customers over the last five years is approximately 19 years.

*Repeat Business.* The Company enjoys significant repeat business from its customer base. Over the last five years, approximately 66% of the Company's annual bus manufacturing revenue has been derived from repeat customers that have purchased buses from the Company during each respective prior five-year period.

*No Reliance on Any One Customer.* The Company does not generally depend on the same group of top customers for yearly recurring sales. While the Company's top ten customers in any year have typically accounted for 50% to 70% of its bus manufacturing revenue in that year, the large contract procurements undertaken by many municipal and local transit authorities every few years generally creates a new customer base for the Company each year.

### ***Aftermarket Parts and Support Capability***

Aftermarket parts and support is an important element in the purchase criteria of a transit authority. The Company's leading share of all heavy-duty transit buses currently in service provides recurring demand for and a significant opportunity to grow its aftermarket parts business. The Company provides parts and support for products manufactured by New Flyer, NABI, Orion (after the purchase of the Orion aftermarket parts business in 2013), as well as other manufacturers. The cost of aftermarket support (including warranty and training requirements) is typically included in the customer's bus purchase contract, while parts are sold separately when required after the initial bus purchase. Management believes that the Company provides the most comprehensive aftermarket service and support of all manufacturers in the industry. Aftermarket operations represented approximately 18% of the Company's 2013 revenue and 33% of the Company's 2013 Adjusted EBITDA.

### ***Experienced and Committed Management Team***

The Company's senior management team consists of experienced and committed individuals who have implemented robust processes to manage bidding, contracts management, engineering, strategic sourcing, manufacturing, quality assurance and aftermarket parts and service which have resulted in the Company's growth and profitability. Management brings expertise from a wide range of transportation manufacturing industries including bus, railcar, automotive, military vehicles and aerospace.

The executive leadership team participates in the Issuer's performance unit plan, restricted share unit plan and share option plan, and all of the Company's senior management and sales teams participate in some form of incentive plan. See "Directors, Officers and Management — Long Term Incentive Plans".

### **Corporate Mission Statement and Strategy**

The Company's mission statement is – "To deliver the best bus value and support for life."

The Company's business strategy is as follows:

- to maintain market leadership in the heavy-duty transit bus industry in Canada and the United States and to focus on growth strategies in adjacent markets such as the medium-duty transit and shuttle bus industry.
- have a customer focus on both public transit agencies and private operators, providing lifetime value-added transit vehicle solutions that lower direct operating costs.
- to be both a technology developer and integrator.
- to diversify and grow its product offering, such as the introduction of the MiDi<sup>®</sup>, and to pursue strategic opportunities with other parties where it makes commercial sense; and
- to continue to provide traditional aftermarket services such as parts sales, maintenance information, bus field support, warranty services, and product training services. As part of New Flyer's life cycle product support strategy, the Company has begun to provide vendor-managed parts inventory services and is investigating fleet management services, provision of maintenance programs and developing and delivering product reliability services.

### ***Operational Excellence***

One of the primary operational focuses of the Company is on developing and implementing strategies and tactics to support “Operational Excellence”, one of the Company’s core operating principles. The Company’s vision of “Operational Excellence” is to provide and maintain for all employees a safe, clean and efficient working environment to become the most efficient heavy-duty transit bus manufacturer and achieve the highest level of first-time quality in its products through the implementation of well-defined and robust processes and procedures that are sustainable for future growth. Management believes that Operational Excellence has resulted in a transformation of the Company’s facilities, improved employee safety and morale, a reduction in the cost of manufacturing, improved quality and improved overall customer satisfaction.

In 2013, the Company was selected as the winner of the 2013 Manufacturing Leadership 100 Award in the category of Operational Excellence. The award, sponsored by the Manufacturing Leadership Community, a global business leadership network for the manufacturing industry, annually honours 100 world-class manufacturing companies and individual leaders that are shaping the future of global manufacturing. The Operational Excellence Award recipients have undertaken projects that transform production processes and systems with an eye toward reducing costs and enhancing agility.

### **Products and Services**

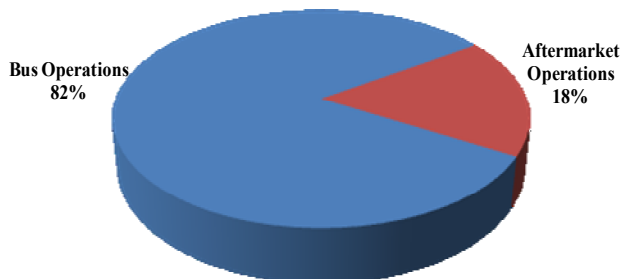
The Company derives its revenue and cash flows from the following two segments:

- *Bus Manufacturing Operations* — design, manufacture and sales of heavy-duty transit buses of various body lengths with diverse propulsion systems. Bus manufacturing operations represented approximately 87%, 86% and 82% of the Company’s total 2011, 2012 and 2013 revenue, respectively.
- *Aftermarket Operations* — support of all post-sale activities, including parts distribution, field services, support documentation and training. Aftermarket operations represented approximately 13%, 14% and 18% of the Company’s total 2011, 2012 and 2013 revenue, respectively.

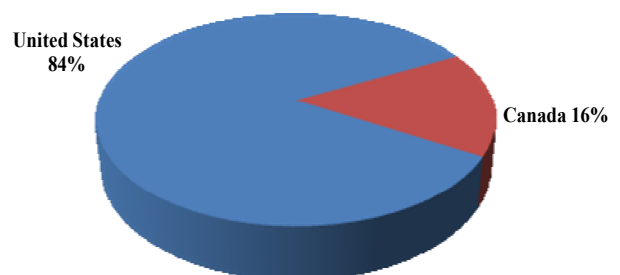
The following chart shows the breakdown of the Company’s 2013 revenue by operating segment and geography:

**2013 Revenue Breakdown**  
(Total Revenue: \$1,199 million)

**2013 Revenue by Operating Segment**



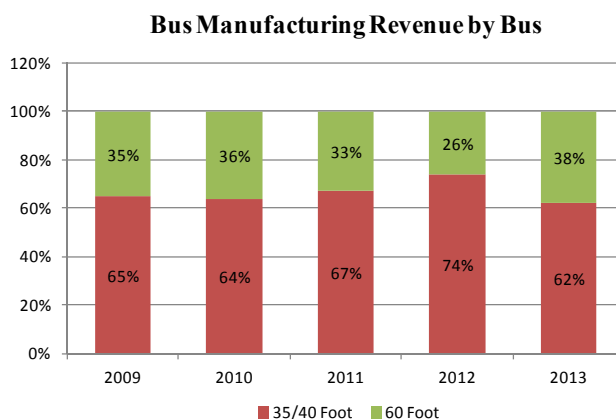
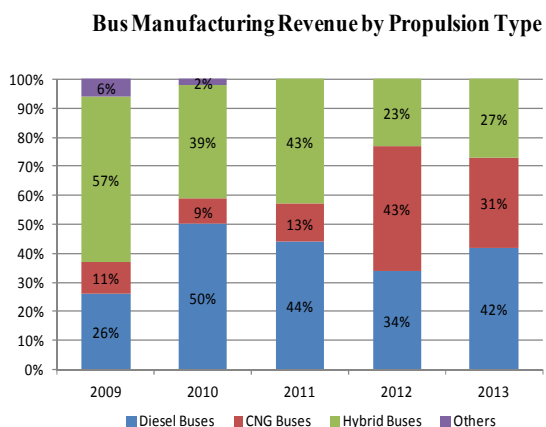
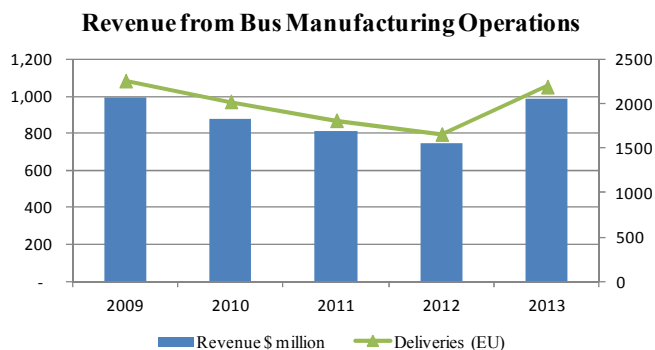
**2013 Revenue by Geography**



## Bus Manufacturing Operations

The Company has the broadest and most advanced product offering in the combined United States and Canadian heavy-duty transit bus industry, giving it an advantage when competing for new customer contracts. The Company's sales, reputation, product range, engineering capabilities and product quality position it as the leading manufacturer in the industry and in specialty areas such as bus rapid transit vehicles, electric trolleys, hydrogen fuel cell and battery-electric propulsion system buses. The Company offers the following bus models, all of which can be modified to meet a wide range of customer specifications:

Model	Lengths	Propulsion System(s)
New Flyer Xcelsior <sup>®</sup> heavy-duty transit bus and BRT	35', 40', 60'	Clean diesel, CNG, diesel-electric hybrid, electric trolley (40' and 60'), hydrogen fuel cell hybrid (40') and battery-electric (40')
NABI LFW heavy-duty transit bus and BRT	30', 35', 40', 60'	Clean diesel, CNG, diesel-electric hybrid
New Flyer MiDi <sup>®</sup> mid-size transit bus	30', 35'	Clean diesel



Heavy-duty transit buses are highly customized to meet specific customer needs and preferences based on geographic and local factors. Each customer contract includes a precise set of technical specifications for the buses being ordered. The Company's sales and engineering departments work

directly with the customer to ensure that all specifications are met and that any changes to the specifications are seamlessly incorporated into the production process.

### **Product Development and Innovation**

The Company continually seeks new solutions to meet the needs of its customers, and many of its product innovations have become the industry standard. The sales group tests design criteria and concepts with select customers to identify products that will be viable in the marketplace. The Company ensures that its engineering capacity is appropriately balanced between new product development and ongoing manufacturing operations.

Once successfully test-marketed with customers, innovation concepts are directed to the Company's New Product Development group ("NPD") for development and prototyping. NPD's primary objectives are to implement product design concepts, fabricate, test and certify engineering prototypes, and develop practical solutions to problems identified by the engineering and marketing departments and customers.

Product innovations introduced into the heavy-duty transit bus market in the United States and Canada by the Company include:

*Low Floor Bus* — Introduced by New Flyer in 1988, low floor buses have become the industry standard in the United States and Canada. Low floor buses permit passengers to board and exit the bus more quickly and allow for improved accessibility, particularly for children and disabled and elderly individuals.

*Programmable Logic Control ("PLC")* — Introduced by New Flyer in 1992, a PLC system is an on-board local network system that controls many of the electrical functions of a transit bus. Since 1993, all of the Company's transit buses have been manufactured with a PLC system.

*Articulated Body* — An articulated bus is an extra-long bus (55-feet to 60-feet in length), composed of two passenger compartments connected by a joint mechanism. The joint mechanism allows the vehicle to bend when the bus turns a corner yet have a continuous interior. New Flyer introduced the articulated 60-foot low floor bus in 1996 and has been the leading manufacturer of articulated low floor buses in the United States and Canada for the last 16 years.

*Hybrid Propulsion Systems* — New Flyer pioneered the integration of hybrid propulsion systems, replacing conventional diesel powerplants with diesel engines coupled with generators. In conjunction with the engine/generator, a roof-mounted battery pack provides the additional power required when a bus is accelerating or climbing grades. Hybrid propulsion systems are now well-accepted in the industry and assist in reducing greenhouse gases and improve fuel efficiency.

*Alternative Fuels* — New Flyer was the first manufacturer to promote natural gas propulsion systems in high floor and low floor body types. Since the products were introduced, approximately 5,000 natural gas buses have been delivered to customers by New Flyer. In 2012 New Flyer launched a CNG articulated bus based on the Xcelsior<sup>®</sup> model.

*Hydrogen Fuel Cell Buses* — New Flyer first began development of hydrogen fuel cell buses in 1993, when it, along with its technology partners, introduced the world's first fuel cell bus. Twenty 40-foot hydrogen fuel cell buses were delivered to BC Transit in 2010 and were showcased at the 2010 Winter Olympics in Whistler, BC. Given the lack of mainstream customer use of this type of technology and no current customer orders for hydrogen fuel cell buses, management has no visibility whether this product will be sold to any customers in the near future.

*Electric Trolleys* — An electric trolley is a bus powered by electricity from overhead wires. New Flyer manufactures both 40-foot and 60-foot (articulated low floor) heavy duty electric trolley buses, with all the standard features of its diesel counterpart, creating an environmentally-friendly zero-emission solution for urban transit operators.

*Bus Rapid Transit* — New Flyer developed and has, since 2006, manufactured new bus rapid transit (“BRT”) vehicles in both 40-foot and 60-foot lengths. NABI also sells BRT style buses in 35-foot, 40-foot and 60-foot lengths. BRT provides efficient intra-city transit using high capacity buses and dedicated lanes. BRT is an option for municipalities seeking an alternative or complement to light rail.

*Xcelsior*<sup>®</sup> — In 2008, New Flyer introduced Xcelsior<sup>®</sup>, the customer-centric evolution of the standard low-floor transit bus. Its many product improvements make Xcelsior<sup>®</sup> a “best-in-class” vehicle. In independent third-party testing at Altoona’s test facility, Xcelsior<sup>®</sup> achieved the highest ever recorded miles per gallon for buses in its class. Upgraded styling, a redesigned bumper and LED headlamps address customers’ expectations for an advanced vehicle design. A single-reduction axle, all wheel disc brakes and improved access to components address maintenance concerns. Accessibility has been greatly improved with a wider door and entry area, a lower front step and an improved ramp angle. The single-reduction axle, along with the rooftop AC and improved insulation reduces interior noise levels. Passengers and drivers can enjoy improved ride quality, better visibility, interior LED lighting and many other interior advancements, including a new dashboard and instrument panel for the operator. From 29 Xcelsior<sup>®</sup> buses delivered in 2010, Xcelsior<sup>®</sup> now represents 100% of New Flyer’s heavy-duty transit bus production.

*New Flyer MiDi*<sup>®</sup> — New Flyer has entered into a joint venture with Alexander Dennis Limited to introduce a versatile 30’ and 35’ mid-size bus. New Flyer is conducting tests on several prototypes and manufacturing has commenced in the Company’s St. Cloud, Minnesota facility.

*Battery Electric Bus* — New Flyer is currently developing a battery-electric bus. The Company is conducting tests on several prototypes and management expects to deliver the first production bus to a customer in 2014.

### **Aftermarket Parts and Support Services**

Aftermarket parts and support have become increasingly important to transit authorities in their purchase decisions. The increasing complexity of the technologies of transit buses, combined with transit authorities’ increasingly constrained operating budgets and high bus utilization levels, have in the past driven demand for aftermarket parts and support. The Company’s leading share of heavy-duty transit buses currently in service provides recurring demand for and a significant opportunity to grow its aftermarket parts and service business. The Company provides parts and support for products manufactured by New Flyer, NABI, Orion (after the purchase of the Orion aftermarket parts business in 2013), as well as other manufacturers. Management believes that the Company provides the most comprehensive aftermarket parts support of all manufacturers in the industry.

Delivering the best bus value and support for life and maximizing the life cycle support opportunities are also key elements of the aftermarket parts and support team’s strategy. This includes providing services in the areas of maintenance material supply chain, special labor services for selected maintenance and repair programs, bus maintenance management support, and the ongoing development of new products and kits in support of the bus maintenance process. New Flyer has also begun providing vendor-managed parts inventory services.

Given the Company's position in the industry, and the current general drive for cost reduction in the areas of bus maintenance, it is well-positioned to maximize the opportunities to provide life cycle support services to the transit industry.

Aftermarket parts and support services consist of the following components:

### ***Parts***

The aftermarket parts team is recognized as a leader in its area, both in size and service quality. It distributes a wide assortment of service parts for a variety of models of heavy-duty transit buses, including buses built by other manufacturers. Competitors in the aftermarket parts business include competing transit bus manufacturers, bus parts distributors and parts divisions of related industries (e.g., heavy-duty trucks). New Flyer, with an estimated market share of 28% in 2013 in the transit parts business, provides the following competitive advantages over its competition: widest original equipment product assortment, most distribution centers in North America and tremendous industry knowledge and the ability to cross reference products to create solutions for customers. New Flyer also distributes its own line of service parts under the New Flyer "Kinetik" brand. The cost of aftermarket support is typically included in the customer's bus purchase contract, while parts are sold separately when required after the initial bus purchase.

Part of the Company's long-term strategy is to have warehousing and distribution capability to provide industry-leading response times to all of the Company's customers in Canada and the United States. This network of strategically located parts distribution centres has significantly improved the response times to the customers and minimizes transportation costs. This industry-leading network also provides a solid logistics infrastructure to facilitate planned growth in the new and additional areas of customer life cycle support.

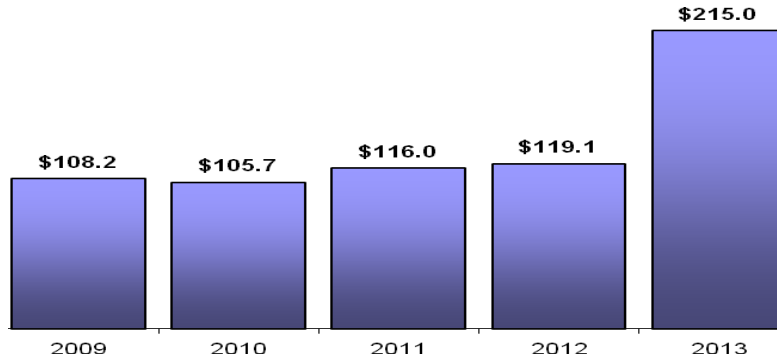
The Company's aftermarket parts and service segment has grown significantly over the last 18 months. This growth has been driven by the acquisition of both the Orion and NABI aftermarket parts business, an increase in bus mid-life overhaul contracts with customers and from organic growth of customer maintenance spending. These factors have led to a significant increase in market share. Management estimates the aggregate industry sales in the heavy-duty transit aftermarket parts sector was approximately \$800 million in 2013 and that New Flyer's market share in 2013 was approximately 28%, an increase from its estimated market share of 18% in 2012.<sup>2</sup>

The following tables show the growth in the Company's revenue generated from aftermarket operations since 2008, and management's estimates as to the market share of New Flyer, NABI and certain of their competitors in the aftermarket parts industry for 2013.

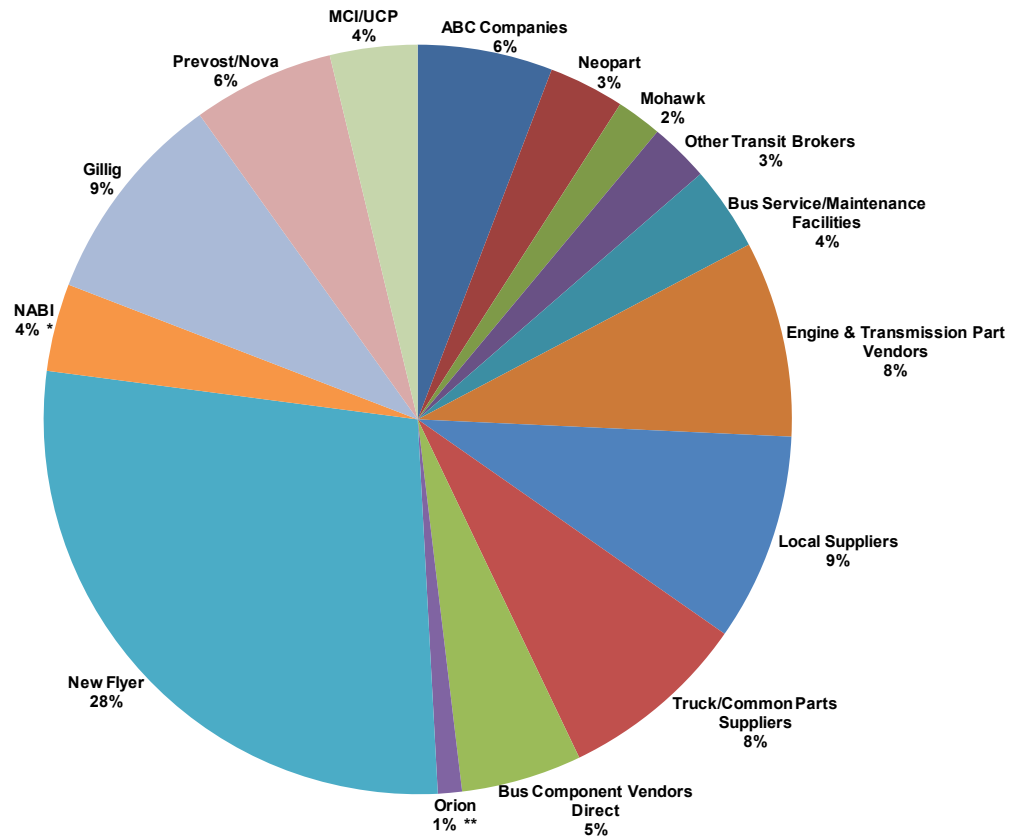
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<sup>2</sup> Based on New Flyer's aftermarket parts sales in 2013, plus Orion's aftermarket parts sales on or after March 1, 2013, plus NABI's aftermarket parts sales on or after June 21, 2013.

**2013 Revenue from Aftermarket Operations**  
*(\$ in millions)*



**2013 Aftermarket Market**



Source: Management estimates regarding the size of the heavy-duty transit aftermarket parts sector and the Company's share is based on publicly available information relating to customers' material and maintenance budgets and management's general industry experience and knowledge.

\* NABI's aftermarket parts sales in 2013 prior to June 21, 2013.

\*\* Orion's aftermarket parts sales in 2013 prior to March 1, 2013.

### ***Publications***

The publications team produces a wide range of parts, maintenance and operational documentation, tailored to the needs of each of the Company's customers. Focusing on content accuracy and user-friendliness, a variety of documents are published in hard copy or electronic format. New Flyer's "Transit Information Viewer", a CD-ROM containing all information unique to each bus purchased by a customer, was introduced in the mid-1990s and is a product feature that has set the standard for customer specifications in the industry.

New Flyer's production of customer-specific maintenance information remains the standard within the industry. New technologies (such as Product Life Cycle Management) are being developed and implemented to provide this information in new formats and through new media that will further benefit and provide the customer with accurate and up-to-date information to maintain the customer's buses throughout their life cycle.

### ***Service Support***

The customer service team is responsible for product acceptance, field support, field engineering and warranty management. Management believes the Company has the highest level of density of service representatives per bus in the field, to help ensure a timely and complete response to each customer request throughout the operating life of a bus.

New Flyer uses iWarranty, a web-based electronic warranty claim, administration and campaign management system. The online system provides many features to the customer to submit, manage and monitor their warranty claims submitted to New Flyer. Since its implementation in 2009, the iWarranty system has improved customer response times and provides New Flyer with greater visibility in the areas of product reliability and safety, warranty campaign planning and management. This system has received tremendous acceptance by New Flyer's customers and virtually all customers with existing base warranties for their buses, are on-line and are actively using the iWarranty system.

New Flyer opened a service centre in Arnprior, Ontario at the beginning of 2010 to provide bus warranty, technical and integrated supply chain services for the buses operated in Southern Ontario and the North-Eastern United States. New Flyer also opened another service centre in the Los Angeles, CA area in the fourth quarter of 2013.

### ***Product Training***

Operator and maintenance training is provided to the Company's customers as part of a transit bus purchase contract or separately as an aftermarket service. The New Flyer Institute, the name given to New Flyer's training and education function provides training to customers and employees. See "Description of the Business – People and Labour Relations – "A Great Place to Work" and New Flyer Institute".

In certain circumstances training will also be subcontracted to third party service providers and managed by the Company. Training aids and tools are specifically developed and provided as required, and refresher courses are provided as part of the overall bus life cycle support strategy.

### ***E-Learning***

The Company, through the New Flyer Institute, offers internet-based training modules, or e-learning, to its customers using a web hosted learning management system ("LMS") that stores and provides courses and maintains the training records of the students. This technology allows students to be trained using consistent course content and delivery methods. In addition, courses are taken on an individual

basis and on a schedule that fits the student's needs. Course offerings can include topics ranging from bus maintenance to driver self defence training. See "Description of the Business – People and Labour Relations – "A Great Place to Work" and New Flyer Institute".

### ***New Flyer Connect™***

The New Flyer Connect™ system is an on-board telematic system that includes a modem, GPS unit and a driver interface. The system permits real-time monitoring of the driver and vehicle performance on an individual bus basis and on a fleet-wide basis. New Flyer Connect™ integrates this data and provides monitoring and prognostic performance information to the customer. This information in turn can be used to improve driver safety, improve driving efficiency, save fuel and predict maintenance events. The New Flyer Connect™ reporting system is web-based, with each on-board system uploading data in real time from the bus to a hosted web-based software platform. The software which houses the data, generates notifications based on exceptions and generates reports that can be accessed through any internet portal.

### ***Xtended Life™ Products***

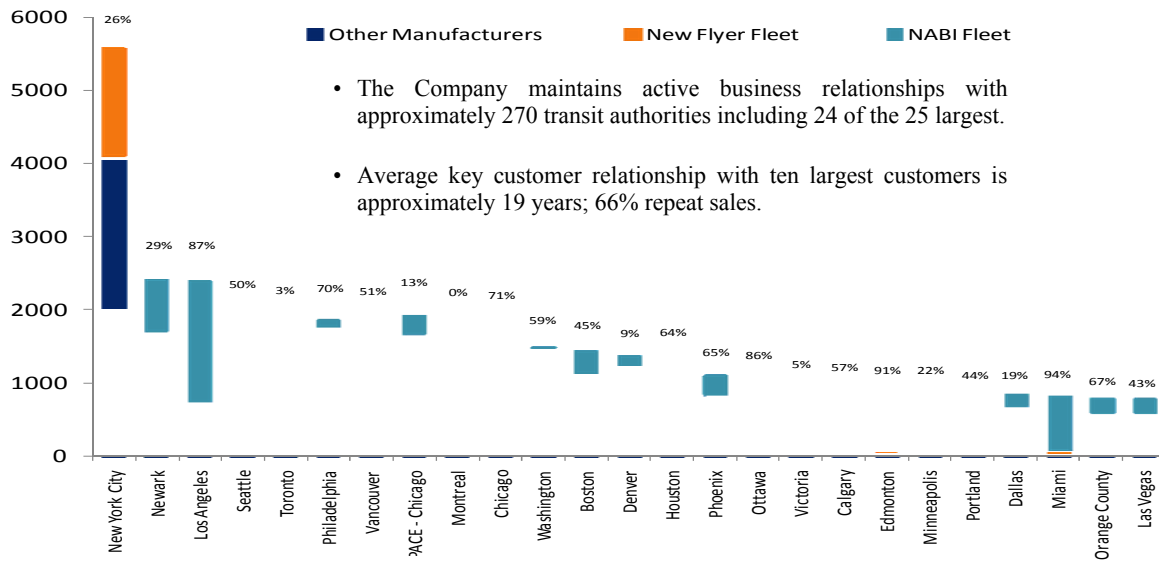
The New Flyer aftermarket parts group introduced a new line of products branded Xtended Life™ in the first quarter of 2013. This line of products consists of products that exceed the normal longevity of the parts they replace on a transit bus. Although selling at a higher price than generic products, the expected benefits to transit customers include the products' longer life, intended to lower actual operating cost per kilometre/mile. The first product introduced under the Xtended Life™ product line is brake maintenance kits. New Flyer has entered into an exclusive world-license with Power Brake, LLC under which New Flyer has the exclusive right to sell brakes and brake components for transit bus applications that have been treated with Power Brake's technology designed to extend brake life and reduce maintenance costs.

## **Customers**

The Company's principal customers are municipal and other local transit authorities in the United States and Canada that provide mass transit to local communities. While the Company's top ten customers typically account for 50% to 70% of its bus manufacturing revenue in a given year, the large contract procurements undertaken by many municipalities every few years generally creates a new customer base for the Company each year. Nonetheless, given the Company's broad and high quality product offering and comprehensive aftermarket parts and service capabilities, the Company enjoys significant repeat business from its customer base. Over the last five years, approximately 66% of the Company's annual bus manufacturing revenue has been derived from repeat customers that have purchased buses from the Company during each respective prior five-year period.

Twenty-four out of the 25 largest transit authorities in the United States and Canada (based on the number of buses in service in 2013), operate New Flyer and NABI buses. The Company has active business relationships (which include the sale of parts) with approximately 270 transit authorities in Canada and the United States. Management estimates that these 270 transit authorities operated approximately 75% of the total heavy-duty transit buses in Canada and the United States in 2013. The average tenure of the Company's relationships with its ten largest customers over the last five years is approximately 19 years. The Company's leading share of all heavy-duty transit buses currently in service gives it an advantage in bidding for new contracts, as operators are increasingly seeking to standardize fleets to minimize the cost of parts and maintenance.

The following chart shows the top 25 transit authorities in the United States and Canada in 2013.



- The Company maintains active business relationships with approximately 270 transit authorities including 24 of the 25 largest.
- Average key customer relationship with ten largest customers is approximately 19 years; 66% repeat sales.

Sources: Metro Magazine, 2013 and management estimates.

Notes: Customers may also operate other manufacturer’s buses in their fleets.

### Forward Visibility of Orders and Backlog

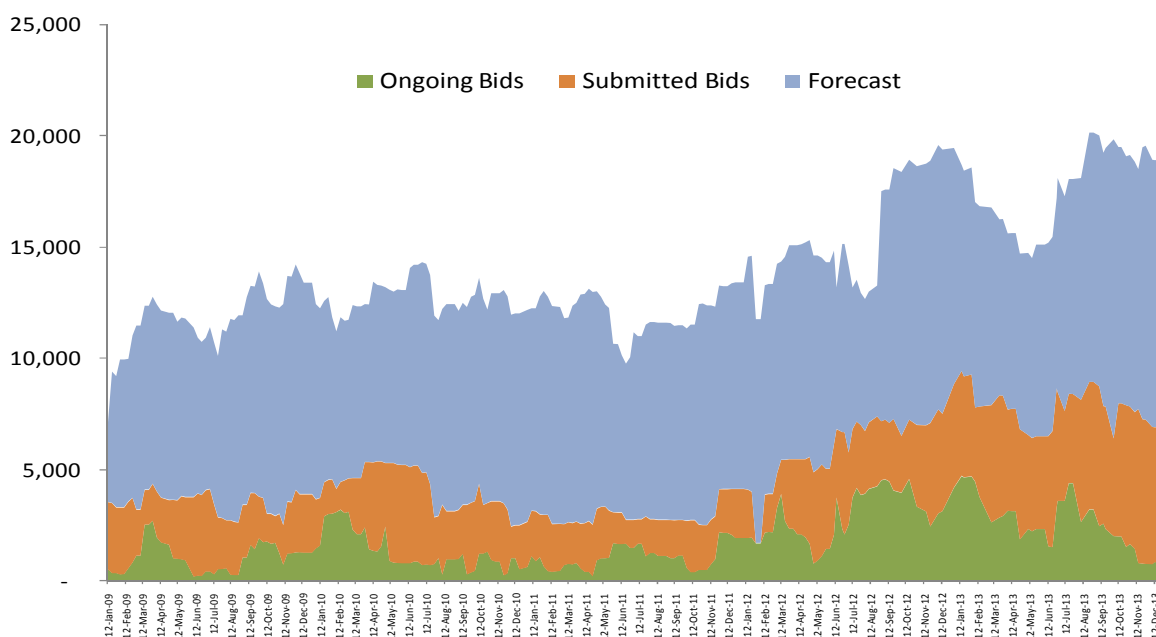
The Company has some forward order visibility due to the fleet planning, budgeting and funding application processes its customers undertake in order to purchase new vehicles. New buses are often ordered three months to one year in advance of delivery, and because the funds for base order bus purchases under procurements are generally approved and allocated at the time the base order is made, cancellations are rare.

Many purchase contracts also include options to purchase additional buses in the future. These purchase options are typically exercisable over a period of three to five years and are often transferable to other transit authorities. In the United States, the options are approved for federal funding at the time that the original contract is signed, and when options are exercised or assigned by one transit agency to another transit agency to exercise there is no need to re-apply for federal funding. In addition, the approved federal funding is generally transferable together with the options to other United States transit authorities, provided that the transferee of the options meets certain federal criteria for funding. Transit authorities are increasingly adding options to their contracts in order to provide flexibility, shorten the buying cycle and reduce administrative costs. The assignment of options is however limited by Federal Transit Administration (“FTA”) rules such that an option is applicable to a specific bus length and fuel type. Minor changes to the bus specification under an option may be made by the assignee agency, but “cardinal” changes are not permitted by the FTA. Given the increasing importance of options to its customer base and the significant source of potential orders that options represent, the Company actively seeks to both grow its option backlog and encourage customers to exercise existing options.

In the last few years, the Company has entered into contracts where the customer is a state or consortium of buyers and the contract is a “standing offer” under which any US transit agency may purchase buses. As these types of contracts are not for a specific stated amount of buses and represent a “standing offer”, the Company does not record any of the buses available under these contracts in its backlog until actual purchase orders are received.

Management tracks the “pipeline” or “bid universe” of anticipated order and production activity within a five-year horizon for the industry. This includes forecasted orders, active bids and active option quotations to be submitted, and pending bid awards and option orders. The pipeline reflects the cumulative anticipated needs of the universe of transit bus customers, rather than funded opportunities. As at December 29, 2013, management estimates there were approximately 18,600 equivalent units in New Flyer’s current pipeline for heavy-duty transit buses. The pipeline is expected to remain volatile as customers manage through fleet replacement planning and deal with funding and budget uncertainties. Management is not able to predict at this stage how many bids will result in awarded orders nor how many options will be exercised to form firm orders.

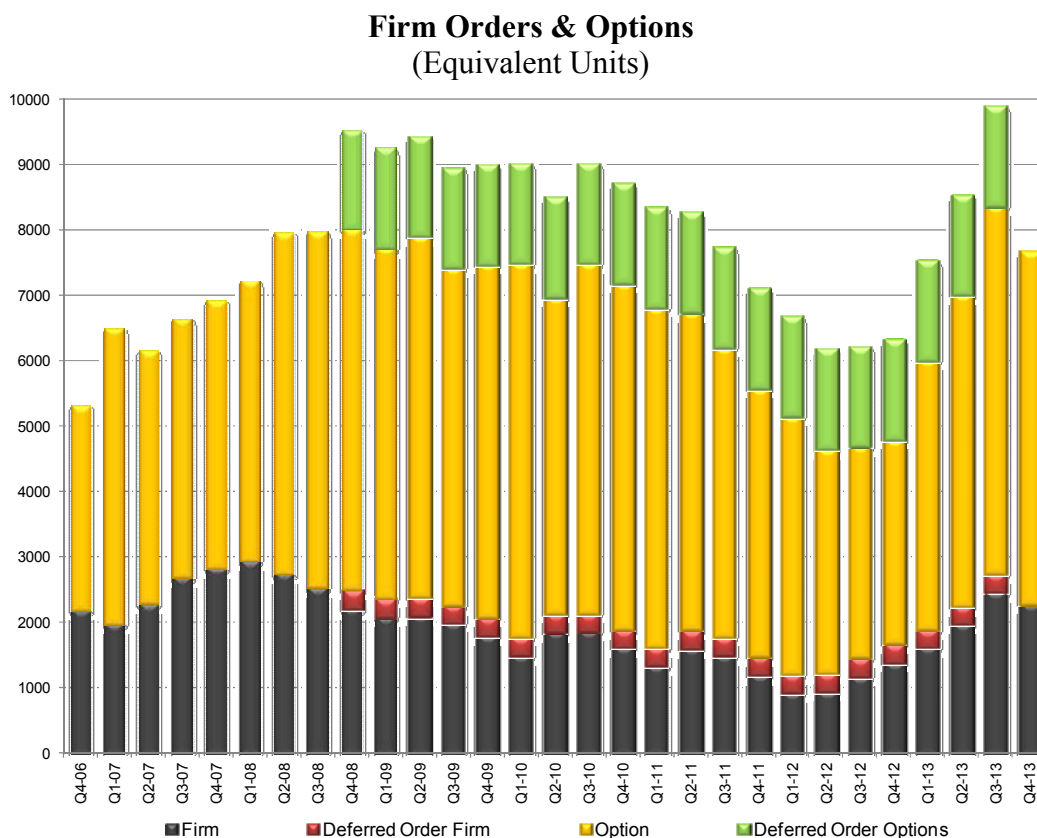
### New Flyer Bid Universe



Source: Management estimates.

As at December 29, 2013, the Company’s total backlog, which includes buses to be manufactured in 2014 and future years, was 7,678 equivalent units (representing approximately \$3.66 billion of revenue, including approximately \$1.1 billion in firm orders and approximately \$2.56 billion in options). Although historically such options have represented a significant source of revenue for the Company, there can be no assurance that customers will continue to exercise or assign these options in the future. Some of the available options are unable to be assigned to third-party agencies because of local procurement rules, and some options are unlikely to ever be exercised because they represent models that are not widely used in the industry. In addition, some agencies secure options based on specific growth and replacement plans which may or may not crystallize. For these reasons, in some cases options are neither exercised nor assigned to third parties, but are simply allowed to expire by the transit agency. Further, given the current economic environment and uncertainty around state and local government funding, management believes that option conversion rates may be lower than in previous years. See also, “Risk Factors — Risks Related to the Business of the Company — Absence of fixed term customer contracts and customer termination for convenience”.

The following chart shows the Company's firm order and option backlog as at the end of each quarter from the fourth quarter of 2006 through 2013.



Source: Management estimates.

At the end of 2013, 1,800 equivalent units were removed from the backlog that related to one US customer order that was added to the backlog in 2008 and deferred by the customer in 2009. Since the deferred order has now reached the five-year maximum contract length with no order activity, the Company has removed all 280 firm equivalent units and options for 1,520 equivalent units from the backlog.

## Sales and Marketing

The Company sells and markets its products primarily through its experienced internal sales force comprised of 14 sales and marketing representatives and ten field sales representatives with geographic coverage responsibilities in the United States and Canada. The Company's executive leadership team is also responsible for developing and maintaining relationships with key contacts at certain of the Company's major customers. The Company has also entered into distribution or dealer agreements with certain parties to sell and support the Xcelsior® and MiDi® to private and certain public customers to whom New Flyer traditionally does not sell buses.

Sales resources are directed on the basis of a customer priority rating determined by a variety of criteria including solicitation type (IFB or RFP), size, multi-year procurement opportunities, aftermarket opportunities and complexity relative to volume.

### ***Customer Identification and Solicitation of Bids***

The Company maintains a database of Canadian and US transit agencies and the approximate age of all of the agencies' buses. This database is used to identify potential customer opportunities. The Company also identifies potential opportunities in each of the following ways:

- (i) Through its sales force and network of industry contacts, the Company works with its customers to understand their capital spending plans. Through these efforts the Company is able to identify municipalities that are planning to upgrade their bus fleets or have vehicles approaching the minimum bus life hurdles (seven to 12 years or 200,000 to 500,000 miles) for United States federal funding of replacements.
- (ii) Ongoing dialogue with existing customers, enhanced by a parts service or support relationship, assists in identifying opportunities for new business. Over each of the last five years, approximately 66% of buses produced by the Company were for customers who had purchased buses from the Company in the preceding five years.
- (iii) The Company also assists customers in having options of other transit agencies assigned to them. Some United States customers seek to add or replace new buses to their fleets without starting a new solicitation process and without applying for United States federal funding (provided that the transferee of the options meets the minimum U.S. federal criteria for funding) and can "piggyback" off an existing customer contract.
- (iv) The Company has the option of selling buses to transit agencies who do not desire to nor have the means to start a solicitation process to sell buses under the "standing offer" contracts it has entered into with certain customers.

### ***Approved Equal Process***

A customer will generally provide a detailed specification of its requirements to New Flyer, NABI Bus and competing manufacturers. The manufacturers will enter into a non-binding negotiation process with the customer known as the "approved equal process". Customer specifications are very detailed and specific, and will include interior and exterior colour schemes, seat selection and electronic components as well as type and length of bus and fuel and propulsion systems required. While customization is present in most buses, not all customer requests can be economically or technically met within the constraints of the core design. Manufacturers will submit an explanation of the differences between the customer's specification and the manufacturer's proposal, detailing the benefits of alternative components offered. Over a four to six-week period, the manufacturers and customer will negotiate adjustments to the specifications and the commercial terms or agree to amendments to or waivers of specific requirements. Both the RFP and IFB solicitation processes described below follow the approved equal process.

### ***Bid Stage and Contract Award***

There are generally two types of solicitation processes that municipalities use to purchase buses. An invitation to bid ("IFB" or "low bid") requires manufacturers to submit a bid and the contract is awarded to the lowest priced bidder who has met the bid specifications. The second type of solicitation is the request for proposal ("RFP" or "negotiated bid") process in which manufacturers submit proposals that address specific criteria for evaluation such as past history, financial capability, quality, reliability, maintenance, aftermarket parts and service and price. Bids are negotiated on the basis of all the relevant criteria, which allows manufacturers to win contracts on factors other than price alone.

During 2011, 2012 and 2013, management estimates that approximately 77% of new bus procurements awarded to the Company were the result of bids awarded through the RFP process. Management believes that the industry as a whole continues to migrate towards the RFP solicitation process, with approximately 80% of procurements being issued through the RFP process in 2013. Management believes that customers have increasingly come to prefer the RFP process because it enables them to factor the lifetime cost of the bus into their purchase decision, taking into account maintenance costs, aftermarket support and warranties and fleet standardization objectives, rather than merely the initial capital purchase cost. While there is a trend among customers to use the RFP process, customers still place a significant emphasis on price.

In preparing its bid, the Company will cost most elements of the product, factoring in component and conversion costs and production slot availability and targeting a minimum dollar contribution to margins. The Company seeks to obtain cost and delivery commitments from suppliers for major components and systems in order to lock in as much of the cost as possible.

### ***Issuance of Purchase Order***

Once a bid has been awarded, there is usually a one to three-month period of documentation negotiation prior to a purchase order being issued by the customer. In the case of most United States customers, a purchase order is issued once all required funding is arranged, a “Buy America” audit is complete and applicable insurance and bonding are in place. See “Legal and Regulatory Matters — Rules of Origin (Buy-America) Legislation”.

### ***Pre-Production***

Once a bus contract is signed, the Company initiates the pre-production process that ideally begins between seven and eight months prior to production of a bus. This period is often compressed as transit agencies continue to face pressures in obtaining funding on time for the production build of their buses. The project is transferred to the customer management department where the contract is assigned to a dedicated customer program manager who is responsible for establishing and managing the project. Over the course of the pre-production period, the Company and the customer review the specifications in the contract to confirm their mutual understanding and expectations. Typically, this process yields changes to the original specifications, which are permitted at the customer’s expense. The contracts also typically permit customers to independently make changes at their own expense. Changes are logged and approved by the customer prior to commencement of production. Any changes, along with the technical summary (which is a running log of the original specifications), will follow the bus order through the production line to ensure strict adherence to the final specifications. The sale process culminates with a final inspection and acceptance by the customer. The customer generally sends a representative to the Company’s facilities to inspect and test the vehicles before taking delivery. Third party drivers then deliver the buses to customers and customers are then given a final opportunity to inspect and accept the vehicle. Payment terms are typically either net 30 days from final acceptance or, in a few situations, progress payments based upon completion of key milestones.

Some contracts have holdbacks (of up to approximately 10% of the total contract price) over a 45 to 60 day (or longer) period following acceptance to ensure that any minor deficiencies are corrected. The Company is also subject to holdback arrangements with some of its customers in lieu of providing warranty bonds. From time to time, customers hold back more than they are entitled to under contract. In such cases, the holdback typically is in the amount of the expected warranty provision, less any extended warranties purchased, for the warranty period. The customer can then charge any warranty claims against the holdback account once such claims are approved by the Company. Any money remaining from the holdback is returned to the Company. Warranty holdback periods generally last for one to two years.

## Facilities and Manufacturing Process

### *Facilities*

The Company's production facilities are well-equipped. Over the last few years the Company's facilities have been significantly upgraded in terms of safety systems, paint, lighting (especially on the production floor) and the removal of waste and scrap. Other significant projects have included a new small parts paint line and the reduction to a single production line at the New Flyer Winnipeg, MB facility, in-sourcing of parts such as weld kits and the installation of a compressed natural gas pumping station at New Flyer's St. Cloud, MN facility and NABI Bus' Anniston, AL facility.

New Flyer's manufacturing facilities in Winnipeg, Manitoba and St. Cloud and Crookston, Minnesota have each been registered to the ISO 9001 (quality), ISO 14001 (environmental) and OHSAS 18001 (safety) certifications.<sup>3</sup> New Flyer has been recognized for outstanding occupational health and safety management.

The following table provides details of the Company's major facilities:

<u>Location</u>	<u>Function</u>	<u>Established</u>	<u>Approximate Size (Sq. ft.)</u>	<u>Ownership</u>	<u>Lease Expiration</u>
<b>Winnipeg, Manitoba</b>					
Manufacturing Facility	administration, sub-assembly, structure weld, shell assembly and paint support services	1973 (expanded 1998)	364,000	Owned	N/A
Distribution Center	aftermarket parts	2013	50,000	Leased	2020
Development Facility	new product development	2013	33,000	Leased	2020
<b>St. Cloud, Minnesota</b>					
Manufacturing Facility	structure weld, shell assembly, paint, final assembly and customer inspection/acceptance	1999	338,000	Leased	2024
<b>Crookston, Minnesota</b>					
Manufacturing Facility	final assembly	1996 (expanded 1998)	89,000	Owned	N/A
Customer Acceptance	customer inspection/acceptance	1998	27,000	Owned	N/A
<b>Anniston, Alabama</b>					
Manufacturing Facility	administration, final assembly, paint, parts fabrications and customer inspection/acceptance	1992	288,000	Owned	N/A
Structure Weld and Assembly Facility	structure weld and shell assembly	2007	150,000	Lease	2017
<b>Hebron, Kentucky</b>					
Distribution Center	parts distribution center	2013	113,000	Leased	2018
<b>Delaware, Ohio</b>					
Distribution Center	parts distribution center	2008	95,000	Leased	2027
<b>Fresno, California</b>					
Distribution Center	parts distribution center	2009	32,000	Leased	2014

<sup>3</sup> ISO 9001 (Quality), ISO 14001 (Environmental) and OHSAS 18001 (Health & Safety) certifications confirm that New Flyer's management system has been assessed by accredited bodies, which found the Quality, Environmental, and Health & Safety components of the system to be in conformance with applicable standards.

<u>Location</u>	<u>Function</u>	<u>Established</u>	<u>Approximate Size (Sq. ft.)</u>	<u>Ownership</u>	<u>Lease Expiration</u>
<b>Brampton, Ontario</b> Distribution Center	parts distribution center	2011	32,000	Leased	2014
<b>Ontario, California</b> Service Center	final assembly, customer acceptance, warranty support and parts distribution	2013	104,000	Leased	2019
<b>Arnprior, Ontario</b> Service Center	warranty support and parts distribution	2010	26,000	Leased	2015
<b>Elkhart, Indiana</b> TCB Enterprises' facilities	parts fabrication	2010	24,000	Leased	2014

### ***Manufacturing Process***

The manufacturing planning process begins at the time of the initial bid, well in advance of actual fabrication or assembly. During this period the supply chain is managed such that when the unit enters the production line, all necessary materials and components are delivered direct to the point of use on the production line to allow for timely installation or assembly. Generally, the Company manufactures its buses, from frame welding to final assembly, in approximately five weeks.

The Winnipeg production facility operates one production line with a number of off-line component and small parts assembly stations and a pre-production fabricating group that creates materials for assembly on the production line. In Winnipeg, a bus goes through the structure weld, shell assembly and painting phases of production. The partially completed shell is then shipped to Crookston for final assembly.

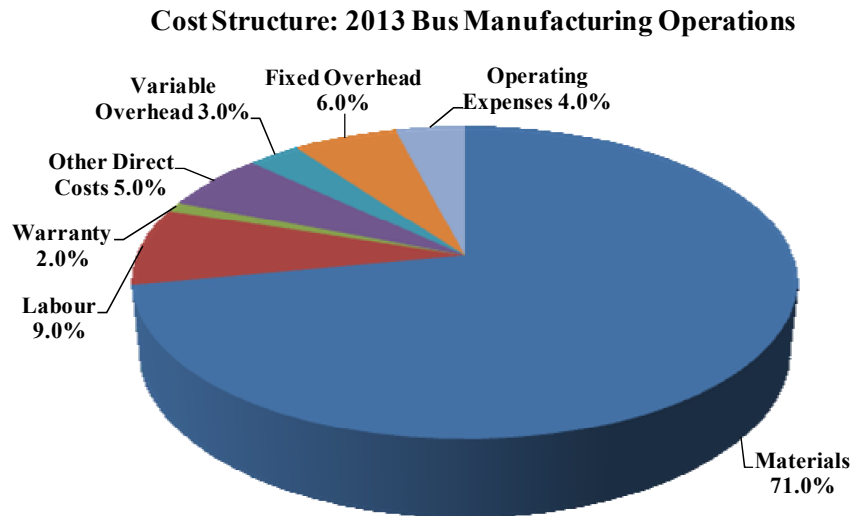
The Crookston production facility is a final assembly plant. Running two identical production lines in parallel, the facility completes the bus shells delivered from the Winnipeg facilities and tests the finished products. In order to facilitate compliance with “Buy America” legislation, New Flyer installs most major components such as the engine, axles, transmission, driver and passenger seating and air conditioning systems at the Crookston facility.

Constructed in 1999, the St. Cloud production facility produces a complete bus from frame welding to final assembly. In 2011, specialized ventilation equipment was installed in the St. Cloud facility in order to build CNG-powered buses to accommodate operational flexibility and to address the increasing demand for CNG buses. St. Cloud, Minnesota will also be the facility from which the MiDi<sup>®</sup> will be manufactured.

The NABI Bus facility in Anniston, Alabama also produces complete buses. Steel tubes are purchased and then cut, welded and formed to build the bus chassis. Assembly operations then complete the buses for customers. In 2007, as an industry first, a robotic paint system was purchased and installed as part of a plant expansion. In 2013, a CNG fuel station was installed and became operational allowing for more efficient production of CNG buses.

The Company currently has a heavy-duty transit bus production capacity of approximately 2,000 to 3,000 equivalent units per year based on both engineering capacity and production capacity. New Flyer generally runs one to two shifts per day, five days a week at each of its three facilities. See “Risk Factors — Risks Related to the Business of the Company — The Company may not be able to successfully renegotiate collective bargaining agreements when they expire and may be adversely affected by labour disruptions and shortages of labour”.

Due to the assembly nature of the Company’s manufacturing process and the high cost of the major components incorporated into buses, approximately 90% of the total cost structure of its bus manufacturing operations is variable, based on the Company’s 2013 financial results. The following chart provides a breakdown of the Company’s cost structure for bus manufacturing operations:



### ***Quality Organization and Principles***

There are approximately 70 employees at New Flyer employed by the Quality Department as inspectors, supervisors, managers and technicians. New Flyer has implemented several quality system improvements over the last five years that are designed to increase the build quality of buses. Quality standards are provided to customers during the pre-production process. This is done to ensure that customers agree with the quality standards under which the bus will be built and inspected at New Flyer’s facilities. New Flyer engages in a modified version of Advanced Product Quality Planning to provide quality and inspection planning prior to the production build. This process seeks to ensure that any quality or design issues identified during previous builds are addressed by design or process improvements. New Flyer utilizes an online manufacturing system (“Live Bus”) and an online quality system (“Live QA”) to record the completion of installations and to identify issues in real time.

New Flyer has also taken measures to standardize tests and inspections conducted on the buses to ensure consistency across New Flyer facilities and personnel. Quality gates have been implemented for purposes of identifying defects on the buses closer to the source. The intent of the quality gate is to provide information back to the work cell in a timely manner to correct the issue and prevent recurrence. The completion of the bus manufacturing culminates in a final inspection of the bus completed by Quality Department personnel prior to the bus being inspected by the customer. In addition to the quality gate inspection and final inspection activities, there are other inspections conducted throughout the process, including, for example, inspection of safety critical installations, oversight of critical torque applications and “virtual quality gate” inspections of major systems on the bus (called such because Live Bus informs the quality team when an installation has been completed and is ready for inspection).

NABI Bus’ approach to quality is three-pronged. First, Quality Alerts raise awareness for small or one-off issues that have appeared in the manufacturing process. Second, Problem Reports are generated for issues that require engineering or any change to processes. Lastly, Corrective Action Requests (“CARs”) are created for any repeat issue or major issue that is discovered. These can be issued

internally or externally. Problem Reports and CARs can only be closed by the individual who opens them to ensure that they are satisfied. As with any manufacturing operation there are natural variations, but these programs and processes serve to improve the long-term quality at NABI Bus.

There is a strong commitment on the part of the Company to provide continuous improvement in meeting customers' expectations. The Company utilizes customer feedback in several facets of the organization to drive systemic quality improvements.

### **Product Warranty and Other Contractual Provisions**

For all United States federally funded contracts, the FTA stipulates certain warranty levels for the bus, structure and major subsystems. Transit agencies will often request additional coverage as part of the initial capital purchase to minimize their operational costs. The Company prices extended warranty costs into its bids. Extended warranties for major subsystems such as engines, transmissions, axles and air conditioning are normally purchased for the customer from the component supplier. For certain other extended warranties, including those covering brake systems, lower level components, fleet defect provisions and engine-related components, the Company is responsible for warranty costs during a warranty period of approximately one to five years, depending on the contract.

Under the fleet defect provisions included in some bus purchase contracts, the Company is required to repair the entire fleet of buses delivered under the contract if the same defect occurs in more than a specified percentage of the fleet (typically 10% to 25%) within the initial twelve-month period following delivery of the bus. The Company also frequently provides a parts supply guarantee in its bus purchase contracts, under which the Company guarantees that bus parts will be available to the customer for a certain period of time, usually 15 years following delivery of the bus. The Company generally provides its customers with a one-year base warranty on the entire bus and a 12-year corrosion warranty on the bus structure. The Company provisions an estimate of these costs into each of its contracts based on the Company's historical experience and technical expectations. For bus purchase contracts entered into over the last five years, the Company's aggregate warranty costs have, on average, not materially varied from the aggregate of the amounts incorporated into the pricing of the applicable contracts and management believes that the Company's current policy for reserving for warranty obligations is appropriate and conforms to the Company's current warranty spending levels. See "Risk Factors — Risks Related to the Business of the Company — The Company may incur material losses and costs as a result of product warranty claims".

New Flyer uses iWarranty, an industry-leading electronic online warranty claim and campaign management system that allows customers to manage and monitor their submitted warranty claims. It also provides New Flyer with greater visibility in the areas of product reliability, safety and warranty campaign management.

While NABI Bus uses a different warranty system, it also collects, analyzes and assesses its warranty data. This data is then used to improve quality through engineering, component selection and manufacturing improvements.

Bus manufacturing contracts typically include liquidated damages provisions, which result in fines on a per bus per day basis when buses are not delivered to the customer by the deadline specified in the contract. The Company actively manages these terms with its customers in the event of specification changes that impact production timing. The Company does not expect to incur material liquidated damages penalties in the normal course of its operations and liquidated damages incurred by the Company in fiscal 2013 were not material. See "Risk Factors — Risks Related to the Business of the Company — Production delays may result in liquidated damages under the Company's contracts with its customers".

In addition, bus purchase contracts in the heavy-duty transit bus industry typically include a right of transit authorities to terminate the contract for convenience. As such, the Company's customers may, with notice, terminate their relationships with the Company during the term of a contract. See "Risk Factors — Risks Related to the Business of the Company — Absence of fixed term customer contracts and customer termination for convenience".

### **Bonding Requirements**

Many municipalities and transit authorities require suppliers to obtain performance bonds from surety companies or letters of credit to protect against non-performance by suppliers. Approximately 28% of the Company's contracts require performance guarantees, with an average guarantee rate of approximately 10% of the value of the contract. Management believes that the Company's current surety capacity is sufficient to meet its surety requirements.

Performance guarantees are generally valid from contract award to completion of the contract. Contract completion is generally defined as customer acceptance of all buses in a given contract and generally excludes warranty obligations. Contracts can stipulate single or multi-year procurements, and performance guarantee requirements are structured accordingly. Where contracts include options to acquire additional buses, performance bonds are issued as the options are exercised.

The surety bonding market does not provide for committed bonding facilities. Surety companies provide limits on the maximum coverage they will provide. Surety companies issue bonds on an as-needed basis and take into account current financial performance and the state of the surety market in making their credit decisions. Management believes the Company currently has sufficient capacity to meet the performance guarantee needs of its business through both its arrangements with its primary surety provider and its letter of credit facility. See "Risk Factors — Risks Related to the Business of the Company — The Company may not be able to maintain performance bonds or letters of credit required by its contracts or obtain performance bonds or letters of credit required for new contracts".

### **Materials and Suppliers for Production**

Materials represented 71% of the cost structure of the Company's bus manufacturing operations in 2013. The Company has long-standing relationships with a diverse group of established suppliers and generally has a number of sources of supply for most of its raw materials and components. For several major bus components however, supply is dependent upon a single supplier in order to meet the unique customer specifications within a contract. In addition, for certain components such as engines, the Company, and the other manufacturers in the heavy-duty transit industry, are dependent on a single source of supply that is certified to industry requirements and standards. The Company has established strategic relationships with its suppliers and actively monitors and manages the risks associated with supply continuity. Management believes the Company can continue to leverage these relationships through its market leadership position. See "Risk Factors — Risks Related to the Business of the Company — Dependence on limited sources of supply".

The Company typically attempts to negotiate fixed price contracts on annual or multi-year basis with most of its suppliers. Additionally, the Company will negotiate fixed prices and contractual requirements for the supply of special customer specified materials and parts at the time of the bid. See "Risk Factors — Risks Related to the Business of the Company — The Company's profitability can be adversely affected by increases in raw material and component costs".

New Flyer has implemented world-class lean processes to plan and deliver material directly to its production lines. Suppliers receive and process orders electronically using an internet web portal utilizing Oracle iSupplier technology. This efficient and effective communication tool permits suppliers to directly

access material requirements, accept and manage purchase orders, process shipments, enter invoices directly, and manage delivery schedules in a real-time system that is available 24 hours a day, 7 days a week. As at the end of 2013, management estimates that 95% of incoming shipments are being managed and processed through iSupplier. New Flyer also maximizes the use of shop floor Kanban and pull systems, utilizes just-in-time delivery on major components, and manages all in-bound logistics from each supplier's dock in order to deliver all material requirements direct to the point of use on the production line, without the need for warehousing. New Flyer closely monitors and reports to suppliers in respect of their monthly performance and distributes supplier performance awards on an annual basis.

## Capital Expenditures

Due to the assembly nature of the Company's manufacturing process, production requires limited specialty tooling, machinery and equipment. As a result, the Company generally has predictable ongoing maintenance capital expenditure requirements related to its assembly operations. Capital expenditure requirements for new tooling, machinery and equipment may fluctuate from period to period depending on the Company's requirements for in-house fabrication and manufacturing of parts instead of outsourcing them from third parties. Management will also consider capital expenditures where there is an opportunity to grow or diversify the business.

The table below shows the amount and components of the Company's capital expenditures since 2009.

	2009	2010	2011	2012	2013
Land and Building	\$1.0	\$0.9	\$1.2	\$0.5	\$2.9
Machinery, Equipment & Tooling	5.9	3.6	4.9	9.8	8.1
Computer, Hardware & Office Equipment	2.2	2.0	1.7	2.5	3.2
Demonstrator Buses	0.7	1.2	0.9	0.0	2.3
Total Capital Expenditures	9.8	7.7	8.7	12.9	16.5
Less Capital Expenditures funded by capital leases and term loan	(4.2)	(0.5)	(5.0)	(8.9)	(2.3)
Cash Capital Expenditures	\$5.6	\$7.2	\$3.7	\$3.9	\$13.8
Comprised of:					
Maintenance Capital Expenditures	\$2.6	\$3.3	\$2.0	\$1.7	\$3.8
Growth Capital Expenditures	3.0	3.9	5.7	2.2	10.0
	\$5.6	\$7.2	\$7.7	\$3.9	\$13.8

With a heavy-duty transit bus production capacity of approximately 2,000 to 3,000 equivalent units per year (based on both engineering capacity and production capacity), compared to 2013 deliveries of 2,191 equivalent units, and with well-equipped facilities, the Company is positioned to expand its current production with limited additional capital expenditure requirements.

In 2013, the Company incurred capital expenditures of \$16.5 million related to investments for new tooling to support expanded product lines, expand investment in its information technology and for facility transformation to support its Operational Excellence initiatives. The Company financed approximately \$2.3 million of these capital expenditures through borrowings and funded the balance of the expenditures from operating cash flows.

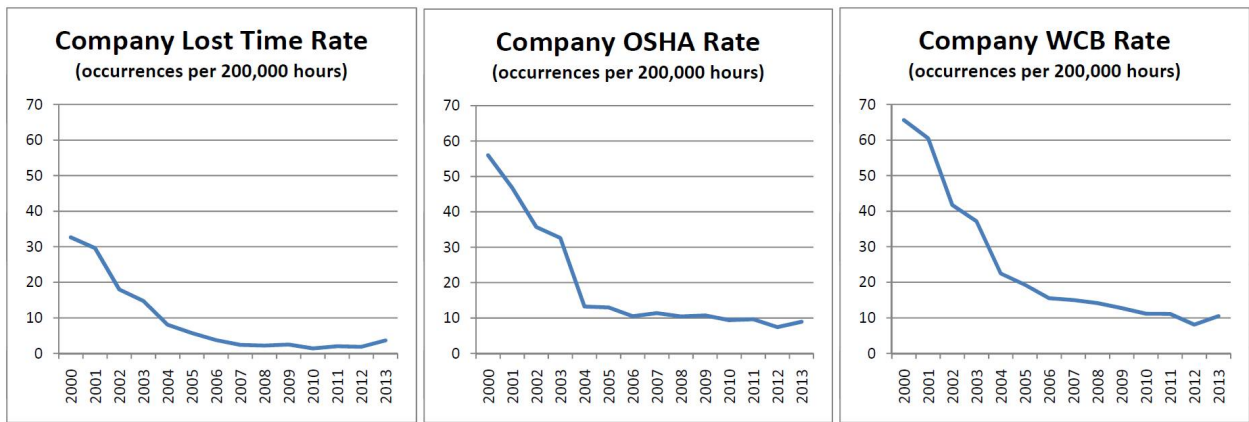
## People and Labour Relations

As at December 29, 2013, the Company had a total of approximately 3,200 employees, of which approximately 2,200 were paid hourly and approximately 1,000 were salaried. Approximately 47% of the Company's employees are represented by unions. The average hourly employee age is approximately 44 years with an average tenure with the Company of approximately eight years.

## ***Occupational Health and Safety Management***

New Flyer’s focus on occupational health and safety management has resulted in strong and continuous improvements over the past decade. Historical occupational health and safety performance (depicted in the charts below) indicates that New Flyer’s lost time numbers and workers’ compensation and occupational health and safety rates have decreased, by 85% since 2000. Management believes that the Company’s dedicated commitment to safety improvements is not only a competitive advantage for the organization, but is essential to the creation of a safe working environment for New Flyer’s employees and its operations. Safety assessments were recently performed at NABI’s facilities. These assessments will provide baseline data and a reference point for the integration of NABI’s safety program into New Flyer’s safety system.

### **New Flyer Safety Trend History**



**Missed time from work:**

*Definition of Lost Time Injuries: The injury caused absence from work. Time spent obtaining medical treatment is not defined as “lost-time.” - OSHA*

**Required modified duties:**

*Definition of OSHA Recordable Accidents: Cannot perform all of his or her normal job duties, defined as any duty he or she would be expected to do throughout the calendar year or cannot work a full shift. - OSHA*

**Went to see a doctor:**

*Definition of WCB Accident: Injuries or illnesses are work related if an event or exposure in the work environment either caused or contributed to the resulting condition or significantly aggravated a pre-existing injury or illness. It must also be something that the worker is not equally exposed to outside the workplace. - OSHA*

Source: New Flyer’s reporting to Occupational Health and Safety Act and Workers’ Compensation Board agencies.

### ***“A Great Place to Work” and New Flyer Institute***

“A Great Place to Work” is one of the Company’s core operating principles, and is an approach that the Company strives to embody in all of its work environments. In order to fully support the Company’s commitment to this strategy, the Company has expanded its corporate training function and has developed a robust training framework that will enable it to meet the needs of all of its employees. This training and education function has been named the “New Flyer Institute”. Access to increased training and skills development, which is strongly aligned with the needs of all employees, is critical to the success of the Company’s customer service, Operational Excellence and supplier-partnership principles. The New Flyer Institute is dedicated to developing partnerships with local, regional and national manufacturing programs as well as working with educational institutions to recognize and give credit for New Flyer certifications. The Company is also focusing on leadership and management development of all of its employees with managerial responsibilities. As the Company expands its capabilities and increases its product and service

offerings to achieve its key strategic objectives, the Company continues to identify, develop and enhance its employees' training and education requirements. Management believes that the New Flyer Institute helps to teach skills to enable and empower employees, and to develop its current and future leaders to differentiate New Flyer and lead it to sustaining a competitive advantage. Since the inception of the New Flyer Institute, all leaders have participated in the Institute's leadership program. The Company has conducted an analysis of technical skill development requirements and as a result, all production employees are currently completing core skill training and certification programs.

### ***iBus and Enhanced Employee Communication***

New Flyer has continued to enhance its innovative employee communication tool called "iBus" and has implemented additional features to improve employee communication. iBus, which stands for "Internal Business User Site", provides employees with one-stop access to essential business links and important Company information. Information kiosks have been installed at all of New Flyer's facilities. Employees are also greeted by the iBus home page every time they open their personal work computer internet browsers or visit one of the shop floor information kiosks. iBus is part of the Company's overall approach to consistent and strong communications which management believes is essential in fostering a culture of teamwork, engagement and positive employee relations.

Launched in 2012 and embedded in iBus is an interactive feedback tool known as Xpressline. This tool provides all employees the opportunity to submit questions or concerns anonymously, and responses are provided by the appropriate leadership employees.

New Flyer has also implemented another innovative communication tool called People TV. People TV was introduced to augment the employee communication framework through the use of creative video presentations, assisting to further align employees with the Company's operating principles, core values and culture. People TV broadcasts important employee information across the organization and continues to be an important employee communication tool.

Key elements of the employee communication framework include regularly scheduled communication from the CEO and executive team to ensure timely and transparent information is available to all New Flyer team members. These sessions include quarterly meetings conducted by the executive leadership team regarding their areas of responsibility, an annual "State of New Flyer" CEO address at all New Flyer locations and quarterly CEO updates posted on iBus and distributed throughout the organization.

### ***Employee Engagement and Culture***

New Flyer has conducted comprehensive employee surveys in order to provide all employees with an opportunity to present feedback on their jobs, work environment and views of the Company. Management believes that this information is essential to improving business performance and is a critical enabler to the "Great Place to Work" strategy. In July 2013 an Employee Survey was conducted to continue efforts in providing employees with an opportunity to provide feedback on their jobs, work environment and views of New Flyer. These results are a means to guide action planning and measure improvements to support our overall business performance. Participation rate increased to 86% from the 2010 Employee Survey participation rate of 84%. The survey results showed a 2% improvement in progress in 12 of the 13 total response groupings from 56% to 58% to our Employee Engagement Index since the last full survey in 2010. A similar survey is planned for NABI in 2014 to guide action planning and establish a baseline for performance improvement and culture alignment on a Company-wide basis.

The Company maintains social committee chapters at all Company's locations to promote and encourage leadership and employee participation in Company-sponsored events and to advance the

development of an inclusive and team-oriented culture. Winter holiday parties are held for all employees at all of New Flyer’s facilities. Management believes this is also fundamental to the “Great Place to Work” strategy and will contribute to the Company’s competitive advantage.

### **Long-Term Collective Bargaining Agreements**

<u>Location</u>	<u>Union</u>	<u>Approximate Number of Unionized Employees</u>	<u>Term of Collective Agreements</u>
Winnipeg.....	UNIFOR - Local 3003, (Production Unit)	740	April 1, 2012 to March 31, 2015
	UNIFOR - Local 3003, (Inspection Unit)	20	April 1, 2012 to March 31, 2015
Crookston.....	Communication Workers of America — AFL-CIO, CLC District 7	250	January 1, 2011 to December 31, 2015
St. Cloud .....	Communication Workers of America — AFL-CIO, CLC District 7	480	April 1, 2013 to March 31, 2017

On September 1, 2013, CAW – Canada and the Communications, Energy and Paperworkers Union of Canada merged and formed a new union called “UNIFOR”.

### **Pensions**

Union employees working at the Winnipeg facility are participants in a defined benefit pension plan. As of December 29, 2013, the estimated plan deficit was approximately \$300,000. Salaried employees at the Winnipeg facility participate in a defined contribution plan in which employees are required to contribute 3% of earnings and New Flyer matches this contribution.

New Flyer employees working at the St. Cloud and Crookston facilities and the NABI employees working at its facilities participate in a tax-qualified defined contribution 401(K) plan to which participants may defer their eligible compensation as employee pre-tax elective deferral contributions and to which the companies may make discretionary matching contributions based upon a percentage of a participant’s pre-tax elective deferral contributions.

### **Competition**

Price, engineering to customer specification, product quality, on-time delivery, established track record, strong customer relationships and financial strength are key factors in winning manufacturing contracts in the heavy-duty transit bus industry. The competitive landscape of the industry in the United States and Canada is now limited to three major competitors: New Flyer, Gillig Corporation, and NOVA Bus Inc. On June 21, 2013, New Flyer acquired NABI from an affiliate of Cerberus. Gillig Corporation is privately owned and Nova Bus Inc. has been owned by Volvo Bus Corporation since 2004. Orion buses, owned by DBNA, was a heavy-duty transit bus manufacturer in the industry until DBNA announced in 2012 that it was exiting the market. It has since completed all of its obligations to finish production on contracts and is no longer building buses. DBNA assigned two of its bus contracts with large US transit agencies to New Flyer. New Flyer purchased the Orion parts business from DBNA in March 2013. See “General Development of the Business — Recent Developments — Fiscal 2013”.

As US federal funding and state tax collections have recovered from the recent recession, the industry has seen an increase in the demand for replacement buses. As a result of these events, management estimates new awards (including options) from transit agencies in 2013 continued at a higher level to that of 2012, in the range of 60% higher than 2012 levels. Management notes that competition for orders among the major bus manufacturers continues to be intense with aggressive pricing in response to public tenders as all manufacturers strive to build their backlogs.

DesignLine, a recent entrant into the heavy-duty transit bus market, entered bankruptcy in 2013. The company, which offers its buses with all electric, diesel, CNG and hybrid propulsion systems, was renamed Environmental Performance Vehicles after its assets were purchased from bankruptcy by Wonderland Investment Group. The company also offers a 40' and 45' suburban coach model with diesel and CNG propulsion systems.

Another recent entrant to the United States heavy-duty transit bus industry is Proterra, formerly Mobile Energy Solutions. Proterra's new manufacturing facility is located in South Carolina. Proterra builds 35' zero-emission heavy-duty vehicle systems and transit buses (including hydrogen-electric buses), and has introduced an all-electric bus with a roof-top charging station. Proterra has sold buses to a few US transit agencies, including The Transit Authority of River City (TARC) in Kentucky.

Chinese bus manufacturers have also shown an interest in the industry. BYD Company Limited, a Chinese company in which MidAmerican Energy Holdings Company, a subsidiary of Berkshire Hathway Inc., has invested, opened an office in Los Angeles and is participating in US industry trade shows and conducting demonstrations of its bus. BYD has opened a new electric bus manufacturing plant in California, and is testing a vehicle at Altoona. BYD has successfully bid electric bus procurements in California.

There are barriers to new entrants, including the need for an established industry track record, a limited number of major customers, the need for significant capital investment and financial stability, the requirement for a sophisticated supply network (which, in the United States includes disadvantaged business enterprises), the requirement for a service and aftermarket parts support structure, United States Buy-America legislation, Ontario and Quebec policies regarding Canadian content and environmental, disability access and other regulatory requirements.

New Flyer differs from its competitors by having the broadest and most diverse product offering in the industry, a strong reputation for quality and innovation and the largest production capacity and by being a leading provider of aftermarket parts and support. As a result, management believes that New Flyer is well positioned to continue to compete successfully and maintain its leading market share in the industry.

## **Legal and Regulatory Matters**

In the United States and Canada, government regulation has had a significant impact upon the heavy-duty transit bus manufacturing industry. These legislative and regulatory requirements continue to affect the structure of the industry, the location of manufacturing facilities, the sourcing of parts and materials and the source of funding for bus purchases. Regulation represents a barrier to entry in the industry. A description of each of the major areas of regulation follows.

### ***Funding for New Bus Purchases***

Public transit infrastructure is considered an "essential service" by and is a key priority of governments and public authorities due to the significant population base that is highly dependent on public transportation and the importance of reducing inner city and suburban traffic congestion.

#### *United States*

The United States federal government has provided funding for the purchase of new heavy-duty transit buses since 1964. Purchases are now largely funded through the FTA funding allocations derived from gasoline taxes. Under these programs, municipal and local transit authorities in the United States receive up to 80% of the funding for new bus purchases from the federal government for (i) the

replacement of buses that have operated for the FTA minimum service life, and (ii) new buses to support fleet growth based on population and ridership trends. In order to receive federal funding for new bus purchases, a minimum 20% contribution commitment from local transit authorities must be in place and the new bus purchase must comply with “Buy-America” legislation. See — “Rules of Origin (Buy-America) Legislation”.

Federal funding for public transit in the United States is provided under surface transportation legislation covering highway, rail and marine transport. On October 1, 2012, a two-year transportation authorization took effect, entitled “Moving Ahead for Progress in the 21st Century” (“MAP-21”). The law authorizes \$10.6 billion of spending in fiscal year 2013 and \$10.7 billion in fiscal year 2014 for public transportation. Primary changes with this funding legislation include the establishment a new needs-based formula program and new asset management requirements. In addition, it establishes performance-based planning requirements for transit agencies that align federal funding with key goals and tracks progress of each grantee towards these goals.

On March 4, 2014, the U.S. Budget proposal for 2015 fiscal year was released. The centerpiece of the transportation budget is a four-year, \$302 billion surface transportation authorization proposal that provides \$72.3 billion for public transportation over that period and \$17.6 billion in 2015 fiscal year. The \$17.6 billion figure includes almost \$14.0 billion for transit formula grants, and \$2.5 billion for capital investment grants.

The U.S. Senate Banking, Housing and Urban Affairs Committee, the U.S. Senate Environment and Public Works Committee, and the U.S. House of Representatives Transportation and Infrastructure Committee are working toward drafting bills for reauthorization and hope to pass them prior to the expiration of MAP-21 on September 30, 2014. U.S. mid-term elections are in November 2014 and there is no certainty that a reauthorization bill will be passed. Without a new bill, an extension of MAP-21 will be required. Although management expects that an extension would be passed if a reauthorization bill is not passed, there is no assurance that this will happen.

Operating funds for U.S. transit agencies have also been stressed over the past five years and have resulted in many transit agencies reducing service, increasing fares, and laying off employees. Others are attempting to off-set budget shortfalls with new revenue streams such as the sale of naming rights for stations and routes, advertising on transit system websites and advertising on buses. While state and local budgets remain challenged, there have been some positive signs recently. According to the Nelson Rockefeller Institute, preliminary data indicates that state tax collections for the third quarter of 2013 increased 6.1% over the previous year. State tax collections include personal income tax and sales tax, both of which have increased for 15 quarters, and corporate income taxes have increased for the past five quarters. Overall state tax revenues have recovered to pre-recession levels. Although these budgets are driven by tax revenue, there is a lag before any improved economic activity translates into new bus orders. See “Risk Factors — Risks Related to the Business of the Company — Funding may not continue to be available to the Company’s customers at current levels or at all”.

These state, county, and municipal taxes also comprise the principal source of the “local match” funding required for agencies to qualify for the FTA capital grants discussed previously. In most cases, the FTA provides 80% of the capital cost of buses, and the local municipality must provide the remaining 20%. In the wake of the recent recession, municipal budgets have been under extreme pressure and the ability of many transit agencies to provide the local match funding has been greatly compromised. This has been further aggravated in some cases by cost-saving initiatives to cut back on transit routes and/or service hours, which in some cases has cascaded to the idling of buses and the consequent deferral of their replacement.

APTA reports that the average fleet age in the US has decreased from 8.0 years in 2011 to 7.8 years in 2013. Management believes that other than fleet age statistics, there is no high-level indicator of the health of funding for transit bus purchases.

### *Canada*

Historically, purchases of new transit buses in Canada have been funded primarily by provincial and municipal governments. Unlike the US, in Canada there is no central source of funding for bus procurements. Instead, funding of bus purchases comes from a patchwork of provincial funding, municipal funding, fare box revenue, various federal programs, and other smaller sources. Across Canada the funding approach varies widely from province to province and even from city to city within a single province.

Recognizing however, the infrastructure deficit in Canadian cities and the role transit can play to fight climate change, reduce congestion and increase quality of life, since 2003, successive federal governments have funded transit capital projects. Some cost share funding for public transit projects and new bus purchases has been provided since 2003 by other federal programs such as the Canadian Strategic Infrastructure Fund and the Infrastructure Canada Program. The Canadian federal government announced in the 2008 budget that the federal Gas Tax Fund became permanent. This fund provided approximately C\$2.0 billion per year from 2009 through 2014 to help municipalities improve their infrastructure. In February 2014, the Canadian federal government announced the C\$53 billion New Building Canada Plan for provincial, territorial and municipal infrastructure which also continues the approximate C\$2.0 billion annual federal Gas Tax Fund until 2019. While the overall federal contribution to infrastructure projects has increased, the eligibility categories have also become broader. Management does not believe this new federal program will significantly increase purchases of buses by transit agencies in Canada.

There continue to be significant lobbying efforts by the industry underway to provide longer-term Canadian federal funding for public transit, including new bus purchases and development of alternative fuel technologies.

The Canadian Urban Transportation Association has reported a decrease in average fleet age from 10.8 years in 2002 to 6.9 years in 2012.<sup>4</sup> Management believes that other than fleet age statistics, there is no high-level indicator of the health of funding for the industry.

### ***Environmental and Emissions Legislation***

The Company is subject to numerous environmental and health and safety laws, including statutes, regulations, bylaws and legal requirements contained in approvals or that arise under common law. These laws relate to the generation, use, handling, storage, transportation and disposal of regulated substances, including hazardous substances, dangerous goods and waste, emissions or discharges into soil, water and air, including noise and odours (which could result in remediation obligations), and occupational health and safety matters, including indoor air quality. These legal requirements vary by location and can arise under federal, provincial, state or municipal laws.

The Company believes that it is in substantial compliance with all material environmental and health and safety legal requirements. The Company is not aware of any breach of such requirements or other similar liabilities the resolution of which would have a material adverse effect on the Company and its operations.

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<sup>4</sup> CUTA, Canadian Transit Fact Book, 2012

The Environmental Protection Agency (the “EPA”) mandates compliance with United States emissions standards for vehicles and Environment Canada mandates such compliance in Canada. The United States EPA mandated additional stringent emission standards that were phased in for 2013. To the knowledge of management, only one engine manufacturer sells diesel engines that comply with these new emissions requirements for use in heavy-duty transit buses in North America.

Effective January 1, 2014, the California Air Resources Board (“ARB”) requires a dual certification for emission compliance for engines used in a hybrid configuration. This requires separate certifications from the engine supplier as well as the hybrid system supplier, but not the transit bus manufacturer such as New Flyer or NABI Bus. There is currently no indication when or if the hybrid system suppliers will be able to achieve this certification. As a result, transit bus manufacturers are currently not able to supply buses in California or in Pennsylvania (one of the states that follow the ARB regulations) with a diesel - hybrid electric engine configuration. All other states that follow ARB regulations have provided an exemption from these regulations for urban transit buses. Unless this certification requirement is waived or until it can be achieved by the suppliers, transit agencies in these three states will need to purchase or convert options to diesel or CNG powered buses. The current impact to New Flyer’s planned production in 2014 is not material. The EPA does not require this dual certification and therefore, these regulations only affect buses purchased by transit agencies in states that follow ARB regulations. See “Risk Factors — Risks Related to the Business of the Company — Dependence on supply of engines that comply with emission regulations”.

#### ***Rules of Origin (Buy America) Legislation***

Introduced in the 1980s, Buy America regulations require that buses meet the following fundamental requirements to be eligible for United States FTA funding: (i) final bus assembly/manufacture must occur within the United States, and (ii) the bus must contain a minimum 60% United States content by cost. The Company is compliant with Buy America requirements and customers regularly conduct audits to validate such compliance for buses purchased with federal funds. To date, the Company has never failed a Buy America compliance audit.

In early 2011, a bill was introduced in the United States House of Representatives to require that buses purchased with federal funds contain a minimum of 80% United States content by cost for 2012, with United States content increasing to 100% in 2013 and future years. This bill was not enacted. In early 2012 an amendment to a pending transportation reauthorization bill that would increase United States content requirements for heavy-duty transit buses from 60 to 100% over a five-year period was also unsuccessfully proposed. The same or similar attempts to amend the transportation reauthorization bill may be renewed. See “Risk Factors — Risks Related to the Business of the Company — Current requirements under ‘Buy America’ legislation may change and/or become more onerous or suppliers’ ‘Buy America’ content may change”.

#### ***United States Content Bidding Preference***

Legislation passed in the State of California in 2011 permits agencies in the State to grant bidding preference to a bidder based on the amount by which the buses it is proposing exceed the minimum US content requirements under the United States federal “Buy America” regulations. As there has been no contract yet awarded under this new legislation, management does not know what impact this legislation will have on the Company’s ability to win procurements by California agencies employing such bid preference rules. There is no publicly available data regarding the US content of competitor’s buses compared to buses sold by the Company. See “Risk Factors — Risks Related to the Business of the Company — United States content bidding preference rules may create a competitive disadvantage”.

### ***Policies Regarding Canadian Content***

The Ontario provincial government has implemented a policy requiring that all transit vehicles procured by Ontario municipalities using sources of provincial funding must contain a minimum 25% Canadian content by cost. A recent solicitation originating from a large Quebec transit agency also had a Canadian content requirement. Management believes that the Company complies with these policies requirements. See “Risk Factors — Risks Related to the Business of the Company — Current requirements under the Ontario government’s or Canadian transit agencies’ Canadian content policy may change and become more onerous”.

### ***Policy of the Toronto Transit Commission***

The Toronto Transit Commission (the “TTC”) passed a policy in 2009 requiring that 50% of the assembly labour costs for new public transit buses purchased by the TTC comprise Canadian labour. In addition, the TTC policy requires that a new forty-foot standard diesel bus contain a minimum of 40% Canadian content by cost. Although New Flyer is not currently building buses for the TTC and has no contract to build buses for the TTC in the future, management believes that the Company would comply with these policy requirements.

### ***Disadvantaged Business Enterprises***

In accordance with United States Department of Transportation regulations, “Participation by Disadvantaged Business Enterprises in Department of Transportation Financial Assistance Programs”, the FTA reviews and approves bus manufacturers’ annual goals for supporting qualified disadvantaged business enterprises (as defined in the regulations). Compliance by manufacturers with these disadvantaged business enterprises regulations is required in order to be eligible to build buses for transit agencies that use FTA funding. The Company’s annual goals for previous years in respect of disadvantaged business enterprises have been approved by the FTA and the FTA has approved the Company’s goals for 2014.

### ***Motor Vehicle Safety Standards***

All buses sold in the United States and Canada must comply with federal, state and provincial motor vehicle safety standards. In both the United States and Canada, vehicles that meet or exceed all federally mandated safety standards are certified under the federal regulations. Rigorous testing and the use of approved materials and equipment are among the requirements for achieving federal certification. The Company’s entire product offering has been certified under applicable federal standards in both the United States and Canada and the Company certifies each new bus model before its market launch. The Company agrees to comply with state and provincial motor vehicle safety regulations in its customer contracts. Management believes that the Company is in material compliance with all current federal, state and provincial motor vehicle safety regulations. The Company is currently not aware of any limitations as to where its buses can operate in the United States and Canada.

### ***Motor Vehicle Road Use Standards***

Transit bus operators are subject to federal, state and/or provincial motor vehicle road use regulations. Although it is the responsibility of the transit bus operator to comply with such regulations, the Company is required to comply with applicable federal, provincial and state regulatory requirements under its customer contracts. The Company must also comply with regulatory requirements whenever it drives its buses over the roadways from its facilities to its customers. Management believes that the Company’s buses are in material compliance with such motor vehicle regulations. However, there are some heavy-duty transit buses in the industry, including certain types of buses manufactured by New Flyer and NABI

that do not currently comply with regulations governing maximum axle weight or length in certain jurisdictions. To date, only a few of New Flyer's customers have required that the Company reconfigure its buses to comply with local axle weight regulations. Transit bus operators often obtain waivers from the province or state in which they operate for vehicles that do not comply with the applicable requirements. However, such waivers are discretionary and as such, there is no assurance that transit operators will continue to be able to obtain them in the future. For example, such waivers have not yet been issued in the province of Ontario. Management believes that this is an industry-wide problem related, in part, to industry trends including evolving environmental, disabled-access and other regulations which have resulted in the production of heavier or longer transit buses throughout the industry. Management believes that many of the provincial and U.S. federal and state axle weight or length regulations have not yet caught up with the other aspects of the overall regulatory regime applicable to transit buses and that such regulations need to be re-examined in light of developments in the industry. Management intends to address provincial and U.S. federal and state axle weight or length restrictions with its customers on a contract-by-contract basis, and expects that the industry and transit operators will lobby the government for changes to these regulations. See "Risk Factors — Risks Related to the Business of the Company — The Company may incur costs in connection with provincial, state or federal regulations relating to axle weight restrictions and bus lengths".

### ***United States Bus Testing***

All applicants for United States federal funding must certify to the FTA that any heavy-duty bus acquired with such funding has been tested in accordance with an endurance test conducted in Altoona, Pennsylvania to simulate 500,000 miles or 12 years of operation. The following tests are conducted at Altoona: safety, structural integrity and durability, reliability, performance, maintainability, noise and fuel economy. The Company's entire product offering has been tested in Altoona, and additional testing occurs regularly with the introduction of new products, or in the case of substantial changes to existing products. The Company is testing the MiDi<sup>®</sup> to simulate 500,000 miles or 12 years of operation.

MAP-21 included major changes to the bus testing requirements performed at the center in Altoona. The current tests are an accelerated whole-bus aging test run on the track, including recording fuel mileage and any minor or major structural and component failures as well as noting the vehicle weight and other physical features. The current test publishes results in a report for every new bus model or major modification. It does not say a bus "passed" or "failed" an Altoona test because it currently is not a pass/fail test. The new law changes will require a pass/fail method and mandates the FTA to develop, with industry input, a revised testing protocol. There is no time established when a new protocol is to be implemented.

Certain major cities in Canada and the United States require a 500,000 mile/12-year shaker table test. This static test simulates revenue service life under challenging conditions to test durability.

### ***Disability Access Legislation***

The Americans with Disabilities Act (the "ADA") prescribes certain minimum accessibility standards for vehicles that are purchased with United States federal funding. All of the Company's buses have been designed and/or tested to be compliant with the ADA. Although there is currently no equivalent federal legislation in Canada, most heavy-duty transit buses in Canada are also manufactured to provide access to persons with disabilities.

### ***Litigation***

The Company is subject to litigation from time to time in the ordinary course of its business. The Company is not aware of any pending or threatened litigation that would have a material adverse effect on the Company and its operations.

## **DESCRIPTION OF CAPITAL STRUCTURE**

### **Share Capital**

The authorized share capital of NFI consists of an unlimited number of Shares. As at December 29, 2013, 55,466,904 Shares were issued and outstanding.

Holders of Shares are entitled to receive dividends as and when declared by the Board and are entitled to one vote per Share on all matters to be voted on at all meetings of shareholders. Upon the voluntary or involuntary liquidation, dissolution or winding-up of NFI, the holders of Shares are entitled to share ratably in the remaining assets available for distribution, after payment of liabilities.

### **Shareholder Rights Plan**

On August 29, 2011, NFI adopted the SRP which was ratified by the shareholders of NFI at the Special Meeting held on September 30, 2011. In connection with the implementation of the SRP, the Board authorized the issuance of one right in respect of each Share outstanding at the close of business on August 29, 2011 and one right in respect of each Share issued thereafter. The rights will separate from the Shares to which they are attached and will become exercisable upon the occurrence of certain events in accordance with the terms of the SRP. Generally, the SRP provides that if a person, or a group acting jointly or in concert, acquires (other than pursuant to an exemption available under the SRP) beneficial ownership of 20% or more of the Shares (except, among other exceptions, pursuant to a permitted bid under the SRP), the rights will separate from the Shares and permit holders of rights (other than the acquiring person) to purchase Shares at a substantial discount to market price. At any time prior to the rights becoming exercisable, the Board may waive the operation of the SRP with respect to certain events before they occur. A copy of the SRP is available on SEDAR at [www.sedar.com](http://www.sedar.com).

### **Description of Debentures**

#### ***General***

As at December 29, 2013, US\$65,000,000 aggregate principal amount of Debentures were issued and outstanding. The Debentures were issued under a trust indenture dated June 5, 2012 (the "Indenture") between NFI and Computershare Trust Company of Canada, as trustee (the "Trustee"). The following summary of certain provisions of the Indenture is subject to, and is qualified in its entirety by reference to all the provisions of the Indenture. A copy of the Indenture is available on SEDAR at [www.sedar.com](http://www.sedar.com).

#### ***Interest Rate***

The Debentures bear interest at a rate of 6.25% per annum.

#### ***Maturity Date***

The Debentures will mature on June 30, 2017.

### ***Conversion Privilege***

The Debentures are convertible at the holder's option into Shares at any time prior to the close of business on the earliest of (i) the business day immediately preceding the maturity date; (ii) if called for redemption, the business day immediately preceding the date specified by NFI for redemption of the Debentures; or (iii) if called for repurchase pursuant to a Change of Control (described below), the business day immediately preceding the payment date, at the conversion price of US\$10.00 per Share. Holders converting their Debentures will receive all accrued and unpaid interest to, but excluding, the date of conversion.

### ***Principal Repayment***

On maturity, NFI will repay the indebtedness represented by the Debentures by paying the Trustee, on behalf of the holders, an amount equal to the principal amount of the outstanding Debentures, together with accrued and unpaid interest.

### ***Optional Redemption***

The Debentures are not redeemable by NFI before June 30, 2015, except in the event of the satisfaction of certain conditions after a Change of Control has occurred as described below. On and after June 30, 2015 and prior to the maturity date, NFI may redeem the Debentures, in whole or in part from time to time, at its option on not more than 60 days' and not less than 30 days' prior written notice at a price equal to the principal amount of the Debentures plus accrued and unpaid interest to, but excluding, the date of redemption, provided that the volume weighted average trading price of the Shares on the TSX for the 20 consecutive trading days preceding the date on which the notice of redemption is given is not less than 125% of the conversion price.

### ***Change of Control***

Within 30 days following the occurrence of a Change of Control, as defined in the Indenture, NFI will be required to make an offer to purchase the Debentures at a price equal to 100% of the principal amount of the Debentures plus all accrued and unpaid interest thereon up to, but excluding, the date of purchase. Holders of Debentures may accept this offer in whole or in part.

If holders of 90% or more in aggregate principal amount of the Debentures outstanding on the date NFI delivers the offer to purchase to the Trustee accept the offer to purchase, NFI will have the right to redeem all the remaining Debentures on such date at the same price. Notice of such redemption must be given to the Trustee within 10 days following the date of purchase, and promptly thereafter, by the Trustee to the holders of the Debentures not tendered pursuant to the offer to purchase.

### ***Cash Change of Control***

Upon the occurrence of Cash Change of Control, as defined in the Indenture, then, during the period beginning 10 trading days before the anticipated date on which the Cash Change of Control becomes effective and ending 30 days after NFI delivers notice to the Trustee of the occurrence of a Cash Change of Control, holders of Debentures are entitled to convert their Debentures and receive, in addition to the number of Shares they would otherwise be entitled to receive as set forth under "— Conversion Privilege" above, an additional number of Shares per US\$1,000 principal amount of Debentures as set forth under the Indenture.

### ***Interest Payment Election***

Unless an Event of Default, as defined in the Indenture, has occurred and is continuing, NFI may elect to satisfy all or part of its interest obligation on the Debentures, (i) in cash; (ii) by delivering Shares to the Trustee, for sale, to satisfy the interest obligations in accordance with the Indenture in which event, holders of the Debentures will be entitled to receive a cash payment equal to the interest payable from the proceeds of the sale of such Shares; or (iii) any combination of (i) and (ii) above.

### ***Rank and Subordination***

The Debentures are direct, subordinated, unsecured obligations of NFI and are subordinate to all other existing and future senior secured and senior unsecured indebtedness of NFI, including all trade creditors, and rank pari passu to all future subordinated unsecured indebtedness of NFI. The Indenture does not restrict NFI or its subsidiaries from incurring additional indebtedness or from mortgaging, pledging or charging its properties to secure any indebtedness or liabilities.

### **Book-Entry Settlement and Clearance**

#### ***General***

CDS acts as securities depository for the Shares and the Debentures, which are referred to collectively as the “Securities”. The Securities are represented by one or more global certificates (each, a “Global Certificate”). The Global Certificates for the Securities are issued as fully-registered in book-entry only form in the name of CDS or its nominee, CDS & Co.

If an investor intends to purchase Securities, an investor must do so through direct and indirect CDS participants. The participant through which a purchase is made will receive a credit for the applicable number of Securities on CDS’ records. The ownership interest of each actual purchaser of the applicable security, referred to as a “beneficial owner”, is recorded on the participant’s records. Beneficial owners will not receive written confirmation from CDS of their purchases, but beneficial owners are expected to receive written confirmations providing details of the transaction, as well as periodic statements of their holdings, from the CDS participant through which the beneficial owner holds its Securities.

All interests in the Securities are subject to the operations and procedures of CDS. The following is a summary of those operations and is provided by the Issuer solely for convenience. The operations and procedures of each settlement system may be changed at any time. The Issuer is not responsible for those operations and procedures.

To facilitate subsequent transfers, all Securities deposited by direct CDS participants are registered in the name of CDS. The deposit of Securities with CDS and their registration in the name of CDS effect no change in beneficial ownership. CDS has no knowledge of the actual beneficial owners of the Securities. CDS’ records reflect only the identity of the direct CDS participants to whose accounts such Securities are credited, which may or may not be the beneficial owners. The CDS participants remain responsible for keeping account of their holdings on behalf of their customers.

Transfers of beneficial ownership interests in the Securities are effected by entries made on the books of the CDS participants acting on behalf of beneficial owners. Beneficial owners do not receive certificates representing their ownership interests in the applicable Security except in the event that use of the book-entry only system for the Securities is discontinued.

Cross-market transfers between CDS participants, on the one hand, and Depository Trust Company (“DTC”) participants, on the other hand, will be effected within CDS through DTC. To deliver or receive

an interest in Securities held in a DTC account, an investor must send transfer instructions to DTC under the rules and procedures of that system and within the established deadlines of that system. If the transaction meets DTC's settlement requirements, DTC will send instructions to its CDS depository to take action to effect final settlement by delivering or receiving interests in the Securities in CDS and making or receiving payment under normal procedures for same-day funds settlement applicable to CDS. DTC participants may not deliver instructions directly to the CDS depository that is acting for DTC.

Conveyance of notices and other communications by CDS to direct participants, by direct participants to indirect CDS participants, and by CDS participants to beneficial owners are governed by arrangements among them, subject to any statutory or regulatory requirements as may be in effect from time to time.

CDS will not consent or vote with respect to the Securities. Only beneficial owners may consent or vote with respect to any Securities. Under its usual procedures, CDS mails an omnibus proxy to the Issuer as soon as possible after the record date. The omnibus proxy assigns CDS' consent or voting rights to those direct participants to whose accounts the Securities are credited on the record date (identified in a listing attached to the omnibus proxy).

The Issuer and the Trustee make payments on the Shares and the Debentures, as applicable, to CDS. CDS' practice is to credit direct CDS participants' accounts on the payment date in accordance with their respective holdings shown on CDS' records unless CDS has reason to believe that it will not receive payment on the payment date. Payments by CDS participants to beneficial owners are governed by standing instructions and customary practices, as is the case with securities held for the accounts of customers in bearer form or registered in "street name", and are the responsibility of such participant and not of CDS, NFI or the Trustee, subject to any statutory or regulatory requirements as may be in effect from time to time.

The Issuer and the Trustee are responsible for the payment of all amounts to CDS. CDS is responsible for the disbursement of those payments to its participants, and the participants are responsible for disbursements of those payments to beneficial owners.

CDS may discontinue providing its service as securities depository with respect to any of the Securities at any time by giving reasonable notice to NFI and the Trustee. If CDS discontinues providing its service as securities depository with respect to any of the Securities and the Issuer is unable to obtain a successor securities depository, an investor will automatically take a position in the component securities and NFI will print and deliver to the investor certificates representing the Securities. If CDS discontinues providing its service as securities depository with respect to any of the Securities and NFI is unable to obtain a successor securities depository, NFI will automatically take a position in such Securities and will print and deliver to the investor certificates for such Securities.

Also, in the event that NFI decides to discontinue use of the system of book-entry only transfers through CDS (or a successor securities depository), NFI will print and deliver to the investor certificates for the Shares and Debentures the investor may own.

The information in this section concerning CDS and CDS' book-entry only system has been obtained from sources that the Issuer believes to be reliable, including CDS, but the Issuer takes no responsibility for its accuracy.

Neither the Issuer nor the Trustee has any responsibility or obligation to participants, or the persons for whom they act as nominees, with respect to:

- the accuracy of the records of CDS, its nominee, or any participant, of any ownership interest in the securities; or
- any payments to, or the providing of notice to, participants or beneficial owners.

### **Dividend Policy**

Effective with the July 2011 distribution, payable on August 15, 2011 to IDS holders of record on July 29, 2011, the Company decreased its IDS distributions from C\$1.17 per annum to C\$0.86 per annum, consisting of an annual dividend payment of C\$0.086 per pre-Consolidation Share (compared to the previous annual dividend level of C\$0.396 per pre-Consolidation Share) and an annual interest payment of C\$0.774 per C\$5.53 principal amount of Subordinated Notes. Following the Consolidation on September 30, 2011 (pursuant to which one post-Consolidation Share was exchanged for every ten pre-Consolidation Shares and the ratio of Shares and Subordinated Notes represented by each IDS was automatically adjusted to one post-Consolidation Share and C\$55.30 principal amount of Subordinated Notes), the dividend rate was adjusted accordingly and the Company began paying annual dividends of C\$0.86 per Share, which, together with annual interest payments of C\$7.74 on the principal amount of Subordinated Notes represented by each IDS, resulted in annual distributions of C\$8.60 per IDS. The Board maintained this dividend rate on a monthly basis until August 2012 when the remaining Subordinated Notes were redeemed.

Following the redemption of the remaining Subordinated Notes, the Board approved a new annual dividend rate of C\$0.585 per Share. This current dividend policy reflects a shift from the previous distribution policy, pursuant to which substantially all of the Company's available cash flow was distributed to IDS holders. The Board believes this dividend policy is consistent with the Company's long-term financial performance and the need to retain cash flows to support the ongoing requirements of the business and to provide the financial flexibility to pursue strategic growth and diversification opportunities.

The dividends on the Shares will be paid, if and to the extent dividends are declared by the Board and permitted by applicable law. Dividend payments are not mandatory or guaranteed. The Board may, in its discretion, modify or repeal NFI's current dividend policy at any time and without prior notice. No assurances can be made that NFI will pay dividends at the level contemplated by its current dividend policy in the future, or at all. See "Risk Factors – Risks Related to the Capital Structure – Payment of Dividends is Not Guaranteed".

NFI will pay dividends on the Shares (if declared) on or before the 15<sup>th</sup> day of each month (or the next business day, if such day is not a business day) to holders of record at the close of business on the last business day of the preceding month.

### ***Dividends and Distributions Declared on Shares and IDSs***

The following tables illustrate the monthly dividends paid on the Shares for the period from January 1, 2011 to December 31, 2013 and the monthly interest payments made on the Subordinated Notes and the monthly distributions made on the IDSs for the period from January 1, 2011 to the redemption date of the remaining Subordinated Notes on August 20, 2012. As of September 30, 2011, dividends on the Shares and distributions on the IDSs were paid on a post-Consolidation basis and reflected a consolidation of the Shares on a 10:1 basis and the adjustment made to the IDSs to reflect that IDSs represented, on a post-Consolidation basis, one Share and C\$55.30 principal amount of Subordinated

Notes. Following the redemption of the remaining Subordinated Notes on August 20, 2012, the dividends on the Shares have been paid at an annual rate of C\$0.585 per Share.

<u>Record Date</u>	<u>Dividend per Share</u> (Cdn\$)	<u>Interest Payment on Subordinated Notes</u> (Cdn\$)	<u>Total Distribution Per IDS</u> (Cdn\$)
January 31, 2011 .....	0.03298	0.06452	0.0975
February 28, 2011 .....	0.03298	0.06452	0.0975
March 31, 2011 .....	0.03298	0.06452	0.0975
April 29, 2011 .....	0.03298	0.06452	0.0975
May 31, 2011 .....	0.03298	0.06452	0.0975
June 30, 2011 .....	0.03298	0.06452	0.0975
July 29, 2011 .....	0.03298	0.06452	0.0975
August 31, 2011 <sup>1</sup> .....	0.007167	0.06452	0.07167
September 30, 2011 <sup>2</sup> .....	0.07167	0.6452	0.7167
October 31, 2011 .....	0.07167	0.6452	0.7167
November 30, 2011 .....	0.07167	0.6452	0.7167
December 30, 2011 <sup>3</sup> .....	0.07167	0.6452	0.7167
Total Fiscal Year 2011 Distributions.....	0.52470	3.09696	3.62 <sup>4</sup>
January 31, 2012 .....	0.07167	0.6452	0.7167
February 29, 2012 .....	0.07167	0.6452	0.7167
March 30, 2012 .....	0.07167	0.6452	0.7167
April 30, 2012 .....	0.07167	0.6452	0.7167
May 31, 2012 .....	0.07167	0.6452	0.7167
June 29, 2012 .....	0.07167	0.6452	0.7167
July 31, 2012 .....	0.07167	0.6452	0.7167
August 31, 2012.....	0.04875	N/A	N/A
September 28, 2012.....	0.04875	N/A	N/A
October 31, 2012 .....	0.04875	N/A	N/A
November 30, 2012 .....	0.04875	N/A	N/A
December 31, 2012 <sup>3</sup> .....	0.04875	N/A	N/A
Total Fiscal Year 2012 Distributions.....	0.74544	4.5164	5.0169
January 31, 2013 .....	0.04875	N/A	N/A
February 28, 2013 .....	0.04875	N/A	N/A
March 29, 2013 .....	0.04875	N/A	N/A
April 30, 2013 .....	0.04875	N/A	N/A
May 31, 2013 .....	0.04875	N/A	N/A
June 28, 2013 .....	0.04875	N/A	N/A
July 31, 2013 .....	0.04875	N/A	N/A
August 30, 2013 .....	0.04875	N/A	N/A
September 30, 2013 .....	0.04875	N/A	N/A
October 31, 2013 .....	0.04875	N/A	N/A
November 29, 2013 .....	0.04875	N/A	N/A
December 31, 2013 <sup>3</sup> .....	0.04875	N/A	N/A
Total Fiscal Year 2013 Distributions.....	0.58500	N/A	N/A

1. Effective with the July 2011 distribution payable on August 15, 2011, dividends on the Shares were decreased from C\$0.03298 per month per Share to C\$0.007167 per month per pre-Consolidation Share (or C\$0.396 per pre-Consolidation Share to C\$0.086 per pre-Consolidation Share on an annual basis).
2. Reflects dividends on the Shares and distributions on the IDSs paid on a post-Consolidation basis.
3. Declared in the year indicated but paid in the following year.
4. Rounded to the nearest hundredth.

## Credit Facility

NFI ULC, NFI and NFAI (collectively, the “Borrower”) have entered into the Credit Facility with a syndicate of financial institutions, in the amount of \$257 million. The Credit Facility consists of a \$142 million secured term loan facility and a revolving credit facility of up to \$115 million (including a \$55 million letter of credit sub-facility). The Credit Facility also includes an accordion feature of \$75 million for future investment or acquisition opportunities. The Credit Facility matures on April 24, 2017. A copy of the Credit Facility can be found on SEDAR at [www.sedar.com](http://www.sedar.com).

The Credit Facility is guaranteed by certain subsidiaries of NFI, and the obligations in respect of the Credit Facility are secured by all of the assets of the Borrower and those guarantors. NFI will continue to receive its cash distributions from the Borrower (other than NFI) and the guarantors of the Credit Facility, and as a result, the amounts owing under the Credit Facility and any interest thereon will be payable in priority to any cash distributions to holders of Shares and Debentures.

## DIRECTORS, OFFICERS AND MANAGEMENT

### Directors and Management

NFI’s articles of incorporation provide for a minimum of three and a maximum of 20 directors. NFI’s Board consists of nine individuals and is comprised as follows:

- The Honourable Brian Tobin, V. James Sardo, Wayne M.E. McLeod, Patricia Jacobsen, Paul Soubry and John Marinucci, each of whom is a Canadian resident. The Honourable Brian Tobin serves as the chairman of the Board; and
- Larry Edwards, Adam Gray and William Millar, each of whom is a U.S. resident.

The following table sets out the name, municipality of residence, position(s) with the Company and principal occupation of the directors of the Issuer.

<b>Name and Municipality of Residence</b>	<b>Position(s)</b>	<b>Director Since</b>	<b>Principal Occupation If not with the Company</b>
The Honourable Brian Tobin ..... Manotick, Ontario	Director (Chairperson of the Board)	2005	Vice-Chair, BMO Capital Markets
V. James Sardo ..... Mississauga, Ontario	Director (Chairperson of the human resources compensation and corporate governance committee)	2005	Corporate Director
Wayne M.E. McLeod ..... Toronto, Ontario	Director (Chairperson of the audit committee)	2005	Corporate Director
John Marinucci ..... Oakville, Ontario	Director	2005	Corporate Director
Larry Edwards ..... Tulsa, Oklahoma, USA	Director	2008	Corporate Director
Patricia Jacobsen ..... Vancouver, British Columbia	Director	2009	Corporate Director
Paul Soubry ..... Winnipeg, Manitoba	Director	2009	President and Chief Executive Officer of the Company
Adam Gray ..... Greenwich, Connecticut, USA	Director	2012	Managing Partner, Coliseum Capital Management, LLC
William Millar ..... Stevensville, Maryland, USA	Director	2012	Corporate Director

The term of office for each of the directors of NFI expires at the time of the next annual meeting of shareholders of NFI. Directors will be elected at each annual meeting of shareholders of NFI.

A director may be removed by a resolution passed by a majority of the shareholders or may resign. The vacancy created by the removal of a director must be filled at the shareholder meeting at which he or she was removed. A vacancy not so filled at a shareholder meeting, or created by the resignation of a director, may be filled by a quorum of the remaining directors. A quorum for meetings of directors is a majority of the directors, provided that a majority of directors present (or one director, where a quorum is two directors) must be residents of Canada. If there is no quorum of directors, a special shareholder meeting must be called to fill vacancies.

The directors supervise the activities and manage the affairs of NFI.

### ***Audit Committee***

The Issuer's audit committee is comprised of a minimum of three directors. All of the members of the audit committee are independent within the meaning of Multilateral Instrument 52-110 *Audit Committees* ("NI 52-110"). The audit committee is comprised of four members, being Wayne M.E. McLeod (Chair), Larry Edwards, Adam Gray and John Marinucci.

The audit committee is responsible for the oversight and supervision of the accounting and financial reporting practices and procedures of the Issuer, the adequacy of internal accounting controls and procedures, the quality and integrity of financial statements of the Issuer and the oversight of the Issuer's enterprise risk management framework. In addition, the audit committee is responsible for directing the auditors' examination of specific areas and for recommending to the Board the selection of independent auditors of the Issuer. The committee annually reviews the Chief Financial Officer's goals and objectives for the upcoming year and conducts regular reviews of the Chief Financial Officer's performance.

### ***Human Resources, Compensation and Corporate Governance Committee***

The Issuer has a human resources, compensation and corporate governance committee comprised of four directors. The members of the committee are V. James Sardo (Chair), The Honourable Brian Tobin, Patricia Jacobsen and William Millar. All of the members of the human resources, compensation and corporate governance committee are independent within the meaning of NI 52-110. The committee reviews and makes recommendations to the directors concerning the appointment of officers of the Issuer and its subsidiaries and the hiring, compensation, benefits and termination of senior officers of the Issuer and its subsidiaries. The committee annually reviews the Chief Executive Officer's goals and objectives for the upcoming year and conducts quarterly reviews of the Chief Executive Officer's performance. The committee also makes recommendations concerning the remuneration of directors of the Issuer and its subsidiaries. The committee administers and makes recommendations regarding the operation of any employee bonus or incentive plans, including the performance unit plan and the restricted share unit plan, and administers the deferred share unit plan for non-management directors. The committee is also responsible for developing the Issuer's approach to corporate governance issues, advising the Issuer's Board on filling vacancies on the Board and the boards of the Issuer and its subsidiaries and periodically reviewing the composition and effectiveness of each board and the contribution of individual directors, considering questions of management succession and considering and approving proposals by the directors of the Issuer to engage outside advisors on their behalf.

### ***Disclosure***

The Board is also responsible for adopting and periodically reviewing and updating the written disclosure policy for the Issuer and its subsidiaries. This policy, among other things:

- articulates the legal obligations of the Issuer, its affiliates and their respective directors, officers and employees with respect to confidential information;
- identifies spokespersons of the Issuer, who are the only persons authorized to communicate with third parties such as analysts, media and investors;
- provides guidelines on the disclosure of forward-looking information;
- requires advance review by senior executives of any selective disclosure of financial information to ensure that the information is not material, to prevent the selective disclosure of material information, and to ensure that if selective disclosure does occur, a news release is issued immediately; and
- establishes “black-out” periods immediately prior to and following the disclosure of quarterly and annual financial results and immediately prior to the disclosure of certain material changes, during which periods the Issuer, its subsidiaries and their directors, managers, officers, employees and consultants may not purchase or sell Shares or Debentures or other securities of the Issuer or its subsidiaries (including securities exchangeable for or convertible into Shares).

### ***Remuneration of the Directors***

In 2013, compensation for non-management directors of NFI was C\$90,000 per year with a maximum amount of C\$75,000 being paid in cash and a minimum amount of \$15,000 being received in the form of deferred share units under NFI’s Deferred Share Unit Plan for Non-Employee Directors (as described below) in four equal quarterly installments. Some non-management directors elected to receive a greater amount of their compensation in the form of deferred share units. Effective January 1, 2013, meeting attendance fees were no longer paid to directors. The Board believes a flat-fee base retainer is more aligned with a director's duties and responsibilities and time commitment to the corporation, which should not be meeting focused, but is a year-round commitment.

In 2013, the chairperson of the Board received additional remuneration of C\$90,000 per year and the chairperson of the audit committee and the chairperson of the human resources, compensation and corporate governance committee each received additional remuneration of C\$15,000 per year.

Directors may also receive a per diem of C\$2,000 in the event that they perform additional work authorized by the Board where such additional work occupies a majority of the director’s day. Directors are also reimbursed for out-of-pocket expenses for attending Board and committee meetings. Directors participate in the insurance and indemnification arrangements described below under “Insurance Coverage for the Company and Indemnification”.

### ***Deferred Share Unit Plan for the Non-Employee Directors***

In 2011, the Board adopted NFI’s Deferred Share Unit Plan for Non-Employee Directors. Pursuant to the plan, non-management directors may elect to receive all or a portion of their annual retainer and meeting fees in the form of DSUs instead of cash. A DSU is the right to receive a cash payment based on the value of a Share credited by means of a bookkeeping entry to an account in the name of the non-employee director. DSUs are credited to the director’s account on the last day of each calendar quarter, the number of which is determined by dividing the amount of the applicable portion of the director’s annual retainer by the fair market value of a Share on that date. When dividends are paid on a Share, additional DSUs equivalent to the amount of the dividend multiplied by the number of DSUs held (and determined based on the then fair market value of the Shares) will be credited to the director’s account. At

the end of the director's tenure as a member of the Board, he or she will be entitled to receive a cash redemption payment equal to the fair market value of a Share multiplied by the number of DSUs held.

### ***Restricted Share Unit Plan for the Non-Employee Directors***

On March 20, 2014, the Board adopted NFI's Restricted Share Unit Plan for Non-Employee Directors (the "Director RSU Plan"). In accordance with the policies of the TSX, the Director RSU Plan is subject to approval by NFI's shareholders at its 2014 annual meeting of shareholders. A maximum of 500,000 Shares will be available for issuance under the Director RSU Plan. Pursuant to the Director RSU Plan, non-employee directors will be permitted to elect, once each calendar year, to receive all or a portion of their annual retainer in the form of restricted Share units ("Director RSUs") and/or DSUs instead of cash. A Director RSU is a right to acquire a fully-paid and non-assessable Share credited by means of a bookkeeping entry to an account in the name of the non-employee director. A director generally must make the election prior to the end of the calendar year preceding the year to which such election is to apply. The Board, in its sole discretion, may award additional Director RSUs, subject to an annual aggregate value of \$150,000 per director. The number of Director RSUs to be awarded to a director is determined by dividing the amount of the applicable portion of the director's annual retainer by the applicable fair market value of a Share on that date. When dividends are paid on a Share, additional Director RSUs equivalent to the aggregate number of Director RSUs held by a director on the dividend record date multiplied by the amount of dividend paid by NFI on each Share, and then divided by the fair market value of the Shares on the dividend payment date, will automatically be credited to the director's account. Under the Director RSU Plan, Director RSUs vest immediately as at each applicable award date. A director (other than a U.S. director) will be permitted to exercise the Director RSUs credited to his or her account at any time prior to December 15 of the year following the year in which the director ceases to be a non-employee director of NFI or one of its affiliates. A U.S. director will be required to specify the exercise date in an annual election form in accordance with Section 409(A) of the U.S. Internal Revenue Code.

### ***Management***

Paul Soubry is the President and Chief Executive Officer, Glenn Asham is the Chief Financial Officer and Colin Pewarchuk is Executive Vice President, General Counsel and Corporate Secretary of the Company.

### ***Biographies of Directors and Executive Officers of NFI***

***The Honourable Brian V. Tobin***, P.C., O.C., ICD.D, was named as an Officer of the Order of Canada for his contribution to Canadian public policy. Mr. Tobin is currently a Vice-Chair of BMO Capital Markets, is the Chairperson of the board of New Flyer and serves as Lead Director and Vice Chairperson on the board of Aecon Group Inc. Previously, Mr. Tobin served as the Premier of Newfoundland and Labrador from 1996 to 2000 and won two consecutive majority governments in provincial elections held in February 1996 and February 1999. Mr. Tobin also served as a Member of Parliament from 1980 to 1996, served as Minister of Fisheries and Oceans in the federal cabinet from 1993 to 1996 and served as the Federal Minister of Industry from October 2000 to January 2002. Prior to joining BMO Capital Markets, Mr. Tobin was a Senior Business Advisor with Fraser Milner Casgrain LLP in Toronto and was a strategic advisor to a number of Canadian corporations. Mr. Tobin served as the Executive Chairman, President and Chief Executive Officer of Consolidated Thompson Iron Mines Limited until May 2011 when that company was purchased by Cliffs Natural Resources Inc. Mr. Tobin has also served as a director of Aurvista Gold Corporation, Calvista Gold Corporation, Cline Mining Corporation, Marret Resources Inc., Lions Gate Entertainment Corp. and Canpages Inc. and was a trustee of Newport Partners Income Trust. Mr. Tobin is a member of the Institute of Corporate Directors and a graduate of the Directors Education Program.

**V. James Sardo**, ICD.D, is a corporate director and since 2013 has served on the board of Cline Mining Corporation. Mr. Sardo also serves on the boards of Currency Exchange International Corporation and Capstone Infrastructure Corporation (formerly Macquarie Power and Infrastructure Corporation). Mr. Sardo was a director of Consolidated Thompson Iron Mines Limited from 2010 to 2011, Royal Group Technologies Limited from 2003 to 2006, Hydrogenics Corporation from 2003 to 2009, SonnenEnergy Corp from 2008 to 2009 and Northstar Healthcare Inc. from 2008 to 2010. Mr. Sardo was also a trustee of Countryside Power Income Fund from 2004 to 2007; Union Waterheater Income Trust from 2003 to 2007; and Custom Direct Income Fund from 2003 to 2007. Prior to these appointments, Mr. Sardo was interim CEO of Royal Group Technologies Limited from 2004 to 2005, President of the Canadian Operations of Moore Corporation Limited, a business forms and communications company, from 1999 to 2001 and President and CEO of SMK Speedy International Inc., an international automotive repair company, from 1997 to 1999. Prior to 1997 Mr. Sardo was Chief Executive Officer of Amre Inc., a Dallas based marketer of home improvement products from 1994 to 1995 and Chief Executive Officer of SNE Inc., a manufacturer and marketer of windows and doors from 1991 to 1994. Mr. Sardo was the President of Firestone Canada Inc. from 1983 to 1988 and its Chief Executive Officer from 1985 to 1988. Mr. Sardo is a member of the Institute of Corporate Directors and a graduate of the Directors Education Program.

**Wayne M.E. McLeod**, FCA, is a corporate director and also serves as a trustee of Richards Packaging Income Fund. Mr. McLeod was a trustee of Atlas Cold Storage Income Fund until October 2006, a director of CanWest Mediaworks Inc. until July, 2007, a director of Turbo Power Systems Inc. until 2008, a director of SMTC Corporation until 2011 and a director of Morguard Investments Inc. until 2013. He is also a Fellow of the Institute of Chartered Accountants of Ontario. He received his Masters of Business Administration from Harvard University in 1965. Mr. McLeod retired in 1999 after 20 years with CCL Industries Inc., where he served as President, Chief Executive Officer and Chairman of the board of directors, among other positions. Mr. McLeod has served twice as an executive-in-residence for the Institute of Corporate Directors and is the past chairperson of the Institute.

**John Marinucci**, C.A., ICD.D, H.R.C.C.C, joined New Flyer as President and Chief Executive Officer in 2002 and retired as an executive officer of the Company at the beginning of 2009. Mr. Marinucci also serves as a director of Intelgenx Corporation. He is a governor and past chairperson of Mohawk College in Hamilton, Ontario and the chairperson of the CWB Group of Companies. Mr. Marinucci previously served as a director of SMTC Corporation. Mr. Marinucci is a Chartered Accountant and holds an Honours Bachelor of Commerce degree from McMaster University. Mr. Marinucci has a strong manufacturing background with a proven track record in operational restructurings and management of highly leveraged business concerns. Mr. Marinucci served for eight years as President and Chief Operating Officer for a major Canadian manufacturer and lessor of freight railcars and is a former President of the Canadian Association of Railway Suppliers. He has also held executive and senior management roles within leading Canadian and United States based organizations. Mr. Marinucci is also a member of several private company boards and is the founder and Chairman of the Marinucci Family Foundation, a registered charity focused on funding education, live arts and proactive healthcare initiatives. Mr. Marinucci is a member of the Institute of Corporate Directors and a graduate of the Directors Education Program.

**Larry Edwards**, ICD.D, is a corporate director and also serves as a director of Red Fork Energy Limited (a company listed on the Australian Securities Exchange) and as a director and Chairman of the board of Victory Energy Organization, LLC, an Oklahoma (USA) based designer and manufacturer of fired packaged boilers, waste heat boilers and heat recovery steam generators and related equipment. Mr. Edwards served on the board of NCI Building Systems, Inc. from 2007 to 2009 and was a director of Global Power Equipment Group Inc. (“GPEG”) and its predecessor Global Energy Equipment Group, Inc. from 1998 until January, 2008. Mr. Edwards served as the President and Chief Executive Officer of GPEG from June 1998 until his retirement in December 2006. Mr. Edwards also served as the CEO of

GPEG's predecessor company from June 1998 until GPEG's initial public offering in May 2001. From February 1994 until June 1998, Mr. Edwards served as the President of Jason Incorporated's power generation division. From 1976 until 1994, Mr. Edwards held various positions with Braden Manufacturing, including Vice President of Operations, General Manager and President. Prior to the IPO, Mr. Edwards served on the board of Transit Holdings since August 2004. Mr. Edwards earned a B.S. in Industrial Engineering and Management from Oklahoma State University and an M.B.A. with honors from Oklahoma City University. Mr. Edwards is a member of the Institute of Corporate Directors and a graduate of the Directors Education Program.

**Patricia Jacobsen**, ICD.D, has been a corporate director since she stepped down in 2008 as the CEO of the Greater Vancouver Transportation Authority (TransLink). Ms. Jacobsen is also a director of Revera Inc., a Canadian investment and operations company with retirement and residential homes in Canada and the United States. Ms. Jacobsen was the Chair of the British Columbia Transportation Property and Casualty Company, and served as a director of Port Metro Vancouver, Air Canada, the Urban Transit Development Corporation (Ontario) and the Canada Line Corporation (B.C.). A graduate of the University of Manitoba, Ms. Jacobsen held several senior positions with the Ontario Provincial Government, including Deputy Minister of Transportation. Following her public service career, Ms. Jacobsen held senior executive positions in the insurance industry with Manulife Financial and Liberty Mutual in Toronto and was the CEO of the Workers' Compensation Board of Manitoba. Ms. Jacobsen is a member of the Institute of Corporate Directors and a graduate of the Directors Education Program.

**Adam Gray**, is a managing partner of Coliseum Capital Management, a private firm that makes long-term investments in both public and private companies, which he co-founded in December 2005. He also serves as non-executive Chairman of Redflex Holdings Limited and on the board of directors of Uno Restaurant Holdings Corporation. Mr. Gray served on the board of directors of DEI Holdings, Inc. since February 2009 until its sale in June 2011, and on the board of directors of Benihana Inc. since September 2010 until its sale in August 2012. From January 2005 to November 2005, Mr. Gray was a consultant for a private investment firm. From 2003 to 2004, Mr. Gray served as Executive Vice President, Strategic Projects and Capital Management at Burger King Corp. From 1993 to 2003, Mr. Gray held several executive positions with the Metromedia Restaurant Group, comprised of S&A Restaurant Corp. and Metromedia Steakhouses Company, LP, which included the Bennigan's, Steak & Ale, Ponderosa and Bonanza restaurant concepts. Prior to that time, Mr. Gray served as an Associate at Kluge & Co. and an Analyst within Morgan Stanley's Merchant Banking Group. Mr. Gray holds both a BSE in Finance from the Wharton School of Business and a BS in Mechanical Engineering from the School of Engineering & Applied Science at the University of Pennsylvania.

**William Millar**, is a well known expert in the fields of public transportation and transportation policy, who effectively led the American Public Transportation Association (APTA) serving as its President/CEO from 1996 to 2011. Mr. Millar served 19 years at the Port Authority of Allegheny County, the principal transit operator serving Pittsburgh, PA. As executive director from 1983-1996, he oversaw the development and operation of bus, busway, light rail, paratransit and inclined plane service. He is the founder of Pittsburgh's award-winning ACCESS paratransit service. Mr. Millar, a strong supporter of transportation research, received the Founding Father Award for his leadership in establishing the Transit Cooperative Research Program (TCRP). He was a member of the executive committee of the Transportation Research Board (TRB) for over two decades serving as its chair in 1992. Mr. Millar serves on the board of directors of Traffax, Inc. and as a Senior Advisor for Rail and Transit at H.W. Lochner, Inc. and a member of the Board of Advisors for Veolia Transportation and the High Speed Rail Expert Review Panel for the Texas Transportation Institute. Mr. Millar is the recipient of many awards including APTA's Jesse Haugh Award as Transit Manager of the Year (1987); the TRB's W. N. Carey, Jr. Distinguished Service Award (1999) and Thomas B. Deen Distinguished Lectureship (2012); Railway Age's Graham Claytor Award (2006); the Texas Transportation Institute's Director's Research Champion Award (2008) and the Eno Foundation's Award for Transportation Excellence

(2011). Mr. Millar has received lifetime achievement awards from the American Association of State Highway and Transportation Officials (AASHTO), the Conference of Minority Transportation Officials (COMTO), the Council of University Centers (CUTC) and was inducted into the Intelligent Transportation Society of America Hall of Fame in 2011 and APTA's Hall of Fame in 2013. Mr. Millar has a BA from Northwestern University in geography and an MA from the University of Iowa in urban and regional planning.

**Paul Soubry**, ICD.D, joined New Flyer as President and Chief Executive Officer in January, 2009. Mr. Soubry holds a Bachelor of Commerce (Honours) degree from the University of Manitoba and completed the executive development program at Harvard Business School. Mr. Soubry has a strong sales, marketing, business development and operations background in highly leveraged businesses held by both trade and private equity owners with substantial experience in business transformations and LEAN operational practices. Prior to joining New Flyer, Mr. Soubry worked for StandardAero where he held a variety of increasingly senior positions including being named President in 2001, Chief Operating Officer in 2006, and Chief Executive Officer in 2007. Mr. Soubry currently serves on the boards of True North Sports and Entertainment Limited and the Winnipeg Jets Hockey Club and the Winnipeg Airports Authority. He has also served on the board of the Mondetta Clothing Company and Economic Development Winnipeg Inc. In 2003, Mr. Soubry was named one of the recipients of "Canada's Top 40 under 40" award. Mr. Soubry is a member of the Institute of Corporate Directors and a graduate of the Directors Education Program.

**Glenn Asham** joined New Flyer in 1992. Mr. Asham obtained his chartered accountancy designation in 1987 and a Bachelor of Commerce from the University of Manitoba in 1984. Prior to joining the Company, he worked with Deloitte & Touche for eight years, providing client services in the areas of accounting, auditing, taxation and management consulting.

**Colin Pewarchuk** joined New Flyer in 2006 and is the Executive Vice President, General Counsel and Corporate Secretary. Mr. Pewarchuk obtained a Bachelor of Commerce (Honours) from the University of Manitoba in 1990 after which he worked for a leading Canadian financial institution as a personal banker. Mr. Pewarchuk obtained a law degree from the University of Manitoba in 1996 and prior to joining New Flyer, was a lawyer at the law firm of Aikins, MacAulay & Thorvaldson LLP since 1997. Mr. Pewarchuk is a member of the Institute of Corporate Directors and a graduate of the Directors Education Program.

As at December 29, 2013 the directors and executive officers of NFI as a group beneficially owned, directly or indirectly, or exercised control or direction over, approximately 825,000 Shares, representing approximately one and one-half percent of all issued and outstanding Shares. The executive officers of NFI's subsidiaries, together with the directors and executive officers of NFI, as a group, beneficially owned, directly or indirectly, or exercised control over, approximately one million Shares, representing approximately two percent of all issued and outstanding Shares as at December 29, 2013. None of the directors or officers of NFI or the executive officers of NFI's subsidiaries own Debentures.

#### ***Cease Trade Orders, Bankruptcies, Penalties and Sanctions***

Between April 3, 2006 and May 3, 2006, Mr. Sardo, who was then a director of Royal Group Technologies Limited, was prohibited from trading in securities of Royal Group Technologies Limited pursuant to a management cease trade order issued by the Ontario Securities Commission in connection with the delay in filing of certain of Royal Group Technologies Limited's financial statements.

On September 28, 2006, Global Power Equipment Group Inc. ("GPEG") and all of its U.S. subsidiaries filed voluntary petitions for reorganization under chapter 11 of title 11, United States Code in the United States Bankruptcy Court for the District of Delaware. Mr. Edwards served as Chairman of the

Board, President and Chief Executive Officer at the time of filing. On November 22, 2006, Mr. Edwards resigned as President and Chief Executive Officer of the Company; remaining as Chairman of the Board. GPEG and its U.S. subsidiaries emerged from bankruptcy proceedings in January, 2008 and Mr. Edwards resigned as a director of GPEG.

For a period of less than two months between October 26, 2004 and December 12, 2004, Mr. Soubry served as a director of Crocus Investment Fund (“Crocus”), a labour-sponsored venture capital corporation created by The Crocus Investment Fund Act (Manitoba). On December 10, 2004, in connection with an organizational review and assessment of the value of its portfolio, Crocus received regulatory approval from the Manitoba Securities Commission to suspend redemptions and to halt sales of its shares. On June 28, 2005, Deloitte & Touche Inc. was appointed receiver and manager of Crocus by the Manitoba Court of Queen’s Bench pursuant to an application made by the Manitoba Securities Commission and on September 4, 2009, the Manitoba court approved an interim distribution to all shareholders of Crocus and the distribution of funds to shareholders in settlement of various proceedings brought against Crocus.

Except as described above, to the knowledge of the Issuer, no director or executive officer of the Issuer or a shareholder holding a sufficient number of securities of the Issuer to affect materially the control of the Issuer is, or within the ten years prior to the date hereof has been, a director or executive officer of any company (including the Issuer) that, while that person was acting in that capacity, (i) was the subject of a cease trade or similar order or an order that denied the relevant company access to any exemption under securities legislation for a period of more than 30 consecutive days; (ii) was subject to an event that resulted, after the director or executive officer ceased to be a director or executive officer, in the company being the subject of a cease trade or similar order or an order that denied the relevant company access to any exemption under securities legislation for a period of more than 30 consecutive days; or (iii) within a year of that person ceasing to act in that capacity, became bankrupt, made a proposal under any legislation relating to bankruptcy or insolvency or was subject to or instituted any proceedings, arrangement or compromise with creditors or had a receiver, receiver manager or trustee appointed to hold its assets.

To the knowledge of the Issuer, no director or executive officer of the Issuer or a shareholder holding a sufficient number of securities of the Issuer to affect materially the control of the Issuer has, within the ten years prior to the date hereof, become bankrupt, made a proposal under any legislation relating to bankruptcy or insolvency, or become subject to or instituted any proceedings, arrangement or compromise with creditors, or had a receiver, receiver manager or trustee appointed to hold the assets of the director, officer or shareholder.

## **Long-Term Incentive Plans**

### ***New PUP and RSU Plans***

Effective January 1, 2011, NFI ULC amended the existing performance unit plan as the New Performance Unit Plan (the “New PUP”). The terms of the New PUP govern awards made on or after January 1, 2011. As a result of the changes in the capital structure of NFI and NFI ULC, the human resources compensation and corporate governance committee determined that it was necessary to make certain changes to the New PUP. Accordingly, the New PUP was amended on October 2, 2011 to treat the New PUP awards on an equivalent basis as IDSs that were converted into Shares pursuant to the August 19, 2011 offering and taking into account the September 30, 2011 consolidation of Shares.

On December 13, 2011, the Board approved the NFI ULC Restricted Share Unit Plan (the “RSU Plan”) which provides for grants of restricted share units (“RSUs”) to officers and senior managers of the

Company. An RSU is the right to receive a cash payment based on the fair market value of a Share, subject to vesting.

The purposes of the New PUP and the RSU Plan (collectively, the “Incentive Plans”) are to attract, retain, motivate and reward officers and senior managers of the Company by making a significant portion of their long term incentive compensation dependent on the Company’s financial performance. One of the key advantages of the Incentive Plans are that they will further align the interests of management and investors given that the award grant and redemption values will be determined based on the fair market value of the Shares. Under the terms of the Incentive Plans, the human resources, compensation and corporate governance committee may grant eligible participants each year unit grants thereunder which give the holders thereof the right to receive, upon vesting and redemption of units, a cash payment equal to the fair market value of a Share. When dividends are paid on a Share, additional units equivalent to the amount of the dividends multiplied by the number of units held (and determined based on the then fair market value of the Shares) will be credited to the participant’s account. Units granted under the New PUP generally vest at the end of the third fiscal year following the date of grant in an amount equal to a percentage of between approximately 38% and 256% of the units in the participant’s account, depending on the position and subject to and based on the Company achieving certain specified performance targets. RSUs will generally vest at the end of the third fiscal year following the date of grant. Following the time of vesting, participants will be entitled to receive cash redemption payments equal to the fair market value of a Share for every vested unit held. Units shall also immediately vest upon the closing of a transaction resulting in certain change of control events and upon certain terminations of employment.

Effective December 17, 2012, the Board approved the Performance and Restricted Share Unit Plan (the “PRSU Plan”) to consolidate the New PUP and RSU Plan into one document. The terms of the PRSU Plan will govern awards made on or after January 1, 2013. The PRSU Plan was amended effective December 16, 2013 (the “Amended PRSU Plan”) to change the performance measure from 3-year cumulative Adjusted EBITDA to 3-year average annual return on invested capital. The terms of the Amended PRSU Plan will govern awards made on or after the 2014 plan year.

### ***Share Option Plan***

On March 21, 2013, the Board adopted a new Share Option Plan (the “Option Plan”) for NFI. Only employees of NFI and certain affiliates (“participants”) may receive grants of share options (“Options”) under the Option Plan. Non-employee directors of NFI are not eligible to participate in the Option Plan. The Option Plan was approved by NFI’s shareholders at the annual general meeting held on May 9, 2013. A maximum of 3,600,000 Shares of NFI are available for issuance under the Option Plan.

The purposes of the Option Plan are to: (i) support the achievement of NFI’s performance objectives; (ii) ensure that interests of key persons are aligned with the success of NFI; and (iii) provide compensation opportunities to attract, retain and motivate senior management critical to the long-term success of NFI and its subsidiaries. The human resources, compensation and corporate governance committee may award Options to any eligible employee. The exercise price of an Option may not be less than fair market value on the date of the grant which, for these purposes means the closing price of a Share on the principal stock exchange on which the Shares are traded on the last trading day immediately preceding the applicable day. The vesting terms and expiry of an Option will be determined by the committee for each applicable grant, provided that Options must expire no later than the eighth anniversary of the date of grant, except that Options which would otherwise expire during, or within 10 business days following a blackout period will expire 10 business days following the end of the blackout period. Each Option will vest on the date or dates designated in the grant agreement or such earlier date as is provided for in the Option Plan or is determined by the committee. If no specific provision is made, Options will vest 25% on each of the first through fourth anniversaries of the date of grant. Vested Options may be exercised by the participant providing a notice of exercise and paying the exercise price

in full to NFI. On exercise of a vested Option, NFI will issue to the participant one Share for each vested Option elected to be exercised. Options are not transferable or assignable other than by will or the laws of descent and distribution.

On March 21, 2013, the human resources, compensation and corporate governance committee approved the grant of a total of 490,356 Options (determined based on a valuation using the closing price of the Shares on the TSX on March 25, 2013) to eleven executives. The Options will expire on March 26, 2021.

### **Insurance Coverage for the Company and Indemnification**

The Company obtained a policy of insurance for directors and officers of NFI and for the directors and officers of its subsidiaries. Under the policy, each entity has reimbursement coverage to the extent that it has indemnified directors and officers. The policy includes securities claims coverage, insuring against any legal obligation to pay on account of any securities claims brought against NFI and its subsidiaries. The total limit of liability will be shared among NFI and its subsidiaries and their respective directors and officers so that the limit of liability will not be exclusive to any one of the entities or their respective directors and officers.

The by-laws of NFI provide for the indemnification its directors and officers from and against liability and costs in respect of any action or suit brought against them in connection with the execution of their duties of office, including in respect of periods prior to closing of the IPO, subject to certain limitations.

### **AUDIT COMMITTEE AND AUDITOR’S FEES**

The Issuer has an audit committee consisting of four directors: Wayne M.E. McLeod (Chair), Larry Edwards, Adam Gray and John Marinucci, each of whom is independent of the Issuer and “financially” literate within the meaning of NI 52-110. The audit committee is responsible for the oversight and supervision of the accounting and financial reporting practices and procedures of the Issuer, monitoring the adequacy of internal accounting controls and procedures, reviewing the quality and integrity of financial statements of the Issuer and the oversight of the Issuer’s enterprise risk management framework. The independent auditors of the Issuer report directly to the audit committee. In addition, the audit committee is responsible for reviewing and approving the auditors’ audit plan and for recommending to the Board the selection of independent auditors of the Issuer. The charter of the audit committee is attached hereto as Appendix “A”.

### **Relevant Education and Experience of Audit Committee Members**

The following is a brief summary of the education or experience of each member of the audit committee that is relevant to the performance of his or her responsibilities as a member of the audit committee, including any education or experience that has provided the member with an understanding of the accounting principles used by the Issuer to prepare its annual and interim financial statements:

<b>Name of Audit Committee Member</b>	<b>Relevant Education and Experience</b>
Wayne M.E. McLeod (Chair) .....	Mr. McLeod is a FCA and spent 12 years as an audit partner of Thorne Riddell and served on the CICA Audit Research Committee for three years in the 1970s.
Larry Edwards .....	Mr. Edwards holds a MBA and was the President and CEO of a NYSE-listed public company.

<u>Name of Audit Committee Member</u>	<u>Relevant Education and Experience</u>
Adam Gray .....	Mr. Gray has an undergraduate business school education with a major in finance. He has worked in several investment banks, has served as Investment Manager for several investment funds and has served on other audit committees.
John Marinucci .....	Mr. Marinucci is a chartered accountant and has worked as an audit manager in an international chartered accounting firm. Mr. Marinucci has served as president and chief executive officer of other companies, including the Issuer.

## Non-Audit Services

The audit committee has adopted specific policies and procedures for the engagement of external auditors for all services, including non-audit services. In particular, the audit committee is required to pre-approve the appointment of the auditor for any non-audit service to be provided to the Issuer or to any subsidiary of the Issuer; provided that it is not required to approve any service that is prohibited under the rules of the Canadian Public Accountability Board or the Independence Standards of the Canadian Institute of Chartered Accountants. Before the appointment of the auditor for any non-audit service, the audit committee will consider the compatibility of the service with the auditor's independence.

The audit committee may delegate to one or more members the authority to pre-approve the appointment of the auditor for any non-audit service to the extent permitted by applicable law. The pre-approval of non-audit services by any member to whom authority has been delegated must be reported to the full audit committee at its first scheduled meeting following such pre-approval.

## External Auditor Service Fees

The following table summarizes the Audit, Audit Related, Tax Related and Other Fees (excluding expenses and taxes) of the Issuer's external auditor for the last two fiscal years:

	<u>Fiscal 2013</u>	<u>Fiscal 2012</u>
Audit Fees	C\$737,160	C\$532,960
Audit-Related Fees	C\$218,759 <sup>(1)</sup>	C\$114,372 <sup>(2)</sup>
Taxation Fees	C\$235,189 <sup>(3)</sup>	C\$169,427 <sup>(4)</sup>
All Other Fees	C\$ 5,800 <sup>(5)</sup>	C\$0

<sup>(1)</sup> The 2013 fees related to the audit of NABI's opening balance sheet.

<sup>(2)</sup> The 2012 fees related to convertible debt insurance.

<sup>(3)</sup> The 2013 fees related to compliance matters as well as the NABI acquisition.

<sup>(4)</sup> The 2012 fees related to various consultations with external tax advisors.

<sup>(5)</sup> The 2013 fees related to the investment by Marcopolo.

## Audit Committee Oversight

At no time since the commencement of the Issuer's most recently completed fiscal year has a recommendation of the audit committee to nominate or compensate an external auditor not been adopted by the Board.

## Risk Management

Risk management practices have been part of the Company's regular business operations to help enhance decision-making and resource allocation. The Company's risk management process focuses on the identification of risks associated with the Company's business and its operational and strategic objectives, and the assessment and mitigation of those risks. The alignment of risks has been enhanced

across the Company while taking into account both internal and external risk factors. The Company continues to evaluate its risk tolerances for specific strategies and objectives. In order to support management's commitment to enhancing risk management practices and enhanced accountability, the Company continues to deploy risk assessment training to employees involved in the risk management processes. The Company has embedded risk management practices within the annual budget and annual operating planning process and determination of management objectives. The Company's risk management program is managed through an executive level risk committee in conjunction with and chaired by the Company's Director of the Audit and Risk Management Services department.

## **RISK FACTORS**

An investment in the Shares and the Debentures involves a number of risks. The risks described below are not the only risks facing the Company. Additional risks and uncertainties not currently known or that are currently considered to be immaterial may also materially and adversely affect the Company. If any of these risks actually occur, the business, financial condition, results of operations and cash flows of the Company and the amount of cash available for distribution to investors could be adversely affected, in which case the trading prices of the Shares and the Debentures may decline.

### **Risks Related to the Business of the Company**

#### ***Ability to successfully execute strategic plans and maintain profitability***

The Company's future operating results will depend on a number of factors, including its ability to successfully execute its strategic plans. The Company's past results may not be indicative of its future prospects and there is no assurance that the Company will sustain or grow profitability in future periods. The Company's capital structure may inhibit its ability to successfully achieve its strategic plans by limiting or preventing the Company from obtaining additional capital (either by borrowing funds from its lenders or raising equity capital in the capital markets).

In addition, the successful execution of the Company's strategic plans may require additional employees, additional operating and financial systems and additional financial resources. There is no assurance that the Company will be able to hire and train qualified employees (or do so on a timely basis), that the Company will be able to expand operations and systems to the extent, and in the time required, or that the Company will be able to fund such strategic plans, either internally through operations, through the use of available credit or through the capital markets. There is no assurance that the Company will be able to effectively execute and manage its strategic plans and any future growth, and any failure to do so could have a material adverse effect on the Company's business, financial condition, liquidity and operating results.

#### ***Competition in the heavy-duty transit bus industry***

There is significant competition and excess production capacity in the heavy-duty transit bus industry in Canada and the United States. Although the Company is the current market leader, its principal competitors (among which are Gillig and Nova Bus Inc.) may gain market share and new competitors may emerge in the industry. There can be no assurance that the Company will maintain its current leading position. There is also strong competition in the aftermarket parts and service markets where the Company sells parts and services to transit agencies. New Flyer is the only publicly-traded heavy-duty transit bus manufacturer in the United States and Canada and is subject to certain legal disclosure requirements. These disclosure requirements may put New Flyer at a competitive disadvantage. In addition, the recent recession, the funding pressures on transit agencies for capital purchases and operating funds, combined with aging bus fleets have increased the importance of price in the evaluation

criteria for replacement buses and aftermarket parts and services, have resulted in extremely aggressive pricing among competitors in the heavy-duty transit bus industry.

There can be no assurance that the Company will be able to compete successfully against its current or future competitors or that such competition will not have a material adverse effect on the Company's business financial condition, liquidity and operating results.

***Funding may not continue to be available to the Company's customers at current levels or at all***

The Company's principal customers are municipal and other local transit authorities that rely on funding from various levels of government to purchase heavy-duty transit buses. There can be no assurance that this funding will continue to be available at current levels, on the same terms or at all. Eighty percent of the total eligible funding for purchases of new heavy-duty transit buses in the United States is provided by the federal government through allocations to the FTA. Under MAP-21, \$10.6 billion of spending was authorized for fiscal year 2013 and \$10.7 billion for fiscal year 2014 for public transportation. Primary changes with this funding legislation include the establishment a new needs-based formula program and new asset management requirements. In addition, it establishes performance-based planning requirements for transit agencies that align federal funding with key goals and tracks progress of each grantee towards these goals.

On March 4, 2014, the U.S. Budget proposal for 2015 fiscal year was released. The centerpiece of the transportation budget is a four-year, \$302 billion surface transportation authorization proposal that provides \$72.3 billion for public transportation over that period and \$17.6 billion in 2015 fiscal year. The \$17.6 billion figure includes almost \$14.0 billion for transit formula grants, and \$2.5 billion for capital investment grants.

The U.S. Senate Banking, Housing and Urban Affairs Committee, the U.S. Senate Environment and Public Works Committee, and the U.S. House of Representatives Transportation and Infrastructure Committee are working toward drafting bills for reauthorization and hope to pass them prior to the expiration of MAP-21 on September 30, 2014. U.S. mid-term elections are in November 2014 and there is no certainty that a reauthorization bill will be passed. Without a new bill, an extension of MAP-21 will be required. Although management expects that an extension would be passed if a reauthorization bill is not passed, there is no assurance that this will happen.

Any decline in or changes in the terms of governmental and local funding for purchases of new heavy-duty transit buses and/or purchases of aftermarket parts or services could have a material adverse effect on the Company's business, financial condition, liquidity and operating results.

***The Company may incur material losses and costs as a result of product warranty costs, recalls and remediation of buses***

The Company is subject to product warranty claims in the ordinary course of its business. The Company provides a 12-year warranty (and in some circumstances, a 18-year warranty) on its bus structures and a one to five year warranty on certain other bus components. In addition, many bus purchase contracts have fleet defect provisions whereby if a certain percentage of a customer's fleet (typically 10% to 25%) experiences the same defect, the Company is obligated to replace or repair all such components (whether they experienced failures or not) across the fleet. Certain other extended warranties for major subsystems such as engines, transmissions, axles and air conditioning are generally purchased for the customer from the component supplier. The Company attempts to adequately price ongoing warranty costs into its bus purchase contracts. If the Company produces poor quality products, develops new products with deficiencies or receives defective materials or components, it may incur material unforeseen costs in excess of what it has provided for in its contracts or reserved in its financial

statements. The Company is currently aware of warranty issues regarding rear bus structures, structural corrosion and certain engines which may result in unforeseen material warranty costs. In addition, the Company may not be able to enforce warranties and extended warranties received or purchased from its suppliers if such suppliers refuse to honour such warranties or go out of business. Also, a customer may choose to pursue remedies directly under its contract with the Company over enforcing such supplier warranties. In such a case, the Company may not be able to recover its losses from the supplier. The Company is also periodically subject to product warranty claims from its customers due to bus fires. Such fires are common in the transit bus industry, particularly in the engine compartment area due to the restricted size of the compartment, the nature of the components used in the manufacture of buses and the arduous operating life cycles of buses.

The Company is also potentially subject to recalls of its products from customers to cure manufacturing defects or in the event of a failure to comply with customers' order specifications or applicable regulatory standards. The Company is also potentially subject to recalls made by the suppliers of components or parts which the Company purchased and incorporated into buses. The Company may also have to remedy or retrofit buses in the event that an order is not built to a customer's specifications or where a design error has been made. Significant warranty claims, retrofit and remediation costs or product recalls could have a material adverse effect on the Company's financial condition and results of operations and the amount of cash available for distribution to investors. Moreover, the adverse publicity that may result from a product warranty claim, product remediation or retrofit or product recall or perceived or actual defect with the Company's products could have a material adverse effect on the Company's ability to successfully market and sell its products. See "Description of the Business — Product Warranty and Other Contractual Provisions".

***The Company may incur material losses and costs as a result of product liability claims***

The Company faces an inherent risk of exposure to product liability claims if the use of its products result, or are alleged to result, in personal injury and/or property damage. If the Company manufactures a defective product or if component failures or component fires result in damages that are not covered by warranty provisions, it may experience material product liability losses in the future. In addition, the Company may incur significant costs to defend product liability claims. The Company could also incur damages and significant costs in correcting any defects, lose sales and suffer damage to its reputation. The Company's product liability insurance coverage may not be adequate for any liabilities it could incur and may not continue to be available on terms acceptable to it. Significant product liability claims could have a material adverse effect on the Company's financial condition and results of operations and the amount of cash available for distribution to investors. Moreover, the adverse publicity that may result from a product liability claim or perceived or actual defect with the Company's products could have a material adverse effect on the Company's ability to successfully market its products.

***The Company's success depends on a limited number of key executives who the Company may not be able to adequately replace in the event they leave the Company***

The success of the Company's business strategy and its ability to operate profitably depend on the continued employment of its senior management team. The loss of the services of one or more of these key executives could have a material adverse effect on the Company. There can be no assurance that the Company will be able to retain its existing senior management, attract additional qualified executives or adequately fill new senior management positions or vacancies created by expansion or turnover.

***The Company may not be able to successfully renegotiate collective bargaining agreements when they expire and may be adversely affected by labour disruptions and shortages of labour***

The Company is subject to the risk of work stoppages and other potential labour relations issues because a significant portion of its production workforce is unionized. Approximately 47% of the Company's total employees are represented by unions under four collective bargaining agreements. Collective agreements with New Flyer's unionized employees in the Winnipeg, Manitoba, St. Cloud, Minnesota and Crookston, Minnesota plants expire March 31, 2015, March 31, 2017 and December 31, 2015, respectively. The Company may be unable to successfully negotiate new collective bargaining agreements for these employees. Any labour disruption could, depending on the operations affected and the length of the disruption, have a material adverse effect on the Company's business, financial condition, liquidity and operating results. Labour relations problems and work stoppages could also occur at other companies upon which the Company is dependent for raw materials, components or services. The Company is also subject to the risk that sufficient skilled and unskilled labour may not exist in and around its locations. Such occurrences could result in a significant loss of production and revenue and have a material adverse effect on the Company's business, financial condition, liquidity and operating results.

***United States local job creation criteria in solicitations may create a competitive disadvantage***

US transit agencies are assessing whether to evaluate bus manufacturers participating in bus solicitations on the ability to create jobs in the US. Reviews on the permissibility of this type of assessment by the FTA and APTA are currently in progress and it is not yet determined whether agencies will adopt such an evaluation criteria in their procurements nor can the impact be determined. One large US agency did include US job creation as a criteria in its bus solicitation, which was awarded to New Flyer. Any changes in legislation or procurement criteria that mandate a US jobs preference may put the Company at a competitive disadvantage if it is unable to create a sufficient number of US jobs to win a solicitation. To the extent that this prevents the Company from winning a material number of solicitations, it may have a material adverse effect on the Company's business, financial condition, liquidity and operating results.

***Absence of fixed term customer contracts, exercise of options and customer termination for convenience***

As is general industry practice, the Company does not typically enter into long term supply agreements with its customers. Individual transit authorities only undertake significant procurement of new buses once every few years. Customers may, without notice or penalty, terminate their relationship with the Company at any time. Even if customers should decide to continue their relationship with the Company, there can be no guarantee that they will purchase the same volume of products as in the past or that they will pay the same price for those products as they have in the past. Moreover, many customer contracts include options to purchase buses in the future and the Company's order book is increasingly represented by options as opposed to firm orders. Although the Company actively seeks to grow its option backlog as options represent a significant source of potential orders for the Company, there can be no assurance that customers will continue to exercise such options at the same rate or at all in the future. In addition, customer contracts in the heavy-duty transit bus industry generally give transit authorities the right to terminate the contract for convenience (or without any reason). As such, customers may, without notice, terminate their relationship with the Company during the term of the contract. Any loss of customers, or decrease in the volume purchased or price paid by them for products, could have a material adverse effect on the Company's business, financial condition, liquidity and operating results.

***United States content bidding preference rules may create a competitive disadvantage***

New legislation passed in late 2011 in the State of California permits California agencies to grant bidding preference to a bidder based on the amount by which the buses it is proposing exceed the minimum United States content requirements under the United States federal “Buy America” regulations. Although management does not believe that the US content of competitors’ buses is materially different from the US content of the Company’s buses, no such data is publicly available and there can be no assurance that competitor’s buses don’t contain a materially higher percentage of US content than the Company’s buses. If this occurs, it may create a competitive bidding advantage for such competitors in the State of California under procurements utilizing these bid preference rules. If this materially limits the Company’s ability to win awards it may have an adverse effect on the Company’s business, financial condition, liquidity and operating results. See “Description of the Business — Legal and Regulatory Matters — United States Content Bidding Preference”.

***Current requirements under “Buy America” legislation may change and/or become more onerous or suppliers’ “Buy America” content may change***

Manufacturers of new buses must comply with “Buy America” legislation in order for new bus purchases to qualify for United States federal funding. “Buy America” legislation requires that buses purchased with federal funds contain a minimum of 60% United States content by cost and that final assembly take place in the United States. There can be no assurance that these “Buy America” requirements will not change and/or become more onerous. In early 2011, a bill was introduced in the United States House of Representatives to require that buses purchased with federal funds contain a minimum of 80% United States content by cost for 2012, with United States content increasing to 100% in 2013 and future years. This bill was not enacted. In early 2012, an amendment to a pending transportation reauthorization bill that would increase United States content requirements for heavy duty transit buses from 60 to 100% over a five-year period was also unsuccessfully proposed. The same or similar attempts to amend the transportation reauthorization bill may be renewed. In addition, should “Buy America” requirements become less stringent, foreign competitors without significant U.S. operations may be able to penetrate the United States market and gain market share. Also, suppliers may change the source of the components or subcomponents comprising their products thereby potentially reducing the “Buy America” content of their products. Any changes in U.S. Buy America legislation or the reduction of “Buy America” content of suppliers’ products may have a material adverse effect on the Company’s business, financial condition, liquidity and operating results. See “Description of the Business — Legal and Regulatory Matters — Rules of Origin (Buy America) Legislation”.

***Current requirements under the Ontario government’s or Canadian transit agencies’ Canadian content policy may change and/or become more onerous***

Manufacturers selling new buses to transit customers in Ontario, Canada that use provincial funding to purchase such buses must comply with the Ontario government policy requiring that such transit vehicles must contain a minimum 25% Canadian content by cost. There can be no assurance that these “Canadian content” requirements will not change and/or become more onerous or that other provinces or transit agencies (such as transit agencies in Quebec or the TTC) will adopt or enact similar or more onerous policies or legislation that have similar effect. Many major and/or high-cost components such as engines, axles, transmissions, heating and air conditioning units, seats, are not manufactured in Canada and are not considered “Canadian content” in accordance with these policies. In the event that the “Canadian content” requirement increases or additional components or subcomponents cannot be sourced in Canada, the Company may not be able to comply with the policy requirements and will not be able to sell buses to customers to which these policies apply. This may have a material adverse effect on the Company’s business, financial condition, liquidity and operating results. See “Description of the Business – Legal and Regulatory Matters – Ontario Policy Regarding Canadian Content” and

“Description of the Business – Legal and Regulatory Matters – Policy of the Toronto Transit Commission”.

***Production delays may result in liquidated damages under the Company’s contracts with its customers***

Bus manufacturing contracts in the heavy-duty transit bus industry typically include liquidated damages provisions that result in monetary penalties on a per bus per day basis when buses are not delivered to the customer by the deadline specified in the contract. Although the Company actively manages such deadlines, the Company may incur monetary penalties as a result of production interruptions or otherwise, and such monetary penalties may have a material adverse effect on the Company’s business, financial condition, liquidity and operating results.

***Currency fluctuations could adversely affect the Company’s financial results or competitive position***

The Company reports its results in United States dollars. Fluctuations in the exchange rate between the United States dollar and Canadian dollar will affect the Company’s reported results. However, the impact of changes in foreign exchange rates on the Company’s reported results differs over time depending on whether the Company is generating a net cash inflow or outflow of Canadian dollars. This is largely dependent on the Company’s revenue mix by currency as operating costs denominated in Canadian dollars have been relatively stable on a per equivalent unit basis. During 2013 the Company generated a net cash inflow of Canadian dollars. During 2014, based on production plans as of the date hereof, management expects the Company to generate a net Canadian dollar inflow. In addition, the Company competes with United States manufacturers and may be less competitive as the Canadian dollar strengthens relative to the United States dollar. To the extent the Company has borrowings that are denominated in Canadian dollars, its results of operations are also negatively affected by a strengthening in the Canadian dollar compared to the United States dollar.

***The Company may not be able to maintain performance bonds or letters of credit required by its contracts or obtain performance bond and letters of credit required for new contracts***

Many municipalities and local transit authorities require suppliers to obtain performance bonds from surety companies or letters of credit to ensure that suppliers will perform under purchase agreements. In 2013, approximately 28% of bus manufacturing contracts tendered performance guarantees, with an average guarantee rate of approximately 10% of the value of the contract. The surety bonding market does not provide for committed bonding facilities. Surety companies provide limits on the maximum facility they will provide. Surety companies issue bonds on an as-needed basis and take into account current financial performance and the state of the surety market in making their credit decisions. In order to ensure continued performance guarantee availability, the Company has entered into a letter of credit sub-facility as part of its Credit Facility in order to have letters of credit issued to either backstop surety bonds or directly to municipalities and local transit authorities. There can be no assurance that the Company’s customers will not require additional performance security in the future or that either letters of credit or performance bonds will continue to be available to the Company as security for performance of its contracts or, if available, on favourable terms (including cost) to the Company. If the amount of performance security the Company is required to provide significantly increases or if adequate performance security is not available or if the terms or costs of such security are too onerous, the Company may lose existing contracts and may not be able to bid on many new contracts, which could result in a material adverse effect on the Company’s business, financial condition, liquidity and operating results. See “Description of the Business — Bonding Requirements”.

### ***Third party debt service obligations may have important consequences to the Company***

The Company has third party debt service obligations under the Credit Facility, the Debenture and other agreements with third parties. The degree to which the Company is leveraged could have important consequences to investors, including: (i) a portion of the Company's cash flow from operations will be dedicated to the payment of the principal of and interest on the indebtedness, thereby reducing funds available for future operations and distribution to investors, (ii) certain of the Company's borrowings are at variable rates of interest, which exposes the Company to the risk of increased interest rates, and (iii) the Company's ability to obtain additional financing for working capital, capital expenditures or acquisitions in the future may be limited. The Company's ability to make scheduled payments of principal and interest on, or to refinance, its indebtedness will depend on its future operating performance and cash flow, which are subject to prevailing economic conditions, prevailing interest rate levels, and financial, competitive, business and other factors, many of which are beyond its control. These factors might inhibit the Company from refinancing the indebtedness under the Credit Facility and other agreements at maturity.

### ***Interest rates could change substantially, materially impacting the Company's profitability***

The Company's borrowings under the Credit Facility are at variable rates of interest and expose the Company to interest rate risk. The Company's attempts to mitigate this risk through interest rate hedges or swaps could become materially more expensive if interest rates increase or become more volatile. If the cost of hedging interest rates increases, the Company's debt service obligations on its variable rate indebtedness would increase even though the amount borrowed remained the same, and the Company's net income and cash available for servicing its other indebtedness would decrease. The Company has entered into an interest rate swap until April, 2017, which fixes the interest rate on \$142 million of the term Credit Facility at 1.46% plus the applicable interest margin.

### ***The Company may not be able to generate the necessary amount of cash to service its existing debt, which may require the Company to refinance its debt***

The Company's ability to pay principal and interest on its Credit Facility, the Debenture and other debt obligations will depend on its future financial performance. The Company's ability to generate cash will depend on many factors, some of which may be beyond its control, including general economic, financial and regulatory conditions. Other factors may also cause a lower amount of cash to be generated such as an increase in work in process as a result of production or supply issues. If the Company cannot generate enough cash flow in the future to service its debt, it may need to refinance all or a portion of its debt, obtain additional financing (on terms that may be less favourable than existing financing terms) or sell assets. The Company might not be able to implement any of these strategies on satisfactory terms or on a timely basis, if at all. If the Company is unable to meet its debt service obligations or comply with its covenants, a default under its debt agreements would result.

### ***Availability of future financing***

Management expects that the Company's principal sources of funds will be cash generated from its operating activities and borrowing capacity remaining under the Credit Facility and/or from future securities offerings. Management believes that these funds will provide the Company with sufficient liquidity and capital resources to meet its current and future financial obligations, as well as to provide funds for its financing requirements, capital expenditures and other needs for the foreseeable future. Despite management's expectations, however, the Company may require additional equity or debt financing to meet its financing requirements. This financing may not be available when required or may not be available on commercially favorable terms or on terms that are otherwise satisfactory to the Company. The Credit Facility matures in April, 2017. While the Company expects to be able to refinance

the Credit Facility prior to its maturity, if Company is unable to successfully refinance its Credit Facility, the Company may not have sufficient liquidity and capital resources to meet its financial obligations.

***Dependence on limited sources or unique sources of supply***

The Company does not typically enter into long-term agreements with its suppliers, but rather purchases supplies on an order-by-order basis depending on the material requirements to build customers' buses. Certain raw materials and components used in the heavy-duty transit bus manufacturing industry are obtained from a limited group of suppliers. In some cases, there is only a single source of supply of components to the industry, such as engines. In other cases, such as the supply of transmissions, axles, heating and air conditioning units and fiberglass and structural steel tubing, the Company's raw materials and components are not readily available from alternative sources of supply, may be available in limited supply or a particular supplier may be specified by a customer and such supplier may have limited or no supply of such raw materials or components. The Company's reliance on a sole supplier, limited groups of suppliers or raw materials and components that may be available in limited supply and purchasing components from suppliers that have been specifically named by customers involves several risks, including increased risk of inability to obtain adequate supplies (due to accidents, strikes, shortage of raw materials or other events affecting a supplier, including a supplier discontinuing to supply a product or a component), costs arising from poor quality of the materials or components supplied, increased risk of being forced to suspend production of certain of its products, and reduced control over pricing and timely delivery. Although the availability, timeliness, quality and pricing of deliveries from the Company's suppliers have historically been acceptable and although management believes that additional sources of supply should be available on an acceptable basis, there are no assurances that this dependence on a sole supplier or a limited group of suppliers or on certain raw materials and components that may be available in limited supply will not have a materially adverse effect on the Company's business, financial condition, liquidity and operating results.

***The Company's profitability can be adversely affected by increases in raw material and component costs***

Raw materials and components represent a significant majority of the Company's production cost structure. The Company's operating results may be affected by the cost of carbon and stainless steel, aluminum, copper, resins and oil-based products that are the primary raw material and component inputs for its products. Although certain raw material and component prices may be fixed on a quarterly basis, or for longer periods if possible, in the Company's contracts with its suppliers, if raw material or component prices increase significantly, there may be a resulting increase in the Company's supply costs and it may not be able to pass on these higher costs to its customers and the Company's profit margins could be materially adversely affected. Increases in the prices paid for raw materials and components, particularly in situations where prices under multi-year bus purchase contracts have been quoted to customers as firm and fixed, could also impair the Company's ability to compete and have a material adverse effect on the Company's business, financial condition, liquidity and operating results.

***Dependence on supply of engines that comply with emission regulations***

The United States EPA mandated additional stringent emission standards that were phased in for 2013. To the knowledge of management, only one engine manufacturer sells diesel engines that comply with these new emissions requirements for use in heavy-duty transit buses in North America. The failure of this sole engine manufacturer (or any new engine supplier that may enter the transit bus engine market) to supply the heavy-duty transit industry with engines that comply with current emissions standards will have a material adverse effect on the Company's business, financial condition, liquidity and operating results.

Effective January 1, 2014, the California ARB requires a dual certification for emission compliance for engines used in a hybrid configuration. This requires separate certifications from the engine supplier as well as the hybrid system supplier. There is currently no indication when or if the hybrid system suppliers will be able to achieve this certification. As a result, transit bus manufacturers are currently not able to supply buses in California or in Pennsylvania (one of the states that follow the ARB regulations) with a diesel - hybrid electric engine configuration. All other states that follow ARB regulations have provided an exemption from these regulations for urban transit buses. Unless this certification requirement is waived or until it can be achieved by the suppliers, transit agencies in these three states will need to purchase or convert options to diesel or CNG powered buses. Although the current impact to New Flyer's planned production in 2014 is not material, if the ARB regulations are implemented on a wider basis in the United States and no waiver is provided or suppliers are unable to provide the required certifications, the Company will not be able to sell hybrid propulsion systems in such ARB states. Such limitations, depending on their scope and on the availability of alternative propulsion system options and the willingness or ability of customers to purchase buses with such alternative propulsion systems, may have a material adverse effect on the Company's business, financial condition, liquidity and operating results.

### ***Acquisition risk***

The Company will continue to identify, develop and acquire suitable acquisition targets in pursuit of its strategic plans and to diversify and grow. While management intends to be careful in selecting businesses to acquire, acquisitions inherently involve a number of risks, including, but not limited to, the possibility that the Company pays more than the acquired assets are worth; the additional expense associated with completing an acquisition; the difficulty of assimilating the operations and personnel of the acquired business; the challenge of implementing uniform standards, controls procedures and policies throughout the acquired business; the inability to integrate, train, retain and motivate key personnel of the acquired business; the potential disruption to the Company's ongoing business and the distraction of management from the Company's day-to-day operations; the inability to incorporate acquired businesses successfully into the Company's existing operations; and the potential impairment of relationships with the Company's employees, suppliers and customers. If any one or more of such risks materialize, they could have a material adverse effect on the Company's business, financial condition, liquidity and operating results.

In addition, the Company may not be able to maintain the levels of operating efficiency that the acquired company had achieved or might have achieved had it not been acquired by the Company. Successful integration of the acquired company's operations would depend upon the Company's ability to manage those operations and to eliminate redundant and excess costs. As a result of difficulties associated with combining operations, the Company may not be able to achieve the cost savings and other benefits that it would hope to achieve with the acquisition. Any difficulties in this process could disrupt the Company's ongoing business, distract its management, result in the loss of key personnel or customers, increase its expenses and otherwise materially adversely affect the Company's business, financial condition, liquidity and operating results.

Further, inherent in any acquisition there is risk of liabilities and contingencies that the Company may not discover in its due diligence prior to the consummation of a particular acquisition, and the Company may not be indemnified for some or all of these liabilities and contingencies. The discovery of any material liabilities or contingencies in any acquisition could also have a material adverse effect on the Company's business, financial condition, liquidity and operating results.

### ***Joint Ventures***

The Company has entered into a long-term joint venture with Alexander Dennis and may, in the future, enter into other joint venture arrangements. The Company is subject to the risks normally associated with the conduct of joint ventures and having strategic partners, which include:

- disagreement with the partners on how to develop, operate or finance the Company's joint venture activities;
- that the partners may at any time have economic or business interests or goals that are, or become, inconsistent with the Company's business interests or goals;
- that the partners may not comply with the agreements governing the Company's relationship with them;
- disagreement with the partners over the exercise of their respective rights under the agreements governing the relationship;
- that the partners may be in a position to take action contrary to the Company's instructions, requests, policies, objectives or interests;
- the possibility that partners may become insolvent or bankrupt; and
- possible litigation with the partners over joint venture or strategic matters.

These risks could result in legal liability and affect NFI's ability to develop the Company's joint ventures or strategic initiatives. Any failure of partners to meet their obligations to the Company or to third parties, any disagreements and disputes with respect to the parties' respective rights and obligations, or the occurrence of any of the other risks described above could have a material adverse effect on the Company's ability to successfully pursue joint ventures and strategic initiatives, which could have a material adverse effect on the Company's business, financial condition, liquidity and operating results.

### ***Development and testing of new products***

The Company may not be able to successfully design, develop or test new products (for example, the New Flyer MiDi<sup>®</sup>) or improvements to existing products (for example Xtended Life<sup>™</sup> products) in order to effectively compete with competitors. There may be no demand by customers to purchase newly developed or improved products, there may be risks and unbudgeted costs associated with launching a new product into the market place and the Company may not be able to recoup research and development costs, all of which may be material. In addition, there may be material and unforeseen warranty costs related to new products that management did not foresee or adequately price into the bus purchase contracts for such products. Further, there may be no testing facilities available to test the Company's new products to certain governmental or customer requirements, standards or specifications.

### ***Development of competitive products or technology***

The Company may not be able to prevent a competitor from copying its new and existing products or technologies. If a competitor copies the Company's products or develops an equivalent or superior product or technology, there could be a material adverse effect on the Company's financial condition and results of operations and the amount of cash available for distribution to investors. If a competitor develops a superior product or technology, there can be no assurance that the Company would be able to

manufacture a similar or competitive new product or technology and/or effectively compete with manufacturers developing such products or technologies.

***The Company's operations are subject to risks and hazards that may result in monetary losses and liabilities not covered by insurance or which exceed its insurance coverage***

The Company's business is generally subject to a number of risks and hazards, including pollution and other environmental risks and changes in the regulatory environment. Although the Company maintains general liability insurance and property and business interruption insurance, because of the nature of its industry hazards, it is possible that liabilities for occurrences such as pollution, property and equipment damage or injury or loss of life arising from a major or unforeseen occurrence may not be covered by the Company's insurance policies or could exceed insurance coverages or policy limits. Further, insurance may not be available to the Company at reasonable rates in the future. Any significant interruption in its operations could materially adversely affect the Company's business, financial condition, liquidity and operating results.

***The Company may be adversely affected by rising insurance costs***

The Company's cost of maintaining liability, personal injury, property damage and workers' compensation insurance is significant. The Company could experience materially higher insurance premiums as a result of adverse claims experience or because of general increases in premiums by insurance carriers for reasons unrelated to its own claims experience. Generally, the Company's insurance policies must be renewed annually. The Company's ability to continue to obtain insurance at affordable premiums and reasonable deductibles or self-insured retentions also depends upon its ability to continue to operate with an acceptable safety record. A significant increase in the number or value of claims against the Company, the assertion of one or more claims in excess of its policy limits or the inability to obtain adequate insurance coverage for reasonable premiums, with reasonable deductibles or self-insured retentions or at acceptable levels, or at all, could have a material adverse effect on the Company's business, financial condition, liquidity and operating results.

***Dependence on management information systems***

The Company depends on its management information systems in each stage of the manufacture and sale of its products, including entering the customer's order, setting the production schedule, planning material and supply requirements, controlling manufacturing activities and providing aftermarket parts and support. In addition, its management information systems form the basis of its financial reporting. In the event that irreparable damage were to be caused to its information systems and databases (including to its back-up systems) or that the information contained in its management information systems were lost or could not be accessed in a timely manner, there could be a material adverse effect on the Company's business, financial condition, liquidity and operating results.

***The Company may be subject to claims and liabilities under environmental, health and safety laws***

The Company operates in a highly regulated environment. Its facilities and operations are subject to extensive and constantly evolving federal, provincial, state and local environmental and health and safety laws, including laws governing emissions or discharges into soil, water and air, including noise and odours, which could result in remediation obligations, the generation, use, handling, storage, transportation and disposal of regulated substances, and health and safety matters.

The Company is required to have and make certain governmental permits, approvals and registrations related to environmental and health and safety matters. Permits or approvals may be subject to denial, revocation or modification depending on the particular circumstances. Failure to obtain or comply with

the conditions of such permits or approvals may adversely affect operations and may also subject the Company to penalties. In addition, the Company may be required to obtain additional permits or approvals, which may result in material costs, including capital expenditures. There can be no assurance that the Company will be able to meet all applicable regulatory requirements without incurring such additional costs.

The Company may incur substantial costs to comply with environmental and health and safety law requirements. The Company may also incur substantial costs for liabilities arising from past releases of, or exposure to regulated substances. In addition, the Company may discover currently unknown environmental problems or conditions. There can be no assurance that the Company's continued compliance with environmental and health and safety laws, the discovery of currently unknown environmental problems or conditions, changes in environmental and health and safety laws or increased enforcement of same, or other unanticipated events, will not give rise to claims that may involve material expenditures by or liabilities for the Company.

Complying with environmental and health and safety laws has added and will continue to add to the Company's operating costs. While the Company believes that it is in compliance in all material respects with such laws, there can be no assurance that it will not be materially impacted by costs, liabilities or claims with respect to its operations under existing laws or those that may be adopted in the future, or increased enforcement of same. If the present level of price competition continues, it may become increasingly difficult for the Company and other manufacturers of heavy-duty transit buses to recover such costs and, accordingly, lower margins may result.

***The Company may incur costs in connection with provincial, state or federal regulations relating to axle weight restrictions and bus lengths***

The Company is required, in its customer contracts, to comply with applicable provincial, state and federal regulatory requirements. Certain models and types of the Company's buses do not currently comply with regulations governing maximum axle weight or maximum length in certain jurisdictions. The Company may incur material costs as a result of product warranty or contractual claims as a result of existing buses or new buses that are manufactured and that do not comply with local axle weight or length standards. To date, only a few of New Flyer's customers have required that the Company reconfigure its buses to comply with local axle weight regulations. The Company may incur material costs in the future if it is required to redesign new buses to comply with axle weight or length standards.

There can also be no assurance that government weight regulations or restrictions will not change and/or become more onerous such that the Company's buses would not comply with such more onerous regulations. If the Company is unable to design buses that comply with such new weight requirements it will not be able to sell buses to customers whose vehicles are governed by such laws, which depending on the volume of buses typically sold by the Company in that area, may have a material adverse effect on the Company's business, financial condition, liquidity and operating results.

***Catastrophic events may lead to production curtailments or shutdowns***

The Company's facilities are subject to the risk of catastrophic loss due to unanticipated events such as floods, fires, explosions or violent weather conditions. Unexpected interruptions in the Company's production capabilities would adversely affect its productivity and results of operations. Some customer contracts do not have force majeure provisions and if there are unexpected interruptions or long-term disruptions to the production and delivery of buses due to catastrophic losses or unanticipated events, liquidated damages payable to customers may be significant. Moreover, any interruption in production capability may require the Company to make significant capital expenditures to remedy the problem, which would reduce the amount of cash available for its operations. The Company's insurance may not

cover its losses. In addition, longer-term business disruption could harm the Company's reputation and result in a loss of customers. The occurrence of any of these events could materially adversely affect the Company's business, financial condition, liquidity and operating results.

### ***Operational Risk***

The Company is exposed to many types of operational risks that affect all companies. Such risks include the risk of misconduct or fraud by employees or others, unauthorized transactions by employees, operational or human error or not having sufficient levels or quality of staffing resources to successfully achieve the Company's strategic or operational objectives. Operational risk is the risk of loss resulting from inadequate or failed internal processes, people and/or systems or from external events. Operational risk is present in all of the Company's business activities, and incorporates exposure relating to fiduciary breaches, regulatory compliance failures, legal disputes, business disruption, pandemics, technology failures, processing errors, business integration, theft and fraud, damage to physical assets, employee safety and insurance coverage. The occurrence of an event caused by an operational risk that is material could have a material adverse effect on the Company's business, financial condition, liquidity and operating results.

### ***Internal controls over financial reporting***

Management is responsible for establishing and maintaining internal controls over financial reporting ("ICFR"), as defined under rules adopted by the Canadian Securities Administrators. ICFR were designed under the supervision of, and with the participation of, the President and Chief Executive Officer ("CEO") and the Chief Financial Officer ("CFO"). The Company's ICFR are designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with IFRS. Management, under the supervision of the CEO and CFO, evaluated the design of the Company's ICFR as of December 29, 2013 in accordance with the criteria established in Internal Control - Integrated Framework (1992) issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO), and concluded that the Company's ICFR is effective.

The Company has limited its design of ICFR to exclude controls, policies and procedures of NABI, as it was acquired not more than 365 days before the end of the financial period ending December 29, 2013.

ICFR, no matter how well designed, have inherent limitations. Therefore, ICFR can provide only reasonable assurance with respect to financial statement preparation and may not prevent or detect all misstatements.

### ***Disclosure controls***

Management is responsible for establishing and maintaining disclosure controls and procedures in order to provide reasonable assurance that material information relating to the Company is made known to them in a timely manner and that information required to be disclosed is reported within time periods prescribed by applicable securities legislation. There are inherent limitations to the effectiveness of any system of disclosure controls and procedures, including the possibility of human error and the circumvention or overriding of the controls and procedures. Accordingly, even effective disclosure controls and procedures can only provide reasonable assurance of achieving their control objectives. The Company has limited its design of disclosure controls and procedures to exclude controls, policies and procedures of NABI, as it was acquired not more than 365 days before the end of the financial period ending December 29, 2013. The Company's CEO and CFO have concluded that disclosure controls and procedures as at December 29, 2013 were effective.

## Risks Related to the Capital Structure

### U.S. IRS Circular 230 Disclosure

**TO ENSURE COMPLIANCE WITH U.S. INTERNAL REVENUE SERVICE CIRCULAR 230, HOLDERS OF SHARES OR DEBENTURES ARE HEREBY NOTIFIED THAT: (A) ANY DISCUSSION OF U.S. FEDERAL TAX ISSUES IN THIS COMMUNICATION IS NOT INTENDED OR WRITTEN TO BE USED OR RELIED UPON, AND CANNOT BE USED OR RELIED UPON BY SUCH HOLDERS, FOR THE PURPOSE OF AVOIDING PENALTIES THAT MAY BE IMPOSED ON SUCH HOLDERS UNDER THE CODE; AND (B) EACH HOLDER OF SHARES OR DEBENTURES SHOULD SEEK ADVICE BASED ON ITS PARTICULAR CIRCUMSTANCES FROM AN INDEPENDENT TAX ADVISOR.**

#### *NFI is dependent on its subsidiaries for all cash available for distributions*

NFI is dependent on the operations and assets of its subsidiaries. Cash distributions to the holders of Shares and Debentures will be dependent on the ability of NFI's subsidiaries to make dividend payments on their shares. The actual amount of cash available for distribution to holders of the Shares or Debentures will depend upon numerous factors relating to the business of the Company, including profitability, changes in revenue, fluctuations in working capital, capital expenditure levels, applicable laws, compliance with contracts and contractual restrictions contained in the instruments governing any indebtedness. Any reduction in the amount of cash available for distribution, or actually distributed, by NFI's subsidiaries will reduce the amount of cash available to NFI to pay dividends on the Shares and make payments to holders of Debentures. While NFI is contractually obligated to make interest payments on the Debentures, cash dividends by NFI on the Shares are not guaranteed and will fluctuate with the performance of the business of NFI subsidiaries.

#### *A significant amount of the Company's cash is distributed, which may restrict potential growth*

Historically, substantially all of the Company's cash generated from operations has been distributed to investors in the form of dividends on the Shares interest payments on the Debentures and previously, interest payments on the Subordinated Notes. While the distributions to investors have decreased in connection with the Common Share Conversion, a large portion of the Company's cash flow is expected to continue to be distributed to investors in the form of dividends on the Shares and interest on the Debentures until they remain outstanding. Accordingly, to the extent such distributions are made, the Company's ability to make additional capital and operating expenditures and finance acquisitions would be limited which could restrict the Company's growth.

#### *Payment of dividends is not guaranteed*

NFI and its subsidiaries may alter their dividend policies and dividends from these companies, if any, will depend on, among other things, the results of operations, cash requirements, financial condition, contractual restrictions, business opportunities, provisions of applicable law and other factors that the board of directors of each of NFI and its subsidiaries may deem relevant. The directors of these entities, in their discretion, may decrease the level of dividends provided for in their existing dividend policies or discontinue dividends entirely. The Credit Facility contains significant restrictions on NFI's ability to make dividend payments. The payment of dividends is also subject to certain limitations under applicable laws.

***Fluctuations in the exchange rate may impact the amount of cash available to the Issuer for distribution***

Dividends to holders of Shares are denominated in Canadian dollars. Conversely, the interest payments on the Debentures and a significant portion of the Company's revenue and expenses are denominated in U.S. dollars. As a result, the Issuer is exposed to currency exchange rate risks. Changes in the currency exchange rate between U.S. and Canadian dollars could have a material adverse effect on the Company's consolidated financial condition, results of operations and cash flow and may adversely affect the Issuer's cash distributions to investors.

The Company generates cash flows and earns income in both Canadian dollars and U.S. dollars in the ordinary course. The currency mix of cash flows and earnings depends on the geographic source of orders for heavy-duty transit buses and production and other costs and other factors which vary from period to period. As a result, the Company is exposed to fluctuations in the exchange rate between the Canadian dollar and the U.S. dollar. The distributions that NF Holdings will make to NFI on the shares of NF Holdings will be paid in Canadian dollars. Based on production plans as of the date hereof and management's estimates of the Company's Canadian dollar revenues and expenses and resulting cash flows through the end of 2014, management expects the Company to generate a net Canadian dollar inflow. The Company will have temporary surpluses and deficits of Canadian dollar cash flows from time to time during this period. The Company intends to implement an active hedging strategy to minimize the effects of these fluctuations during this period. However, there can be no assurance that the Company will be able to successfully implement this hedging strategy and actual revenues, expenses and resulting cash flows may vary from management's estimates and such variance may be material.

The Company reviews its currency hedging policy on an ongoing basis.

***The Company's substantial consolidated indebtedness could negatively impact the business***

The Company has a substantial amount of indebtedness. As at December 29, 2013, the Company has total third party indebtedness of US\$242 million. In addition, the Credit Facility and the Indenture permits future further indebtedness provided that certain covenants are satisfied.

The degree to which the Company is leveraged on a consolidated basis could have important consequences to the holders of Shares and Debentures, including:

- the Company's ability in the future to obtain trade credit from vendors, performance bonds from surety companies or additional financing for working capital, capital expenditures or other purposes may be limited;
- the Company may be unable to refinance indebtedness on terms acceptable to it or at all;
- a significant portion of the Company's cash flow (on a consolidated basis) is likely to be dedicated to the payment of the principal of and interest on the Company's indebtedness, including the Debentures, thereby reducing funds available for future operations, capital expenditures and/or dividends on the Shares;
- the Company may be more vulnerable to economic downturns and be limited in its ability to withstand competitive pressures;
- the Company may be limited in its ability to plan for or react to changes in its business or the industry in which it operates; and

- the Company may be at a competitive disadvantage to its competitors that have less indebtedness.

***NFI may not be able to repurchase the Debentures upon a change of control as required by the Indenture***

Upon the occurrence of certain specific kinds of change of control events, NFI will be required to offer to purchase outstanding Debentures at their principal amount plus accrued and unpaid interest, if any, to the date of purchase. However, it is possible that NFI will not have sufficient funds at the time of the change of control to make the required purchase or that restrictions contained in other indebtedness will restrict those purchases. Failure to make an offer to purchase the Debentures would constitute a default under the Indenture, which might constitute a default under the terms of NFI's other indebtedness at that time.

If a holder of Debentures converts its Debentures in connection with a Cash Change of Control that occurs, NFI may, in certain circumstances, be required to increase the conversion rate pursuant to the terms of the Indenture. While the increased conversion rate is designed to compensate a holder of Debentures for the lost option time value of its Debentures as a result of a Cash Change of Control in certain circumstances, the increased conversion rate amount is only an approximation of such lost value and may not adequately compensate the holder for such loss. In addition, in some circumstances as described in the Indenture, no adjustment will be made.

***Changes in the Issuer's creditworthiness may affect the value of the Shares and the Debentures***

The perceived creditworthiness of the Issuer may affect the market price or value and the liquidity of the Shares and the Debentures.

***Payments to holders of the Debentures are subordinated in right of payment to existing and future Senior Indebtedness and will depend on the financial health of NFI and its creditworthiness***

The likelihood that holders of the Debentures will receive payments owing to them under the terms of the Debentures will depend on the financial health of NFI and its creditworthiness. In addition, the Debentures are unsecured obligations of NFI and are subordinate in right of payment to all NFI's existing and future Senior Indebtedness (as defined under the Indenture). Therefore, if NFI becomes bankrupt, liquidates its assets, reorganizes or enters into certain other transactions, NFI's assets will be available to pay its obligations with respect to the Debentures only after it has paid all of its Senior Indebtedness in full. There may be insufficient assets remaining following such payments to pay amounts due on any or all of the Debentures then outstanding. The Debentures are also effectively and structurally subordinate to claims of creditors (including trade creditors) of NFI's subsidiaries. The Indenture does not prohibit or limit the ability of NFI or its subsidiaries to incur additional debt or liabilities (including Senior Indebtedness) or to make distributions on the Shares. The Indenture does not contain any provision specifically intended to protect holders of Debentures in the event of a future leveraged transaction involving NFI.

***Debentures may be redeemed by NFI prior to maturity***

The Debentures may be redeemed, at the option of NFI, on and after June 30, 2015 and prior to maturity at any time and from time to time subject to certain conditions. Holders of Debentures should assume that this redemption option will be exercised if NFI is able to refinance at a lower interest rate or it is otherwise in the interest of NFI to redeem the Debentures.

***Conversion of the Debentures following certain transactions could lessen or eliminate the value of the conversion privilege associated with the Debentures***

In the case of certain transactions, each Debenture may (i) become convertible into the securities, cash or property receivable by a holder of Shares based on the number of Shares into which the Debenture was convertible immediately prior to the transaction, or (ii) become convertible into certain prescribed securities with limited liquidity. These changes could substantially lessen or eliminate the value of the conversion privilege associated with the Debentures in the future and result in the receipt of illiquid securities and thereby have a material adverse effect on the value of the Debentures.

***Prevailing yields on similar securities will affect the market value of the Debentures***

Prevailing yield on similar securities will affect the market value of the Debentures. Assuming all other factors remain unchanged, the market value of the Debentures will decline as prevailing yields for similar securities rise, and will likely increase as prevailing yields for similar securities decline.

***Redemption by NFI of the Debentures for Shares may result in possible dilution to holders of Shares***

NFI may determine to redeem outstanding Debentures for Shares or to repay outstanding principal amounts and interest owing thereunder at maturity of the Debentures by issuing additional Shares. Accordingly, holders of Shares may suffer dilution.

***Fluctuations in the exchange rates between the U.S. dollar and the Canadian dollar could impact the number of Shares issuable in certain circumstances***

The Debentures are denominated in U.S. dollars; however, the Shares issuable on conversion of the Debentures trade on the TSX in Canadian dollars. Subject to certain conditions set forth in the Indenture, NFI has the option to repay the principal amount of Debentures or to pay the interest on the Debentures by issuing Shares. Fluctuations in the exchange rates between the U.S. dollar and the Canadian dollar could impact the number of Shares issuable in such circumstances.

***The restrictive covenants in the Credit Facility could impact the Company's business and affect its ability to pursue its business strategies***

The Credit Facility features restrictive covenants that limit the Company's ability, among other things, to:

- incur additional indebtedness;
- pay dividends and make distributions in respect of equity interests or to make certain other restrictive payments or investments;
- sell assets;
- consolidate, merge, sell or otherwise dispose of all or substantially all of the Company's assets;
- enter into transactions with the Company's affiliates;
- create liens; and

- enter into new lines of businesses.

In addition, the Credit Facility includes other and more restrictive covenants and prohibits the Company and certain of its affiliates from prepaying its other indebtedness, including the Debentures, while debt under the Credit Facility is outstanding. The Credit Facility also requires the Company to achieve specified financial and operating results and maintain compliance with specified financial ratios. The Company's ability to comply with these ratios may be affected by events beyond its control.

A breach of any of the restrictive covenants in the Credit Facility or in the Company's ability to comply with the required financial ratios could result in a default under the Credit Facility. If a default occurs, the lenders under the Credit Facility may elect to declare all borrowings outstanding under that facility together with accrued interest and other fees, to be immediately due and payable.

### ***Investment Eligibility and Canadian Federal Income Tax Risks***

There can be no assurance that the Shares and the Debentures will continue to be qualified investments for trusts governed by registered retirement savings plans, registered retirement income funds, deferred profit sharing plans, registered education savings plans, registered disability savings plans and tax-free savings accounts (collectively, "Registered Plans") under the Tax Act. The Tax Act imposes penalties for the acquisition or holding of non-qualified or ineligible investments in Registered Plans.

Effective January 1, 2010, the fifth protocol to the Canada-United States Income Tax Convention (1980), which entered into force on December 15, 2008, increased the Canadian withholding on dividends paid or credited or deemed to be paid or credited to Transit Holdings from NFI ULC from 5% to 25%. The increased withholding tax on dividends paid by NFI ULC to Transit Holdings could reduce the amount of cash otherwise available for the payment of dividends by NFI on its Shares. However, based on its future financial projections, management believes that the increased US federal tax credit expected to result from any increased Canadian withholding tax on dividends paid by NFI ULC to Transit Holdings would likely offset over a period of several years the impact of the increased withholding tax.

### ***Future sales or the possibility of future sales of a substantial amount of Shares or Debentures may impact the price of the Shares and the Debentures and could result in dilution***

Future sales, or the possibility of future sales, of a substantial amount of Shares or Debentures in the public market could adversely affect the prevailing market price of the Shares and the Debentures and could impair the Issuer's ability to raise capital through future sales of those securities. Additionally, the issuance of additional Shares or Debentures may dilute an investor's investment in the Issuer and reduce distributable cash per Share.

The Issuer may issue Shares and Debentures, or other securities from time to time in order to raise capital or as consideration for future acquisitions and investments. If an acquisition or investment is significant, the number of Shares and/or the aggregate principal amount of Debentures, or the number or aggregate principal amount, as the case may be, of other securities that may be issued may in turn be significant. In addition, the Issuer may also grant registration rights covering those Shares, Debentures or other securities in connection with any acquisitions or investments.

***Certain U.S. tax rules may limit the ability of the Issuer and the affiliated group of corporations joining in filing a consolidated tax return for U.S. federal income tax purposes with NF Holdings as the common parent (the “NF Group”) to deduct interest expense for U.S. federal income tax purposes and may increase the NF Group’s tax liability***

Under certain circumstances, Code section 163(j) limits a corporation’s deductions for interest paid to related foreign persons exempt from U.S. tax or for interest paid on debt that is guaranteed by a related foreign person. The terms of the Credit Facility provide that NFI is a guarantor. Thus, the NF Group’s interest deductions may be limited with respect to the Credit Facility, which may result in an increase in the NF Group’s U.S. federal income tax liability. In addition, the NF Group’s interest deductions may be limited under Code section 163(j) with respect to indebtedness owed by NFI ULC to NFI, and a sale-repurchase obligation that is treated for U.S. federal income tax purposes as indebtedness of a U.S. subsidiary owed to NFI (which indebtedness and sale-repurchase obligation amounted to \$60 million as of December 29, 2013). Any such limitation would result in an increase in the NF Group’s U.S. federal income tax liability. In each case, any such increase would adversely affect the Company’s financial position, cash flow and liquidity.

***An ownership change may limit the NF Group’s ability to use certain losses for U.S. federal income tax purposes and may increase the NF Group’s tax liability***

An ownership change may limit the ability of NF Group to use certain losses for U.S. federal income tax purposes and may increase the NF Group’s tax liability.

The IPO and related transactions resulted in an “ownership change” within the meaning of the U.S. federal income tax laws addressing net operating loss carryforwards, alternative minimum tax credits and other similar tax attributes. As a result of such ownership change, as well as any prior ownership changes (if any), there will be specific limitations on the NF Group’s ability to use its net operating loss carryforwards and other tax attributes from periods prior to the IPO. It is possible in the future that such limitations could limit the NF Group’s ability to utilize such tax attributes and, therefore, result in an increase in the NF Group’s U.S. federal income tax liability. Such an increase would adversely affect the Company’s financial position, cash flow and liquidity.

In addition, there may be future ownership changes that result from transactions such as the acquisition of shares by Marcopolo that, taking into account prior transactions, may limit the NF Group’s ability to use its net operating loss carryforwards and other tax attributes in the future.

***U.S. federal income tax legislation relating to inversion transactions could adversely affect the U.S. taxation of the Company and holders***

U.S. federal income tax legislation enacted in 2004 dealing with corporate “inversions” (e.g., certain transactions in which a non-U.S. corporation acquires substantially all of the equity interests in, or the assets of, a U.S. corporation, if, after the transaction, former equity owners of the U.S. corporation own a specified level of stock in the non-U.S. corporation) provides in certain cases that a non-U.S. corporation may be treated as a U.S. corporation for U.S. federal income tax purposes. This legislation should not apply to the Company, because of (i) the ownership of the Company, and (ii) the NF Group’s substantial business activities in Canada. In 2009, the U.S. Treasury Department promulgated final and temporary implementing regulations which replaced temporary implementing regulations that had been issued in 2006, that provide substantial support for the position that the inversion legislation should not apply to the Company. Temporary regulations issued in 2012 allows the Company to continue to rely on the temporary regulations issued in 2009 for purposes of determining whether the NF Group may be viewed as carrying substantial business activities in Canada. However, future regulations or other guidance may modify these rules, possibly retroactively. Moreover, because the determination of whether the NF Group

and its affiliates have substantial business activities in Canada is based on all facts and circumstances, it is possible that the Service or a court could disagree with the Company's conclusion. In that case, NFI would become subject to U.S. federal income tax, which would adversely affect the Company's financial position, cash flow and liquidity.

The Company's auditors have indicated that, if the NF Group does not maintain substantial business activities in Canada, the risk that the inversion legislation may apply to the Company could cause the Company to require a reserve for financial accounting purposes for the potential increased U.S. tax liability of the Company. The nature and magnitude of any such reserve would depend on all the facts and circumstances relating to the Company and the NF Group at the time, as well as the state of guidance from the U.S. Treasury Department on the inversion legislation. Any such reserve could adversely affect the Company's financial position, cash flow and liquidity, and could affect the Company's ability to make dividend payments on the Shares and interest payments on the Debentures. Moreover, the risks associated with the potential application of the inversion legislation to the Company may restrict the Company's ability to pursue U.S. acquisitions in the future and such restrictions may materially adversely affect the Company's growth opportunities.

***The NF Group's interest deductions on intercompany indebtedness between NFI and NFI ULC may generate "dual consolidated losses" for U.S. federal income tax purposes and may result in disallowance of interest deductions if certain "triggering events" occur***

Pursuant to Code section 1503(d) and the Treasury Regulations thereunder (the "DCL" Rules), the interest deductions associated with the intercompany indebtedness between NFI, as lender, and NFI ULC, as borrower, independently or together with any other deductions attributable to NFI ULC, may generate a "dual consolidated loss" ("DCL") for U.S. federal income tax purposes and would, in that case, be deductible by the NF Group only if the NF Group and NFI ULC make an election provided by the DCL Rules, and comply with all applicable requirements, including annual reporting and certification requirements. In the event that NFI ULC has a DCL for a taxable year, the NF Group and NFI ULC intend to make such election and comply with all applicable requirements. Even if such an election is made, however, if any of several "triggering events" occurs (e.g., the use of such losses to offset the income of any other non-U.S. person, or, in certain circumstances, a disposition of NFI ULC stock or assets), the NF Group will generally be required to report all or a portion of the amount of any prior interest deductions on the intercompany indebtedness between NFI and NFI ULC and other deductions (plus interest thereon) as gross income in the year of the triggering event. The NF Group and NFI ULC intend to comply with all of the DCL reporting and certification requirements and to conduct their affairs such that no DCL triggering event occurs. However, if the NF Group and NFI ULC fail to satisfy such reporting and certification requirements, or if a DCL triggering event occurs and no exception applies, the NF Group's taxable income and thus its U.S. federal income tax liability would be materially increased. This would adversely affect the NF Group's financial position, cash flow and liquidity, and could adversely affect the Company's financial position, cash flow and liquidity.

***The IRS May Challenge the Characterization of the Subordinated Notes as Debt***

No statutory, judicial or administrative authority directly addresses the treatment of the IDSs or the Subordinated Notes, or instruments similar to the IDSs or the Subordinated Notes, for U.S. federal income tax purposes. Based on advice of its legal counsel, the Issuer treated the acquisition of an IDS of the Issuer as the acquisition of a Share and a Subordinated Note as separate securities and treated the Subordinated Notes as debt for U.S. federal income tax purposes. Prior to the redemption of the Subordinated Notes, the Issuer deducted interest on the Subordinated Notes for U.S. federal income tax purposes. However, the IRS or the courts may take the position that the IDSs of the Issuer were a single security classified as equity, or that the Subordinated Notes, standing alone, were properly classified as equity for U.S. federal income tax purposes or that the interest rate on the Subordinated Notes was in

excess of an arm's length rate, which could materially increase the Issuer's taxable income and, thus, U.S. federal and applicable state income tax liability for the taxable years that the Subordinated Notes were outstanding. This could adversely affect the Company's financial position, cash flow and liquidity.

***Notification pursuant to IRS Circular 230 precludes reliance by investors for the purpose of avoiding penalties that may be imposed under the Code***

In order to ensure compliance with IRS Circular 230, investors are notified that: (a) any discussion of U.S. federal tax issues in this Annual Information Form is not intended or written to be used or relied upon, and cannot be used or relied upon by such investors, for the purpose of avoiding penalties that may be imposed on such investors under the Code; and (b) each investor should seek advice based on its particular circumstances from an independent tax advisor. This notification precludes investor from using or relying on any discussion of U.S. federal tax issues in this Annual Information Form for the purpose of avoiding penalties that may be imposed on such investors under the Code.

***NFI may not be able to make principal payments on the Debentures***

The Debentures will mature in June 2017. NFI may not be able to refinance the principal amount of the Debentures in order to repay the principal outstanding or may not have generated enough cash from operations to meet this obligation. There is no guarantee that NFI will be able to repay the outstanding principal amount upon maturity of the Debentures.

***The market price for the Shares or Debentures may be volatile***

Factors such as variations in the Issuer's financial results, announcements by the Issuer or others, developments affecting the Company's business, general interest rate levels, the market price of the Shares and general market volatility could cause the market price of the Shares or the Debentures to fluctuate significantly.

In addition, future sales or the availability for sale of substantial amounts of Shares or a significant principal amount of Debentures in the public market could adversely affect the prevailing market price of the Shares and the Debentures and could impair the Issuer's ability to raise capital through future sales of its securities.

## MARKET FOR SECURITIES

### Common Shares

The Shares are listed and posted for trading on the TSX under the trading symbol “NFI”. The total monthly volume of trading and the closing price ranges of the Shares on the TSX in each month of 2013 are set forth in the following table <sup>(1)</sup>:

	<b>CLOSING HIGH (C\$)</b>	<b>CLOSING LOW (C\$)</b>	<b>TOTAL VOLUME</b>
January 2013 .....	10.00	8.53	1,627,146
February 2013.....	10.39	9.72	1,143,883
March 2013.....	10.45	10.12	1,437,898
April 2013.....	10.31	9.60	1,642,520
May 2013.....	10.21	9.62	1,770,035
June 2013.....	11.02	10.02	1,373,472
July 2013.....	11.80	11.06	1,652,562
August 2013.....	11.54	10.80	1,167,636
September 2013 .....	11.53	10.78	1,263,597
October 2013 .....	11.44	10.80	1,282,521
November 2013 .....	11.03	10.33	1,514,331
December 2013 .....	10.71	10.41	773,666

<sup>(1)</sup> Source: Historical data from the TSX.

## Debentures

The Debentures are listed and posted for trading on the TSX under the trading symbol “NFLDB.U”. The total monthly volume of trading and the closing price ranges of the Debentures on the TSX in each month of 2013 are set forth in the following table <sup>(1)</sup>:

	<b>CLOSING HIGH (C\$)</b>	<b>CLOSING LOW (C\$)</b>	<b>TOTAL VOLUME<sup>(2)</sup></b>
January 2013.....	108.01	101.50	50,835
February 2013.....	109.00	106.00	31,310
March 2013.....	109.00	106.40	35,410
April 2013.....	108.00	105.00	13,610
May 2013.....	108.50	104.48	10,020
June 2013.....	110.95	106.50	29,940
July 2013.....	117.40	110.80	57,580
August 2013.....	117.50	109.50	9,790
September 2013 .....	116.00	110.00	68,910
October 2013 .....	115.01	111.00	15,870
November 2013 .....	112.25	106.00	6,040
December 2013 .....	109.50	106.99	6,293

<sup>(1)</sup>Source: Historical data from the TSX.

## AUDITORS, TRANSFER AGENT, REGISTRAR AND TRUSTEE

The auditors of the Company are Deloitte LLP at its office in Winnipeg, Manitoba.

The transfer agent and registrar for the Shares is Computershare Investor Services Inc. at its principal office in Toronto, Ontario.

The trustee for the Debentures is Computershare Trust Company of Canada at its principal office in Toronto, Ontario.

## MATERIAL CONTRACTS

In addition to contracts entered into in the ordinary course of business, the following material contracts have been entered into by the Issuer within the most recently completed financial year, or before the most recently completed financial year but are still in effect:

- the Amended Performance and Restricted Share Unit Plan dated as of December 16, 2013;
- the Credit Facility referred to under “General Development of the Business – Recent Developments – Fiscal 2013” and “Description of Capital Structure – Credit Facility”;

- Purchase Agreement dated as of June 21, 2013 by and among The Traxis Group B.V., NF Transit Holdings, LLC, and NFI referred to under “General Development of the Business — Recent Developments — Fiscal 2013”;
- the Share Option Plan amended and effective March 21, 2013;
- Purchase and Sale Agreement dated as of March 1, 2013, between Daimler Buses North America Inc., Daimler Buses North America Ltd., Daimler North America Corporation and NFI ULC referred to under “General Development of the Business — Recent Developments — Fiscal 2013”;
- the Investment Agreement dated January 23, 2013 between Marcopolo S.A. and NFI referred to under “General Development of the Business – Recent Developments – Fiscal 2013”;
- the Performance and Restricted Share Unit Plan dated as of December 17, 2012;
- the Indenture dated June 5, 2012 referred to under “Description of Capital Structure – Description of Debentures”;
- the underwriting agreement dated May 22, 2012 between NFI and the Underwriters (as defined therein) entered into a connection with the Debenture Offering;
- the investor representation agreement March 21, 2012 between Coliseum Capital Management, LLC and NFI referred to under “General Development of the Business – Recent Developments – Fiscal 2012”;
- the Restricted Share Unit Plan of NFI ULC dated December 13, 2011;
- the Deferred Share Unit Plan for Non-Employee Directors dated November 7, 2011;
- the Performance Unit Plan of NFI ULC dated December 1, 2007, as amended on October 2, 2011;
- the SRP dated August 29, 2011 and referred to under “General Development of the Business – Recent Developments – Fiscal 2011” and “Description of Capital Structure – Shareholder Rights Plan”;
- the Dealer Manager Agreement dated July 7, 2011 between NFI and the Dealer Manager (as defined therein) entered into a connection with the Rights Offering; and
- the New Performance Unit Plan of NFI ULC dated January 1, 2011, as amended on October 2, 2011.

Each of the above material contracts is available for review on SEDAR at [www.sedar.com](http://www.sedar.com).

## **LEGAL PROCEEDINGS**

In the ordinary course of business, the Issuer may, from time to time, be subject to various pending and threatened lawsuits in which claims for monetary damages are asserted. The Issuer is not involved in any legal proceedings that management expects will have a material effect on the Issuer. To management's knowledge, no legal proceedings of a material nature involving the Issuer are pending or threatened by any individuals, entities or governmental authorities.

## **INTERESTS OF MANAGEMENT AND OTHERS IN MATERIAL TRANSACTIONS**

To the knowledge of the directors of the Issuer, as of the date of this Annual Information Form, no director nor officer and no person or company beneficially owning, directly or indirectly, or exercising control or direction over, Shares carrying more than 10% of the voting rights attached to the Shares, nor any associates or affiliates of the foregoing, had any material interest in any transactions involving the Issuer, except as described herein.

## **INTERESTS OF EXPERTS**

Deloitte LLP, the Issuer's auditor, has been named as having prepared a certified statement, report or valuation described or included in a filing, or referred to in a filing, made under National Instrument 51-102 - *Continuous Disclosure Obligations* by the Issuer during, or relating to the Issuer's fiscal year ended December 29, 2013. To the knowledge of the Issuer, Deloitte LLP holds no beneficial interest, directly or indirectly, in any securities or other property of the Issuer or any of its affiliates.

## **ADDITIONAL INFORMATION**

Additional information is provided in the Issuer's financial statements and management's discussion and analysis of the Issuer's financial condition and results of operations for its most recently completed fiscal year. Copies of such documents and any additional information related to the Issuer may be found on SEDAR at [www.sedar.com](http://www.sedar.com). In the alternative, copies may be obtained from the Issuer, upon written request.

Additional information, including directors' and officers' remuneration and indebtedness and the principal holders of the Issuer's securities will be contained in the Issuer's Management Information Circular, to be filed with Canadian securities regulatory authorities in connection with the annual meeting of shareholders of NFI to be held in 2014.

## APPENDIX “A”

### NEW FLYER INDUSTRIES INC. (the “Issuer”)

#### AUDIT COMMITTEE CHARTER

#### 1. **RESPONSIBILITY**

The Audit Committee (the “Committee”) is responsible for assisting the Board of Directors of the Issuer (the “Board”) in fulfilling its oversight responsibilities in relation to:

- (i) the integrity of the Issuer’s financial statements;
- (ii) the Issuer’s compliance with legal and regulatory requirements related to financial reporting;
- (iii) the qualifications, independence and performance of the Issuer’s auditor;
- (iv) the design and implementation of internal controls and disclosure controls;
- (v) the review and identification of the principal risks facing the Issuer and development of appropriate procedures to monitor and mitigate such risks;
- (vi) the development, implementation and administration of the Issuer’s Whistleblower Policy; and
- (vii) any additional matters delegated to the Committee by the Board.

#### 2. **MEMBERS**

The members of the Committee will be selected by the Board on the recommendation of the Issuer’s Human Resources, Compensation and Corporate Governance Committee (the “HR Committee”). The Committee will initially be comprised of three directors of the Issuer and its size may be increased if so determined by the Board.

Each member of the Committee will be both “independent” and “financially literate” within the meaning of applicable securities laws, including without limitation, Multilateral Instrument 52-110 - Audit Committees.

#### 3. **DUTIES**

The Committee is responsible for performing the duties set out below as well as any other duties at any time required by law to be performed by the Committee or otherwise delegated to the Committee by the Board.

##### (a) **Appointment and Review of the Auditor**

The auditor is ultimately accountable to the Committee and reports directly to the Committee. Accordingly, the Committee will evaluate and be responsible for the Issuer’s relationship with the auditor. Specifically, the Committee will:

- (i) select, evaluate and recommend an auditor to the Board for appointment or reappointment, as the case may be, by the shareholders of the Issuer and make recommendations with respect to the auditor's compensation;
- (ii) review and approve the auditor's engagement letter;
- (iii) review, after seeking and taking into account the opinions of senior management, the experience, qualifications, performance and independence (including considering whether the auditor's provision of any permitted non audit services is compatible with maintaining its independence) of the auditor, its engagement and lead partners, with a view to recommending its appointment or reappointment;
- (iv) resolve any disagreements between senior management and the auditor regarding financial reporting;
- (v) at least annually, obtain and review a report by the auditor describing:
  - the auditor's internal quality control procedures, including the safeguarding of confidential information;
  - any material issues raised by (i) the most recent internal quality control review, or peer review, of the auditor, which relates to services provided to the Issuer or its subsidiaries by the auditor, or (ii) the review of the auditor by any independent oversight body, such as the Canadian Public Accountability Board, or governmental or professional authorities within the preceding year respecting one or more independent audits carried out by the auditor, and, in the case of each of (i) and (ii), the steps taken to deal with any issues raised in any such review;
- (vi) meet with senior management not less than quarterly without the auditor present for the purpose of discussing, among other things, the performance of the auditor and any issues that may have arisen during the quarter; and
- (vii) where appropriate, recommend to the Board that the auditor be terminated.

**(b) Confirmation of the Auditor's Independence**

At least annually, and in any event before the auditor issues its report on the annual financial statements, the Committee will:

- (i) review a formal written statement from the auditor describing all of its relationships with the Issuer;
- (ii) discuss with the auditor any relationships or services that may affect its objectivity and independence (including considering whether the auditor's provision of any permitted non audit services is compatible with maintaining its independence);
- (iii) obtain written confirmation from the auditor that it is objective within the meaning of the Rules of Professional Conduct/Code of Ethics adopted by the provincial institute or order of Chartered Accountants to which it belongs and is

an independent public accountant within the meaning of the Independence Standards of the Canadian Institute of Chartered Accountants; and

- (iv) confirm that the auditor has complied with applicable rules, if any, with respect to the rotation of certain members of the audit engagement team.

**(c) Pre Approval of Non Audit Services**

The Committee will pre approve the appointment of the auditor for any non audit service to be provided to the Issuer or to any subsidiary of the Issuer; provided that it will not approve any service that is prohibited under the rules of the Canadian Public Accountability Board or the Independence Standards of the Canadian Institute of Chartered Accountants. Before the appointment of the auditor for any non audit service, the Committee will consider the compatibility of the service with the auditor's independence. The Committee may pre approve the appointment of the auditor for any non audit services by adopting specific policies and procedures, from time to time, for the engagement of the auditor for non audit services. Such policies and procedures will be detailed as to the particular service, and the Committee must be informed of each service, and the procedures may not include delegation of the Committee's responsibilities to management. In addition, the Committee may delegate to one or more members the authority to pre approve the appointment of the auditor for any non audit service to the extent permitted by applicable law provided that any pre approvals granted pursuant to such delegation shall be reported to the full Committee at its next scheduled meeting.

**(d) Communications with the Auditor**

The Committee has the authority to communicate directly with the auditor and will meet privately with the auditor periodically to discuss any items of concern to the Committee or the auditor, such as:

- (i) the scope, planning and staffing of the audit;
- (ii) the auditor's materiality threshold for the audit;
- (iii) the assessment by the auditor of significant audit risk;
- (iv) any material written communications between the auditor and senior management, such as any management letter or schedule of unadjusted differences;
- (v) whether or not the auditor is satisfied with the quality and effectiveness of financial recording procedures and systems;
- (vi) the extent to which the auditor is satisfied with the nature and scope of its examination;
- (vii) whether or not the auditor has received the full co operation of senior management and other employees of the Issuer;
- (viii) the auditor's opinion of the competence and performance of the Chief Financial Officer and other key financial personnel;

- (ix) the items required to be communicated to the Committee under the Canadian authoritative guidance;
- (x) critical accounting policies and practices to be used by the Issuer and its subsidiaries;
- (xi) alternative treatments of financial information within international financial reporting standards (“IFRS”) that have been discussed with senior management, ramifications of the use of such alternative disclosures and treatments, and the treatment preferred by the auditor;
- (xii) any difficulties encountered in the course of the audit work, including any unresolved issues, any restrictions imposed on the scope of activities or access to requested information, any significant disagreements with senior management and their response; and
- (xiii) any illegal act that may have occurred.

(e) **Review of the Audit Plan**

The Committee will discuss with the auditor the nature of an audit and the responsibility assumed by the auditor when conducting an audit under generally accepted auditing standards. The Committee will review a summary of the auditor’s audit plan for each audit and approve the audit plan with such amendments as it may agree with the auditor.

(f) **Review of Audit Fees**

The Committee will review and make recommendations to the Board regarding the auditor’s fee and the terms of the auditor’s engagement. In determining the auditor’s fee, the Committee will consider, among other things, the number and nature of reports to be issued by the auditor, the quality of the internal controls of the Issuer, the size, complexity and financial condition of the Issuer and the extent of support to be provided to the auditor by the Issuer.

(g) **Review of Financial Statements and MD&A**

The Committee will review and discuss with senior management and the auditor the annual audited financial statements, together with the auditor’s report thereon, the interim financial statements, and Management’s Discussion and Analysis relating to the annual and interim financial statements before recommending them for approval by the Board. The Committee will also engage the auditor to review the interim financial statements prior to the Committee’s review of such financial statements.

In conducting its review of the financial statements and related management’s discussion and analysis, the Committee will:

- (i) consider the quality of, and not just the acceptability of, the accounting principles, the reasonableness of senior management’s judgments and estimates that have a significant effect upon the financial statements, and the clarity of the disclosures in the financial statements;

- (ii) discuss any analyses prepared by senior management or the auditor that set out significant financial reporting issues and judgments made in connection with the preparation of the financial statements, including analyses of the effects of alternative IFRS treatment;
- (iii) discuss the effect of off balance sheet transactions, arrangements, obligations (including contingent liabilities) and other relationships with unconsolidated entities or other persons that may have a material current or future effect on the Issuer's financial condition, changes in financial condition, results of operations, liquidity, capital expenditures, capital resources, or significant components of revenues and expenses;
- (iv) consider any proposed changes in accounting practices or policies and their impact on financial statements of the Issuer;
- (v) discuss with senior management, the auditor and, if necessary, legal counsel, a report from senior management describing any litigation, claim or other contingency, including tax assessments, that could have a material effect upon the financial position of the Issuer, and the manner in which these matters have been disclosed in the financial statements;
- (vi) discuss with senior management and the auditor any correspondence with regulators or governmental agencies, employee complaints or published reports that raise material issues regarding the Issuer's financial statements or accounting policies;
- (vii) discuss with the auditor any special audit steps taken in light of material weaknesses in internal control;
- (viii) review the results of the audit, including any reservations or qualifications in the auditor's opinion;
- (ix) discuss with senior management all significant variances between comparative reporting periods;
- (x) discuss with the auditor any difficulties encountered in the course of the audit work, including any restrictions on the scope of their procedures and access to requested information, accounting adjustments proposed by the auditor which were "passed" (as immaterial or otherwise), and significant disagreements with senior management and the method of resolution;
- (xi) discuss with the auditor any material issues on which the audit team consulted the auditor's national office; and
- (xii) consider any other matter which in its judgment should be taken into account in reaching its recommendation to the Board concerning the approval of the financial statements.

(h) **Review of Other Financial Information**

The Committee will review:

- (i) all earnings press releases and other press releases disclosing financial information, as well as financial information and written earnings guidance provided to analysts and rating agencies. The Committee will also review the use of “pro forma” or “adjusted” non IFRS information in such press releases and financial information. Such review may consist of a general discussion of the types of information to be disclosed or the types of presentations to be made;
- (ii) all other financial statements of the Issuer that require approval by the Board before they are released to the public, including, without limitation, financial statements for use in prospectuses or other offering or public disclosure documents and financial statements required by regulatory authorities;
- (iii) the effect of regulatory and accounting initiatives as well as off balance sheet structures on the Issuer’s financial statements; and
- (iv) disclosures made to the Committee by the Chief Executive Officer and Chief Financial Officer during their certification process for applicable securities law filings about any significant deficiencies and material weaknesses in the design or operation of internal controls over financial reporting which are reasonably likely to adversely affect the ability to record, process, summarize and report financial information, and any fraud involving senior management or other employees who have a significant role in internal control over financial reporting.

(i) **Oversight of Internal Controls and Disclosure Controls**

The Committee will review periodically with senior management the adequacy of the internal controls and procedures that have been adopted by the Issuer and its subsidiaries to safeguard assets from loss and unauthorized use and to verify the accuracy of the financial records. The Committee will review any special audit steps adopted in light of material control deficiencies or identified weaknesses.

The Committee will review with senior management the controls and procedures that have been adopted by the Issuer to confirm that material information about the Issuer and its subsidiaries that is required to be disclosed under applicable law or stock exchange rules is disclosed.

(j) **Review of the Internal Audit Function**

The Committee will review the mandate, budget, planned activities, staffing and organizational structure of the internal audit function (which may be outsourced to a firm other than the auditor) to confirm that the internal audit function is independent of management and has sufficient resources to carry out its mandate. The Committee will discuss this mandate with the auditor.

The Committee will review the appointment and replacement of the internal auditor and will review the significant reports to senior management prepared by the internal auditor and senior management’s responses.

The Committee has the authority to communicate directly with the internal auditor. In addition, as frequently as it deems necessary to fulfill its responsibilities, but not less often than annually, the Committee will meet privately with the internal auditor to discuss any areas of concern to the Committee or the internal auditor.

(k) **Legal Compliance**

The Committee will review any legal matters that could have a significant effect on the Issuer's financial statements. It will also review with legal counsel material inquiries received from regulators and governmental agencies and advise the Board accordingly.

(l) **Enterprise Risk Management**

The Issuer has developed an enterprise risk management framework by which management is able to focus on the identification of risks, the assessment of those risks and the mitigation of risks associated with the achievement of the Issuer's strategic objectives. The Issuer's risk management program is managed through an executive level risk committee in conjunction with the Internal Audit department.

The Committee will oversee the Issuer's risk management function and the enterprise risk management framework and, on a quarterly basis, will review a report from senior management describing the major financial, legal, operational and reputational risk exposures of the Issuer and the steps senior management has taken to monitor and control such exposures, including the Issuer's policies with respect to risk assessment and management. The Committee will review environmental, insurance and other liability issues, risk management and information technology issues and review policies and procedures in respect thereof and report to the Board on such matters. The Committee will also review and approve management's information technology strategic plan, business continuity plans and major technology capital investments consistent with the Issuer's capital budget recommended by the Committee and approved by the Board.

(m) **Taxation Matters**

The Committee will review with senior management the status of taxation matters of the Issuer and its subsidiaries. The Committee will also review a report from senior management confirming that the Issuer and its subsidiaries have withheld or collected and remitted all amounts required to be withheld or collected and remitted by them in respect of any taxes, levies, assessments, reassessments and other charges payable to any governmental authority.

(n) **Employees of the Auditor**

The Committee will establish, review and approve policies for the hiring by the Issuer of any partners and employees and former partners and former employees of the present or former auditor.

(o) **Evaluation of Financial and Accounting Personnel**

The Committee will have direct responsibility to:

- (i) develop a position description for the Chief Financial Officer, setting out the Chief Financial Officer's authority and responsibilities, and present the same to the HR Committee and Board for approval;
  - (ii) review and approve the goals and objectives that are relevant to the Chief Financial Officer's compensation and present the same to the HR Committee;
  - (iii) evaluate the Chief Financial Officer's and director of Internal Audit's performance in meeting their goals and objectives;
  - (iv) make specific recommendations to the HR Committee and Board with respect to the Chief Financial Officer's and the director of Internal Audit's compensation based on the evaluation referred to above;
  - (v) review and assess, with the input of senior management and, if required by the Committee, the external auditor, the performance of the Issuer's financial and accounting personnel; and
  - (vi) recommend to the HR Committee and Board remedial action where necessary.
- (p) **Signing Authority and Approval of Expenses**

The Committee will determine the signing authority of officers and directors in connection with the expenditure and release of funds. The Committee will also review the Chief Executive Officer and Chief Financial Officer's expense statements. Director expense statements will be reviewed by the Chief Executive Officer. Where the Chief Executive Officer thinks it advisable, he or she may request that the Committee review director expense statements.

#### 4. **COMPLAINTS PROCEDURE**

The Committee will establish a Whistleblower Policy for the receipt, retention and follow up of complaints received by the Issuer regarding accounting, internal controls, disclosure controls or auditing matters and any violation of the Issuer's Code of Business Conduct and Ethics and a procedure for the confidential, anonymous submission of concerns by employees of the Issuer regarding such matters.

#### 5. **REPORTING**

The Committee will regularly report to the Board on:

- (i) the auditor's independence, engagement and fees;
- (ii) the performance of the auditor and the Committee's recommendations regarding its reappointment or termination;
- (iii) the adequacy of the Issuer's internal controls and disclosure controls;
- (iv) the Issuer's risk management procedures;
- (v) its recommendations regarding the annual and interim financial statements of the Issuer, including any issues with respect to the quality or integrity of the financial statements;

- (vi) its review of the annual and interim management’s discussion and analysis;
- (vii) any complaints made under and the effectiveness of the Issuer’s Whistleblower Policy;
- (viii) the Issuer’s compliance with legal and regulatory requirements related to financial reporting; and
- (ix) all other significant matters it has addressed or reviewed and with respect to such other matters that are within its responsibilities, together with any associated recommendations.

## 6. **AUDIT COMMITTEE MEETINGS**

### (a) **Scheduling**

The Committee will meet as often as it determines is necessary to fulfill its responsibilities, which in any event will be not less than quarterly. A meeting of the Committee may be called by the auditor, the chairperson of the Committee (the “Committee Chair”), the chairperson of the Board, the Chief Executive Officer, the Chief Financial Officer or any Committee member.

Meetings will be held at a location determined by the Committee Chair and notice shall be given in accordance with the provisions of the Issuer’s by-laws.

### (b) **Notice to Auditor**

The auditor is entitled to receive notice of every meeting of the Committee and, at the expense of the Issuer, to attend and be heard thereat and, if so requested by a member of the Committee, shall attend any meeting of the Committee held during the term of office of the auditor.

### (c) **Agenda**

The Committee Chair will establish the agenda for each meeting. Any member may propose the inclusion of items on the agenda, request the presence of or a report by any member of senior management, or at any meeting raise subjects that are not on the agenda for the meeting.

### (d) **Distribution of Information**

The Committee Chair will distribute, or cause the officers of the Issuer to distribute, an agenda and meeting materials in advance of each meeting to allow members sufficient time to review and consider the matters to be discussed.

### (e) **Attendance and Participation**

Each member is expected to attend all meetings. A member who is unable to attend a meeting in person may participate by telephone or teleconference.

### (f) **Quorum**

Two members will constitute a quorum for any meeting of the Committee.

(g) **Voting and Approval**

At meetings of the Committee, each member will be entitled to one vote and questions will be decided by a majority of votes. In case of an equality of votes, the Committee Chair will not have a second or casting vote in addition to his or her original vote.

(h) **Procedures**

Procedures for Committee meetings will be determined by the Committee Chair unless otherwise determined by the by-laws of the Issuer or a resolution of the Committee or the Board.

(i) **Transaction of Business**

The powers of the Committee may be exercised at a meeting where a quorum is present in person or by telephone or other electronic means, or by resolution in writing signed by all members entitled to vote on that resolution at a meeting of the Committee.

(j) **Absence of the Committee Chair**

In the absence of the Committee Chair at a meeting of the Committee, the members in attendance must select one of them to act as chairperson of that meeting.

(k) **Secretary**

The Committee may appoint one of its members or any other person to act as secretary.

(l) **Minutes of Meetings**

A person designated by the Committee Chair at each meeting will keep minutes of the proceedings of the Committee and the Committee Chair will cause an officer of the Issuer to circulate copies of the minutes to each member on a timely basis.

7. **COMMITTEE CHAIR**

Each year, the Board will appoint one member who is qualified for such purpose to be the Committee Chair. If, in any year, the Board does not appoint a Committee Chair, the incumbent Committee Chair will continue in office until a successor is appointed.

8. **REMOVAL AND VACANCIES**

Any member may be removed and replaced at any time by the Board, and will automatically cease to be a member as soon as the member ceases to meet the qualifications set out above. The Board will fill vacancies on the Committee by appointment from among qualified members of the Board. If a vacancy exists on the Committee, the remaining members will exercise all of its powers so long as a quorum remains in office.

9. **ASSESSMENT**

At least annually, the HR Committee will review the effectiveness of the Committee in fulfilling its responsibilities and duties as set out in this Charter and in a manner consistent with the mandate adopted by the Board.

10. **REVIEW AND DISCLOSURE**

The Committee will review this Charter at least annually and submit it to the HR Committee together with any proposed amendments. The HR Committee will review the Charter and submit it to the Board for approval with such further proposed amendments as it deems necessary and appropriate.

This Charter will be posted on the Issuer's Web site and the annual report of the Issuer will state that this Charter is available on the Web site or is available in print to any securityholder who requests a copy.

11. **ACCESS TO OUTSIDE ADVISORS AND RECORDS**

The Committee may, subject to advising the chairperson of the Board, retain independent counsel and any outside advisor at the expense of the Issuer at any time and has the authority to determine any such advisors' fees and other retention terms.

The Committee, and any outside advisors retained by it, will have access to all records and information relating to the Issuer and its subsidiaries and all their respective officers, employees and agents which it deems relevant to the performance of its duties.