Independent Auditor's Report

To the Shareholders of
EXFO Inc.

We have completed integrated audits of EXFO Inc.'s and its subsidiaries 2014, 2013 and 2012 consolidated financial statements and their internal control over financial reporting as at August 31, 2014. Our opinions, based on our audits, are presented below.

Report on the consolidated financial statements

We have audited the accompanying consolidated financial statements of EXFO Inc. and its subsidiaries, which comprise the consolidated balance sheets as at August 31, 2014 and August 31, 2013 and the consolidated statements of earnings, comprehensive loss, changes in shareholders' equity and cash flows for each of the three years in the period ended August 31, 2014, and the related notes, which comprise a summary of significant accounting policies and other explanatory information.

Management's responsibility for the consolidated financial statements

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

Auditor's responsibility

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

An audit involves performing procedures to obtain audit evidence, on a test basis, about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the company's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances. An audit also includes evaluating the appropriateness of accounting principles and policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

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

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of EXFO Inc. and its subsidiaries as at August 31, 2014 and August 31, 2013 and their financial performance and their cash flows for each of the three years in the period ended August 31, 2014 in accordance with International Financial Reporting Standards as issued by the International Accounting Standards Board.

Report on internal control over financial reporting

We have also audited EXFO Inc.'s and its subsidiaries' internal control over financial reporting as at August 31, 2014, based on criteria established in Internal Control - Integrated Framework (1992), issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

Management's responsibility for internal control over financial reporting

Management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting included in the section "Management's Annual Report on Internal Control over Financial Reporting" included in Item 15b) of the Annual Report on Form 20-F.

Auditor's responsibility

Our responsibility is to express an opinion on the company's internal control over financial reporting based on our audit. We conducted our audit of internal control over financial reporting in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects.

An audit of internal control over financial reporting includes obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control, based on the assessed risk, and performing such other procedures as we consider necessary in the circumstances.

We believe that our audit provides a reasonable basis for our audit opinion on the company's internal control over financial reporting.

Definition of internal control over financial reporting

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that: (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Inherent limitations

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions or that the degree of compliance with the policies or procedures may deteriorate.

Opinion

In our opinion, EXFO Inc. and its subsidiaries maintained, in all material respects, effective internal control over financial reporting as at August 31, 2014, based on criteria established in Internal Control - Integrated Framework (1992) issued by COSO.

PricewaterhouseCoopers LLP[1]

Montréal, Québec, Canada
November 24, 2014

[1] CPA auditor, CA, public accountancy permit No. A119427

EXFO Inc.
Consolidated Balance Sheets

(in thousands of US dollars)

	As at August 31, 2014	As at August 31, 2013
Assets		
Current assets		
Cash	$ 54,121	$ 45,386
Short-term investments (note 5)	5,726	4,868
Accounts receivable (note 5)		
Trade	46,031	50,117
Other	2,001	2,778
Income taxes and tax credits recoverable (note 18)	3,796	6,525
Inventories (note 6)	35,232	35,705
Prepaid expenses	2,281	2,561
	149,188	147,940
Tax credits recoverable (note 18)	41,745	41,719
Property, plant and equipment (notes 7 and 20)	42,780	45,523
Intangible assets (notes 8 and 20)	7,293	7,543
Goodwill (notes 8 and 20)	26,488	27,313
Deferred income tax assets (note 18)	9,816	10,807
Other assets	721	693
	$ 278,031	$ 281,538
Liabilities		
Current liabilities		
Accounts payable and accrued liabilities (note 10)	$ 29,553	$ 26,253
Provisions (note 10)	532	756
Income taxes payable	840	679
Current portion of long-term debt	–	296
Deferred revenue	8,990	9,467
	39,915	37,451
Deferred revenue	3,319	3,932
Deferred income tax liabilities (note 18)	3,087	3,226
Other liabilities	340	477
	46,661	45,086
Commitments (note 11)		
Shareholders' equity		
Share capital (note 12)	111,491	109,837
Contributed surplus	16,503	17,186
Retained earnings	113,635	112,852
Accumulated other comprehensive loss (note 13)	(10,259)	(3,423)
	231,370	236,452
	$ 278,031	$ 281,538

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

On behalf of the Board

/s/ Germain Lamonde
GERMAIN LAMONDE
Chairman, President and CEO

/s/ Claude Séguin
CLAUDE SÉGUIN
Chairman, Audit Committee

EXFO Inc.
Consolidated Statements of Earnings

(in thousands of US dollars, except share and per share data)

	Years ended August 31, 2014	2013	2012
Sales (note 20)	$ 230,806	$ 242,150	$ 249,966
Cost of sales [1] (note 16)	86,836	92,469	91,792
Selling and administrative (note 16)	86,429	88,756	94,139
Net research and development (note 16)	44,846	45,444	49,854
Depreciation of property, plant and equipment (note 16)	4,995	6,028	6,169
Amortization of intangible assets (note 16)	4,398	6,643	7,819
Changes in fair value of cash contingent consideration	–	–	(311)
Interest and other income	(326)	(113)	(131)
Foreign exchange (gain) loss	(1,634)	(4,082)	657
Earnings (loss) before income taxes	5,262	7,005	(22)
Income taxes (note 18)	4,479	5,664	3,571
Net earnings (loss) for the year	$ 783	$ 1,341	$ (3,593)
Basic and diluted net earnings (loss) per share	$ 0.01	$ 0.02	$ (0.06)
Basic weighted average number of shares outstanding (000's)	60,329	60,323	60,453
Diluted weighted average number of shares outstanding (000's) (note 19)	61,015	61,110	60,453

(1) The cost of sales is exclusive of depreciation and amortization, shown separately.

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

EXFO Inc.
Consolidated Statements of Comprehensive Loss

(in thousands of US dollars)

	Years ended August 31, 2014	2013	2012
Net earnings (loss) for the year	$ 783	$ 1,341	$ (3,593)
Other comprehensive income (loss), net of income taxes			
Items that will not be reclassified subsequently to net earnings			
Foreign currency translation adjustment	(7,086)	(15,830)	(6,875)
Items that may be reclassified subsequently to net earnings			
Unrealized gains/losses on forward exchange contracts	(618)	(1,256)	185
Reclassification of realized gains/losses on forward exchange contracts in net earnings (loss)	959	(247)	(1,108)
Deferred income tax effect of gains/losses on forward exchange contracts	(91)	403	256
Other comprehensive loss	(6,836)	(16,930)	(7,542)
Comprehensive loss for the year	$ (6,053)	$ (15,589)	$ (11,135)

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

EXFO Inc.
Consolidated Statements of Changes in Shareholders' Equity

(in thousands of US dollars)

	Year ended August 31, 2012				
	Share capital	Contributed surplus	Retained earnings	Accumulated other comprehensive income	Total shareholders' equity
Balance as at September 1, 2011	$ 110,341	$ 18,017	$ 115,104	$ 21,049	$ 264,511
Exercise of stock options (note 12)	310	–	–	–	310
Redemption of share capital (note 12)	(1,696)	(540)	–	–	(2,236)
Reclassification of stock-based compensation costs (note 12)	2,010	(2,010)	–	–	–
Stock-based compensation costs	–	1,831	–	–	1,831
Net loss for the year	–	–	(3,593)	–	(3,593)
Other comprehensive loss					
Foreign currency translation adjustment	–	–	–	(6,875)	(6,875)
Changes in unrealized gains on forward exchange contracts, net of deferred income taxes of $256	–	–	–	(667)	(667)
Total comprehensive loss for the year	–	–	(3,593)	(7,542)	(11,135)
Balance as at August 31, 2012	$ 110,965	$ 17,298	$ 111,511	$ 13,507	$ 253,281

	Year ended August 31, 2013				
	Share capital	Contributed surplus	Retained earnings	Accumulated other comprehensive income (loss)	Total shareholders' equity
Balance as at September 1, 2012	$ 110,965	$ 17,298	$ 111,511	$ 13,507	$ 253,281
Exercise of stock options (note 12)	87	–	–	–	87
Redemption of share capital (note 12)	(2,565)	(531)	–	–	(3,096)
Reclassification of stock-based compensation costs (note 12)	1,350	(1,350)	–	–	–
Stock-based compensation costs	–	1,769	–	–	1,769
Net earnings for the year	–	–	1,341	–	1,341
Other comprehensive loss					
Foreign currency translation adjustment	–	–	–	(15,830)	(15,830)
Changes in unrealized gains/losses on forward exchange contracts, net of deferred income taxes of $403	–	–	–	(1,100)	(1,100)
Total comprehensive income (loss) for the year	–	–	1,341	(16,930)	(15,589)
Balance as at August 31, 2013	$ 109,837	$ 17,186	$ 112,852	$ (3,423)	$ 236,452

	Year ended August 31, 2014				
	Share capital	Contributed surplus	Retained earnings	Accumulated other comprehensive loss	Total shareholders' equity
Balance as at September 1, 2013	$ 109,837	$ 17,186	$ 112,852	$ (3,423)	$ 236,452
Exercise of stock options (note 12)	225	–	–	–	225
Redemption of share capital (note 12)	(831)	(106)	–	–	(937)
Reclassification of stock-based compensation costs (note 12)	2,260	(2,260)	–	–	–
Stock-based compensation costs	–	1,683	–	–	1,683
Net earnings for the year	–	–	783	–	783
Other comprehensive income (loss)					
Foreign currency translation adjustment	–	–	–	(7,086)	(7,086)
Changes in unrealized losses on forward exchange contracts, net of deferred income taxes of $91	–	–	–	250	250
Total comprehensive income (loss) for the year	–	–	783	(6,836)	(6,053)
Balance as at August 31, 2014	$ 111,491	$ 16,503	$ 113,635	$ (10,259)	$ 231,370

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

EXFO Inc.
Consolidated Statements of Cash Flows

(in thousands of US dollars)

	Years ended August 31,		
	2014	2013	2012
Cash flows from operating activities			
Net earnings (loss) for the year	$ 783	$ 1,341	$ (3,593)
Add (deduct) items not affecting cash			
Changes in discount on short-term investments	–	–	45
Stock-based compensation costs	1,696	1,768	1,862
Depreciation and amortization	9,393	12,671	13,988
Changes in fair value of cash contingent consideration	–	–	(311)
Deferred revenue	(804)	(1,266)	(506)
Deferred income taxes	891	2,951	2,050
Changes in foreign exchange gain/loss	(491)	(1,091)	(1,510)
	11,468	16,374	12,025
Changes in non-cash operating items			
Accounts receivable	3,578	(14,765)	7,974
Income taxes and tax credits	1,447	(4,205)	(5,570)
Inventories	(734)	2,916	10,879
Prepaid expenses	210	993	(589)
Other assets	92	(703)	–
Accounts payable and accrued liabilities and provisions	3,832	(2,373)	643
Other liabilities	(107)	(258)	(105)
	19,786	(2,021)	25,257
Cash flows from investing activities			
Additions to short-term investments	(34,222)	(54,489)	(115,886)
Proceeds from disposal and maturity of short-term investments	33,208	57,514	152,797
Additions to capital assets (notes 7 and 8)	(7,931)	(8,026)	(23,849)
	(8,945)	(5,001)	13,062
Cash flows from financing activities			
Bank loan	–	–	(782)
Repayment of long-term debt	(307)	(589)	(577)
Exercise of stock options	225	87	310
Redemption of share capital	(937)	(3,096)	(2,236)
	(1,019)	(3,598)	(3,285)
Effect of foreign exchange rate changes on cash	(1,087)	(2,862)	1,063
Change in cash	8,735	(13,482)	36,097
Cash – Beginning of year	45,386	58,868	22,771
Cash – End of year	$ 54,121	$ 45,386	$ 58,868
Supplementary information			
Interest received	$ 550	$ 668	$ 591
Interest paid	$ 16	$ 37	$ 76
Income taxes paid	$ 1,272	$ 1,373	$ 1,494

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

EXFO Inc.
Notes to Consolidated Financial Statements

(tabular amounts in thousands of US dollars, except share and per share data and as otherwise noted)

1 Nature of Activities and Incorporation

EXFO Inc. and its subsidiaries (together "EXFO" or the company) design, manufacture and market test, service assurance and quality of experience solutions for wireless and wireline network operators and equipment manufacturers in the global telecommunications industry. The company's core-to-edge solutions assess the performance and reliability of converged Internet protocol (IP) fixed and mobile networks.

EXFO is a company incorporated under the Canada Business Corporations Act and domiciled in Canada. The address of its headquarters is 400 Godin Avenue, Quebec, Province of Quebec, Canada, G1M 2K2.

These consolidated financial statements were authorized for issue by the Board of Directors on November 24, 2014.

2 Basis of Presentation

These consolidated financial statements have been prepared in accordance with the *International Financial Reporting Standards* (IFRS), as issued by the *International Accounting Standards Board* (IASB). The company has consistently applied the same accounting policies through all periods presented.

These IFRS consolidated financial statements have been prepared based on the following accounting policies:

Basis of measurement

These consolidated financial statements have been prepared under the historical cost convention, except for the revaluation of derivative financial instruments and available-for-sale investments.

Consolidation

These consolidated financial statements include the accounts of the company and its domestic and international subsidiaries. Intercompany accounts and transactions have been eliminated.

Revenue recognition

Revenue comprises the fair value of the consideration received or receivable for the sales of goods and services in the ordinary course of business.

Sales of goods

Revenue from the sales of goods, which represents the majority of the sales of the company, is recognized when the significant risks and rewards of ownership of the goods have passed to the buyer, usually upon delivery of the goods. Revenue is recorded based on the price specified in the sales arrangement.

Maintenance contracts

Maintenance contracts are usually offered to customers for periods of 12 to 36 months. They generally include the right to unspecified upgrades and enhancements on a when-and-if-available basis as well as customer service. Revenue from these contracts is recognized ratably over the terms of the maintenance contracts on a straight-line basis.

Extended warranties

Extended warranties are usually offered to customers for periods of 6 to 48 months. Revenue from these extended warranties is recognized ratably over the warranty period on a straight-line basis.

Multiple-component arrangements

When a sales arrangement includes multiple separately identifiable components such as goods, extended warranties, maintenance contracts and installation, the revenue recognition criteria are applied to each separately identifiable component. A component is considered separately identifiable if the delivered item has value to the customer on a stand-alone basis and the fair value associated with the component can be measured reliably. The company allocates the selling price of a multiple-component arrangement to each component based on the fair value of each component in relation to the fair value of the arrangement as a whole.

Sales arrangements may include acceptance clauses. When a sales arrangement does include an acceptance provision, acceptance occurs upon the earliest of receipt of a written customer acceptance or expiration of the acceptance period. For these sales arrangements, the sale is recognized when acceptance occurs.

Presentation currency

The functional currency of the company is the Canadian dollar. The company has adopted the US dollar as its presentation currency as it is the most commonly used reporting currency in its industry. The consolidated financial statements are translated into the presentation currency as follows: assets and liabilities are translated at the exchange rate in effect on the date of the balance sheet; revenues and expenses are translated at the monthly average exchange rate. The foreign currency translation adjustment arising from such translation is included in accumulated other comprehensive income in the shareholders' equity.

Foreign currency translation

a) *Foreign currency transactions*

Transactions denominated in currencies other than the functional currency are translated into the relevant functional currency as follows: Monetary assets and liabilities are translated at the exchange rate in effect on the date of the balance sheet, and revenues and expenses are translated at the exchange rate in effect on the date of the transaction. Non-monetary assets and liabilities measured at historical cost and denominated in a foreign currency are translated using the exchange rate at the date of the transaction, whereas non-monetary items that are measured at fair value and denominated in a foreign currency are translated using the exchange rates at the date when the fair value was determined. Foreign exchange gains and losses arising from such translation are included in the consolidated statements of earnings.

b) *Foreign operations*

Each foreign operation determines its own functional currency and items included in the financial statements of each foreign operation are measured using that functional currency. The financial statements of each foreign operation that has a functional currency different from the company are translated into Canadian dollars as follows: Assets and liabilities are translated at the exchange rate in effect on the date of the balance sheet, whereas revenues and expenses are translated at the monthly average exchange rate. The foreign currency translation adjustment arising from such translation is included in accumulated other comprehensive income in the shareholders' equity.

Financial instruments

The classification of financial instruments depends on the intended purpose when the financial instruments were acquired or issued, as well as on their characteristics and designation by the company.

Classification

Financial assets

Cash	Loans and receivables
Short-term investments	Available for sale
Accounts receivable	Loans and receivables
Other assets	Loans and receivables

Financial liabilities

Accounts payable and accrued liabilities	Other financial liabilities
Long-term debt	Other financial liabilities

Available-for-sale financial assets

Available-for-sale financial assets are non-derivative financial assets that are designated as available for sale, or are not classified in any of the other categories. They are initially recognized at fair value plus transaction costs and they are subsequently measured at fair value. After their initial recognition, any changes in their fair value are reflected in other comprehensive income.

Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. After their initial measurement at fair value plus transaction costs, they are carried at amortized cost, using the effective interest rate method, which generally corresponds to the nominal amount due to their short-term maturity.

Other financial liabilities

Other financial liabilities are non-derivative financial liabilities initially measured at fair value plus transaction costs and they are subsequently carried at amortized cost, using the effective interest rate method, which generally corresponds to the nominal amount due to their short-term maturity.

Derivative financial instruments and hedging activities

Forward exchange contracts are utilized by the company to manage its foreign currency exposure. Forward exchange contracts are entered into by the company to hedge anticipated US-dollar-denominated sales and the related accounts receivable as well as Indian-rupee-denominated operating expenses and the related accounts payable. The company's policy is not to utilize those derivative financial instruments for trading or speculative purposes.

The company's forward exchange contracts, which are designated as cash flow hedging instruments, qualify for hedge accounting.

They are initially recorded at fair value plus transaction costs and they are subsequently measured at fair value. After initial recognition, the effective portion of changes in their fair value is reflected in other comprehensive income. Any ineffective portion is recognized immediately in the consolidated statements of earnings. Upon the recognition of related hedged sales and operating expenses, accumulated changes in fair value are respectively reclassified in sales and net research and development expenses in the consolidated statements of earnings.

At the inception of a hedge relationship, the company formally designates and documents the hedge relationship to which the company wishes to apply hedge accounting, the risk management objectives, the hedging instrument, the hedged item and the method used to test effectiveness. The company assesses effectiveness of the hedge relationship at inception and on an ongoing basis using the dollar-offset method.

Fair value hierarchy

The company classifies its derivative and non-derivative financial assets and liabilities measured at fair value using the fair value hierarchy as follows:

Level 1: Quoted prices (unadjusted) in active market for identical assets or liabilities;

Level 2: Inputs other than quoted prices included within level 1 that are observable for the asset and liability, either directly or indirectly;

Level 3: Unobservable inputs for the asset or liability.

The company's short-term investments and forward exchange contracts are measured at fair value at each balance sheet date. The company's short-term investments are classified within level 1 of the fair value hierarchy because they are valued using quoted market prices in active markets. The company's forward exchange contracts are classified within level 2 of the fair value hierarchy because they are valued using quoted prices and forward foreign exchange rates at the balance sheet dates.

Short-term investments

All investments with original terms to maturity of three months or less and that are not required for the purposes of meeting short-term cash requirements are classified as short-term investments. Short-term investments are classified as available-for-sale financial assets; therefore, they are carried at fair value in the balance sheet, and any changes in their fair value are reflected in other comprehensive income. Upon the disposal or maturity of these assets, accumulated changes in their fair value are reclassified in the consolidated statements of earnings.

Inventories

Inventories are valued on an average cost basis, at the lower of cost and net realizable value. Net realizable value is the estimated selling price in the ordinary course of business less the estimated costs necessary to make the sale.

The cost of work in progress and finished goods includes material, labor and an allocation of manufacturing overhead.

Property, plant and equipment and depreciation

Property, plant and equipment are recorded at cost, net of accumulated depreciation and accumulated impairment losses. Such cost is reduced by related research and development tax credits.

Depreciation is provided on a straight-line basis over the estimated useful lives of the asset as follows:

	Term
Land improvements	15 years
Buildings	20 to 60 years
Equipment	3 to 15 years
Leasehold improvements	The lesser of useful life and remaining lease term

The assets' residual values and useful lives are reviewed at each financial year-end, and adjusted prospectively, if appropriate.

Intangible assets, goodwill and amortization

Intangible assets

Intangible assets with finite useful lives primarily include the cost of core technology, customer relationships, brand name and software. The cost of intangible assets acquired in a business combination is the fair value of the assets at the date of acquisition. Following initial recognition, intangible assets are carried at cost less accumulated amortization and accumulated impairment losses. Amortization is provided on a straight-line basis over the estimated useful lives of five years for core technology, customer relationships and brand name, and four and ten years for software. None of the company's intangible assets were developed internally.

The amortization method and the useful lives of intangible assets are reviewed at each financial year-end, and adjusted prospectively, if appropriate.

Goodwill

Goodwill represents the excess of the purchase price of acquired businesses over the estimated fair value of net identifiable assets acquired, and is allocated to each cash-generating unit (CGU) or group of CGUs that are expected to benefit from the related business combination. A group of CGUs represents the lowest level within the company at which the goodwill is monitored for internal management purposes, which is not higher than an operating segment. Goodwill is not amortized but must be tested for impairment on an annual basis or more frequently if events or circumstances indicate that it might be impaired.

Research and development

All costs related to research are expensed as incurred, net of related tax credits and grants. Development costs are expensed as incurred, net of related tax credits and grants, unless they meet the recognition criteria of intangible assets of IAS 38, "*Intangible Assets*'', in which case they are capitalized, net of related tax credits and grants and amortized on a straight-line basis over the estimated benefit period. Research and development expenses are mainly comprised of salaries and related expenses, material costs as well as fees paid to third-party consultants. As at August 31, 2013 and 2014, the company had not capitalized any development costs.

The company elected to account for non-refundable research and development tax credits under IAS 20, "*Accounting for Governmental Grants and Disclosures of Governmental Assistance*'', and as such, these tax credits are presented against gross research and development expenses in the consolidated statements of earnings. Non-refundable research and development tax credits are included in earnings or deducted from the related assets, provided there is reasonable assurance that the company has complied and will comply with the conditions related to the tax credits and that the tax credits will be received.

Impairment of non-financial assets

The company assesses at each reporting date whether there is an indication that the carrying value of property, plant and equipment and finite-life intangible assets may not be recoverable. Non-financial assets that are not amortized (such as goodwill) are subject to an annual impairment test. If any indication exists, or when annual impairment testing is required, the company estimates the asset or asset group's recoverable amount. For the purpose of measuring recoverable amounts, assets are grouped at the lowest levels for which there are separately identifiable cash flows (CGUs). The recoverable amount is the higher of an asset or CGU's fair value less costs of disposal and its value in use. Where the carrying value of an asset or CGU exceeds its recoverable amount, the asset or the CGU is considered impaired and is written down to its recoverable amount. The company performs its annual goodwill impairment test in the fourth quarter of each fiscal year.

For property, plant and equipment and finite-life intangible assets, the reversal of impairment is limited so that the carrying value of the asset does not exceed its recoverable amount, nor exceed the carrying value that would have been determined, net of depreciation or amortization, had no impairment loss been recognized for the asset in prior periods. Impairment losses on goodwill are not reversed.

Leases

Operating leases are leases for which the company does not assume substantially all the risks and rewards of ownership of the asset. Operating lease rentals are charged to the consolidated statements of earnings on a straight-line basis over the lease term.

As at August 31, 2013 and 2014, all significant leases of the company were classified as operating leases.

Government grants

Grants related to operating expenses are included in earnings when the related expenses are incurred. Grants related to capital expenditures are deducted from the related assets. Grants are included in earnings or deducted from the related assets, provided there is reasonable assurance that the company has complied and will comply with all the conditions related to the grants and that the grants will be received.

Warranty

The company offers its customers basic warranties of one to three years, depending on the specific products and terms of the purchase agreement. The company's typical warranties require it to repair or replace defective products during the warranty period at no cost to the customer. Costs related to basic warranties are accrued at the time of shipment, based upon estimates of expected rework and warranty costs to be incurred. Costs associated with separately priced extended warranties are expensed as incurred.

Income taxes

Income taxes comprise current and deferred income taxes.

Current income taxes

The current income tax assets and liabilities for the current and prior years are measured at the amount expected to be recovered or paid to the taxation authorities. The income tax rates used to calculate the amount are those that are enacted or substantively enacted at the balance sheet dates in the tax jurisdiction where the company generates taxable income/loss.

Deferred income taxes

The company provides for deferred income taxes using the liability method. Under this method, deferred income tax assets and liabilities are determined based on deductible or taxable temporary differences between financial statement values and tax values of assets and liabilities as well as the carry-forward of unused tax losses and deductions, using enacted or substantively enacted income tax rates at the balance sheet dates, that are expected to be in effect for the years in which the assets are expected to be recovered or the liabilities to be settled.

Deferred income tax assets are recognized only to the extent that it is probable that future taxable income will be available against which the deductible temporary differences as well as unused tax losses and deductions can be utilized.

Deferred tax liabilities are recognized for all taxable temporary differences and for taxable temporary differences arising on investments in subsidiaries, except where the reversal of these temporary differences can be controlled and it is probable that the differences will not reverse in the foreseeable future.

Deferred income tax assets and liabilities are presented as non-current in the consolidated balance sheets.

Uncertain tax positions

The company is subject to income tax laws and regulations in several jurisdictions. There are many transactions and calculations during the course of business for which the ultimate tax determination is uncertain. The company maintains provisions for uncertain tax positions that it believes appropriately reflect its risk. These provisions are made using the best estimate of the amount expected to be paid based on a qualitative assessment of all relevant factors. The company reviews the adequacy of these provisions at the end of the reporting periods and any changes in the provisions are recognized in the statements of earnings when they occur. However, it is possible that at some future dates, liabilities in excess of the company's provisions could result from audits by, or litigation with, the relevant taxing authorities. Where the final outcome of these tax-related matters is different from the amounts that were initially recorded, such differences will be recognized in the statement of earnings in the period in which such determination is made.

Earnings per share

Basic earnings per share are calculated by dividing net earnings attributable to common equity holders of the company by the weighted average number of common shares outstanding during the year.

Diluted earnings per share are calculated by dividing net earnings attributable to common equity holders of the company by the weighted average number of common shares outstanding during the year, plus the effect of dilutive potential common shares outstanding during the year. This method requires that diluted earnings per share be calculated (using the treasury stock method) as if all dilutive potential common shares had been exercised at the latest at the beginning of the year or on the date of issuance, as the case may be, and that the funds obtained thereby (plus an amount equivalent to the unamortized portion of related stock-based compensation costs) be used to purchase common shares of the company at the average market price of the common shares during the year.

Stock-based compensation

Equity-settled awards

The company's stock options, restricted share units and deferred share units are equity-settled awards. The company accounts for stock-based compensation costs on equity-settled awards using the Black-Scholes option valuation model. The fair value of equity-settled awards is measured at the date of grant. Stock-based compensation costs are amortized to expense over the vesting periods together with a corresponding change in contributed surplus in the shareholders' equity. For equity-settled awards with graded vesting, each tranche is considered a separate grant with a different vesting date and fair value, and each tranche is accounted for separately.

Cash-settled awards

The company's stock appreciation rights are cash-settled awards. The company accounts for stock-based compensation costs on cash-settled awards using the Black-Scholes option valuation model. The fair value of the cash-settled awards is remeasured at the end of each reporting period, with any changes in the fair value recognized in the consolidated statements of earnings.

Operating segments

Operating segments are defined as components of an entity engaged in business activities form which it may earn revenues and incur expenses, and whose operating results are regularly reviewed by the chief operating decision maker (CODM) to make decisions about resources to be allocated to segments and assess their performance and for which discrete information is available. The company's CODM is the Chief Executive Officer who reviews consolidated results for the purposes of allocating resources and evaluation performance. Accordingly, the company determined that it operates within one operating segment as of, and for the years ended August 31, 2012, 2013 and 2014. Entity-wide disclosures are presented in note 20.

Critical accounting judgments and estimates in applying accounting policies

The preparation of financial statements in accordance with IFRS requires management to make judgments, estimates and assumptions that affect the reported amounts of assets, liabilities, revenue and expenses as well as the disclosures of contingent assets and liabilities at the date of the financial statements. Actual results could differ from those judgments, estimates and assumptions.

Critical judgments, estimates and assumptions are the following:

Critical judgments

a) *Determination of functional currency*

The company operates in multiple countries and generates revenue and incurs expenses in several currencies, namely the Canadian dollar, the US dollar, the euro, the British pound, the Indian rupee and the CNY (Chinese currency). The determination of the functional currency of the company and its subsidiaries may require significant judgment. In determining the functional currency of the company and its subsidiaries, management takes into account primary, secondary and tertiary indicators. When indicators are mixed and the functional currency is not obvious, management uses its judgment to determine the functional currency.

b) *Determination of cash generating units and allocation of goodwill*

For the purpose of impairment testing, goodwill must be allocated to each cash-generating unit (CGU) or group of CGUs that are expected to benefit from the synergies of the business combination. Initial allocation and possible reallocation of goodwill to a CGU or a group of CGUs requires judgment.

Critical estimates and assumptions

a) *Inventories*

The company states its inventories at the lower of cost, determined on an average cost basis, and net realizable value, and provides reserves for excess and obsolete inventories. The company determines its reserves for excess and obsolete inventories based on the quantities on hand at the reporting dates compared to foreseeable needs over the next 12 months, taking into account changes in demand, technology or market.

b) *Income taxes*

The company is subject to income tax laws and regulations in several jurisdictions. Under these laws and regulations, uncertainties exist with respect to the interpretation of complex tax laws and regulations and the amount and timing of future taxable income. The company maintains provisions for uncertain tax positions that it believes appropriately reflect its risk based on its interpretation of laws and regulations. In addition, management has made reasonable estimates and assumptions to determine the amount of deferred tax assets that can be recognized in the consolidated financial statements, based upon the likely timing and level of anticipated future taxable income together with tax planning strategies. The ultimate realization of the company's deferred income tax assets is dependent upon the generation of sufficient future taxable income during the periods in which those assets are expected to be realized.

c) *Tax credits recoverable*

Tax credits are recorded provided that there is reasonable assurance that the company has complied and will comply with all the conditions related to the tax credits and that the tax credits will be received. The ultimate recovery of the company's non-refundable tax credits is dependent upon the generation of sufficient future taxable income during the tax credits carry-forward periods. Management has made reasonable estimates and assumptions to determine the amount of non-refundable tax credits that can be recognized in the consolidated financial statements, based upon the likely timing and level of anticipated future taxable income together with tax planning strategies (note 18).

d) *Impairment of non-financial assets*

Impairment exists when the carrying value of an asset or group of assets (cash generating unit (CGU)) exceeds its recoverable amount, which is the higher of its fair value less costs of disposal and its value in use. The fair value less costs of disposal calculation is based on available data from a binding sales agreement in an arm's length transaction, including data from recent transactions of similar assets, within the same industry, when available, available data from observable active market prices less incremental costs for disposing of the asset, or the company's stock price. To supplement this information or when such information is not available, the company uses discounted cash flows. The establishment of discounted cash flows requires the use of estimates and assumptions, including management's expectations of future revenue growth, operating costs and profit margins as well as discount rates for each CGU. Estimates and assumptions used to establish discounted cash flows are described in note 8.

i) Growth rates

The assumptions used are based on the company's historical growth, internal budget, expectations of future revenue growth, sales funnel, as well as industry and market trends.

ii) Discount rate

The discount rate used by the company represents its weighted average cost of capital (WACC), plus a premium to take into account specific risks of the CGU, as the case may be.

New IFRS pronouncements and amendments

Adopted during the year

The company has adopted the following amended and new standards, effective September 1, 2013. These changes were made in accordance with the applicable transitional provisions.

Consolidation

IFRS 10, "*Consolidated Financial Statements*", requires an entity to consolidate an investee when it is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee. IFRS 10 replaces Standing Interpretations Committee ("SIC") 12, "*Consolidation — Special Purpose Entities*", and parts of IAS 27, "*Consolidated and Separate Financial Statements*". The adoption of IFRS 10 had no impact on the company's consolidated financial statements.

Joint arrangements

IFRS 11, "*Joint Arrangements*", requires a venturer to classify its interest in a joint arrangement as a joint venture or joint operations. Joint ventures are accounted for using the equity method of accounting whereas for a joint operation, the venture recognizes its share of the assets, liabilities, revenues and expenses of the joint operation. IFRS 11 replaces IAS 31, "*Interests in Joint Ventures*", and SIC 13, "*Jointly Controlled Entities — Non-Monetary Contributions by Venturers*". The adoption of IFRS 11 had no impact on the company's consolidated financial statements.

Disclosure of interests in other entities

IFRS 12, "*Disclosure of Interests in Other Entities*", establishes disclosure requirements for interests in other entities, such as subsidiaries, joint arrangements, associates and structured entities. This standard carries forward existing disclosures and introduces significant additional disclosure requirements that address the nature of, and risks associated with, an entity's interests in other entities. The adoption of IFRS 12 had no impact on the company's consolidated financial statements.

Fair value measurement

IFRS 13, "*Fair Value Measurement*", is a comprehensive standard for fair value measurement and disclosure requirements for use across all IFRS standards. The new standard clarifies that fair value is the price that would be received to sell an asset, or paid to transfer a liability in an orderly transaction between market participants, at the measurement date. It also establishes disclosures about fair value measurement. Under existing IFRS, guidance on measuring and disclosing fair value is dispersed among the specific standards requiring fair value measurements and, in many cases, does not reflect a clear measurement basis or consistent disclosures. The adoption of IFRS 13 did not require any adjustment to the valuation techniques used by the company to measure fair value. The company provided the required additional disclosure in its consolidated financial statements (note 5).

Financial instruments

IFRS 7, "*Financial Instruments: Disclosures*", has been amended to enhance disclosure requirements related to offsetting of financial assets and liabilities. The adoption of these amendments had no impact on the company's consolidated financial statements.

Issued but not yet adopted

Financial instruments

IFRS 9, "*Financial Instruments*", was issued in October 2010 and will replace IAS 39, "*Financial Instruments: Recognition and Measurement*". IFRS 9 uses a single approach to determine whether a financial asset is measured at amortized cost or fair value, replacing the multiple rules in IAS 39. The approach in IFRS 9 is based on how an entity manages its financial instruments in the context of its business model and the contractual cash flow characteristics of the financial assets. Most of the requirements in IAS 39 for classification and measurement of financial liabilities were carried forward unchanged to IFRS 9. The new standard also requires a single impairment method to be used, replacing the multiple impairment methods in IAS 39. Requirements relating to hedge accounting representing a new hedge accounting model have also been added to IFRS 9. The new standard is effective for annual periods beginning on or after January 1, 2018 and must be applied retrospectively. The company has not yet assessed the impact that the new standard will have on its consolidated financial statements.

Revenue from contracts with customers

IFRS 15, "*Revenue from Contracts with Customers*", was issued in May 2014. The objective of this new standard is to provide a single, comprehensive revenue recognition model for all contracts with customers to improve comparability. This new standard contains principles that an entity will apply to determine the measurement of revenue and timing of when it is recognized. The underlying principle is that an entity will recognize revenue to depict the transfer of goods or services to customers at an amount that the entity expects to be entitled to in exchange for those goods or services. This new standard is effective for annual periods beginning on or after January 1, 2017. Early adoption is permitted. The company has not yet assessed the impact that the new standard will have on its consolidated financial statements or whether or not to early adopt the new standard.

3 Restructuring Charges

In June 2012, the company implemented a restructuring plan to align its cost structure to the challenging market environment. This plan resulted in one-time severance expenses of $2,418,000. During the year ended August 31, 2012, the company recorded charges of $2,329,000 in severance expenses under that plan. The remaining expenses of $89,000 were recorded during the year ended August 31, 2013 (note 16).

4 Capital Disclosures

The company is not subject to any external restrictions on its capital.

The company's objectives when managing capital are:

- To maintain a flexible capital structure that optimizes the cost of capital at acceptable risk;
- To sustain future development of the company, including research and development activities, market development and potential acquisitions of complementary businesses or products; and
- To provide the company's shareholders with an appropriate return on their investment.

(tabular amounts in thousands of US dollars, except share and per share data and as otherwise noted)

No changes were made to the objectives and policies during the years ended August 31, 2013 and 2014.

The company defines its capital as shareholders' equity, excluding accumulated other comprehensive loss. The capital of the company amounted to $239,875,000 and $241,629,000 as at August 31, 2013 and 2014 respectively.

5 Financial Instruments

The following tables summarize financial instruments by category:

	As at August 31, 2014				
	Loans and receivable	**Available for sale**	**Other financial liabilities**	**Derivatives used for hedging**	**Total**
Financial assets					
Cash	$ 54,121	$ –	$ –	$ –	$ 54,121
Short-term investments	$ –	$ 5,726	$ –	$ –	$ 5,726
Accounts receivable	$ 47,981	$ –	$ –	$ –	$ 47,981
Other assets	$ 114	$ –	$ –	$ –	$ 114
Forward exchange contracts	$ –	$ –	$ –	$ 193	$ 193
Financial liabilities					
Accounts payable and accrued liabilities	$ –	$ –	$ 28,990	$ –	$ 28,990
Forward exchange contracts	$ –	$ –	$ –	$ 690	$ 690

	As at August 31, 2013				
	Loans and receivable	**Available for sale**	**Other financial liabilities**	**Derivatives used for hedging**	**Total**
Financial assets					
Cash	$ 45,386	$ –	$ –	$ –	$ 45,386
Short-term investments	$ –	$ 4,868	$ –	$ –	$ 4,868
Accounts receivable	$ 52,895	$ –	$ –	$ –	$ 52,895
Other assets	$ 167	$ –	$ –	$ –	$ 167
Financial liabilities					
Accounts payable and accrued liabilities	$ –	$ –	$ 25,679	$ –	$ 25,679
Forward exchange contracts	$ –	$ –	$ –	$ 722	$ 722
Long-term debt	$ –	$ –	$ 296	$ –	$ 296

Fair value

Cash, accounts receivable and accounts payable and accrued liabilities are financial instruments whose carrying values approximate their fair values due to their short-term maturities. The fair value of other assets and the long-term debt approximates their carrying value due to their relatively short-term maturities.

(tabular amounts in thousands of US dollars, except share and per share data and as otherwise noted)

The fair value of derivative and non-derivative financial assets and liabilities measured at fair value by level of hierarchy is as follows:

	As at August 31, 2014		As at August 31, 2013	
	Level 1	Level 2	Level 1	Level 2
Financial assets				
Short-term investments	$ 5,726	$ –	$ 4,868	$ –
Forward exchange contracts	$ –	$ 193	$ –	$ –
Financial liabilities				
Forward exchange contracts	$ –	$ 690	$ –	$ 808

Market risk

Currency risk

The functional currency of the company is the Canadian dollar. The company is exposed to a currency risk as a result of its export sales of products manufactured in Canada, China and Finland, the majority of which are denominated in US dollars and euros. This risk is partially hedged by forward exchange contracts and certain cost of sales and operating expenses (US dollars and euros). In addition, the company is exposed to a currency risk as a result of its research and development activities in India (Indian rupees). This risk is partially hedged by forward exchange contracts. Forward exchange contracts, which are designated as cash flow hedging instruments, qualify for hedge accounting.

As at August 31, 2013 and 2014, the company held contracts to sell US dollars for Canadian dollars and Indian rupees at various forward rates, which are summarized as follows:

US dollars – Canadian dollars

Expiry dates	Contractual amounts	Weighted average contractual forward rates
As at August 31, 2013		
September 2013 to August 2014	$ 22,200	1.0280
September 2014 to August 2015	15,000	1.0529
September 2015 to August 2016	5,000	1.0716
Total	$ 42,200	1.0420
As at August 31, 2014		
September 2014 to August 2015	$ 22,200	1.0666
September 2015 to August 2016	13,400	1.0923
September 2016 to December 2016	3,400	1.1063
Total	$ 39,000	1.0789

US dollars – Indian rupees

Expiry dates	Contractual amounts	Weighted average contractual forward rate
As at August 31, 2014		
September 2014 to March 2015	$ 2,800	62.11

The carrying amount of forward exchange contracts is equal to fair value, which is based on the amount at which they could be settled based on estimated current market rates. The fair value of forward exchange contracts amounted to net losses of $808,000 and $497,000 as at August 31, 2013 and 2014.

As at August 31, 2014, forward exchange contracts of $51,000 are presented as current assets in other accounts receivable, forward exchange contracts of $142,000 are presented as long-term assets in other long-term assets, forward exchange contracts of $563,000 are presented as current liabilities in accounts payable and accrued liabilities and forward exchange contracts of $127,000 are presented as long-term liabilities in other long-term liabilities in the balance sheet. Forward exchange contracts of $116,000 included in accounts payable and accrued liabilities are recorded in the statement of earnings; otherwise, other forward exchange contracts are not yet recorded in the statement of earnings.

As at August 31, 2013, forward exchange contracts of $574,000 were presented as current liabilities in accounts payable and accrued liabilities and forward exchange contracts of $148,000 were presented as long-term liabilities in other long-term liabilities in the balance sheet.

Based on the portfolio of forward exchange contracts as at August 31, 2014, the company estimates that the portion of net unrealized losses on these contracts as of that date, which will be realized and reclassified from accumulated other comprehensive income to net earnings over the next 12 months, amounts to $396,000.

For the years ended August 31, 2012, 2013 and 2014, the company recognized within its sales foreign exchange gains (losses) on forward exchange contracts of $1,125,000, $380,000 and $(909,000) respectively.

The following table summarizes significant derivative and non-derivative financial assets and liabilities that are subject to currency risk as at August 31, 2013 and 2014:

	As at August 31,			
	2014		2013	
	Carrying/nominal amount (in thousands of US dollars)	Carrying/nominal amount (in thousands of euros)	Carrying/nominal amount (in thousands of US dollars)	Carrying/nominal amount (in thousands of euros)
Financial assets				
Cash	$ 15,382	€ 3,353	$ 9,728	€ 2,106
Accounts receivable	33,127	6,325	33,191	5,284
	48,509	9,678	42,919	7,390
Financial liabilities				
Accounts payable and accrued liabilities	10,824	880	10,355	1,075
Forward exchange contracts (nominal value)	3,800	–	3,800	–
	14,624	880	14,155	1,075
Net exposure	$ 33,885	€ 8,798	$ 28,764	€ 6,315

The value of the Canadian dollar compared to the US dollar was CA$1.0530 = US$1.00 and CA$1.0858 = US$1.00 as at August 31, 2013 and 2014 respectively.

The value of the Canadian dollar compared to the euro was CA$1.3936 = €1.00 and CA$1.4319 = €1.00 as at August 31, 2013 and 2014 respectively.

The following sensitivity analysis summarizes the effect that a change in the value of the Canadian dollar (compared to the US dollar and euro) on derivative and non-derivative financial assets and liabilities denominated in US dollars and euros would have on net earnings, net earnings per diluted share and comprehensive income, based on the foreign exchange rates as at August 31, 2013 and 2014:

(tabular amounts in thousands of US dollars, except share and per share data and as otherwise noted)

- An increase (decrease) of 10% in the period-end value of the Canadian dollar compared to the US dollar would decrease (increase) net earnings by $2,702,000, or $0.04 per diluted share, and $3,001,000, or $0.05 per diluted share, as at August 31, 2013 and 2014 respectively.

- An increase (decrease) of 10% in the period-end value of the Canadian dollar compared to the euro would decrease (increase) net earnings by $870,000, or $0.01 per diluted share, and $1,142,000 or $0.02 per diluted share, as at August 31, 2013 and 2014 respectively.

- An increase (decrease) of 10% in the period-end value of the Canadian dollar compared to the US dollar would increase (decrease) comprehensive income by $2,951,000 and $2,617,000 as at August 31, 2013 and 2014 respectively.

The impact of the change in the value of the Canadian dollar compared to the US dollar and the euro on these derivative and non-derivative financial assets and liabilities is recorded in the foreign exchange gain or loss line item in the consolidated statements of earnings, except for outstanding forward contracts, whose impact is recorded in other comprehensive income. The change in the value of the Canadian dollar compared to the US dollar and the euro also affects the company's balances of income tax recoverable or payable, as well as deferred income tax assets and liabilities denominated in US dollars and euros; this may result in additional and significant foreign exchange gains or losses. However, these tax-related assets and liabilities are not considered financial instruments and are excluded from the sensitivity analysis above. The foreign exchange rate fluctuations also flow through the statements of earnings line items, as a significant portion of the company's cost of sales and operating expenses are denominated in Canadian dollars, euros and Indian rupees, and the company reports its results in US dollars; that effect is not reflected in the sensitivity analysis above.

Interest rate risk

The company has limited exposure to interest rate risk. The company is mainly exposed to interest rate risks through its cash and short-term investments.

Cash

As at August 31, 2013 and 2014, the company's cash balances included an amount of $30,392,000 and $30,102,000 respectively that bears interest at an annual rate of 1.5%.

Short-term investments

Short-term investments consist of the following:

	As at August 31	
	2014	**2013**
Bankers acceptance denominated in Canadian dollars, bearing interest at an annual rate of 1.1%, maturing in September 2014	$ 4,730	$ –
Term deposits denominated in Indian rupees, bearing interest at an annual rate of 9.0%, maturing in December 2014 and January 2015	569	–
Term deposits denominated in Indian rupees, bearing interest at an annual rate of 8.0%, maturing between September 2014 and May 2015 (note 9)	427	–
Commercial paper denominated in Canadian dollars, bearing interest at an annual rate of 1.2%, matured in October 2013	–	4,868
	$ 5,726	$ 4,868

(tabular amounts in thousands of US dollars, except share and per share data and as otherwise noted)

Due to their short-term maturity of usually three months or less, the company's short-term investments are not subject to a significant fair value interest rate risk. Accordingly, changes in fair value have been nominal to the degree that amortized cost approximates the fair value. Any change in the fair value of the company's short-term investments, all of which are classified as available for sale, is recorded in other comprehensive income.

Other financial instruments

Accounts receivable, other assets and accounts payable and accrued liabilities are non-interest-bearing financial assets and liabilities.

Credit risk

Financial instruments that potentially subject the company to credit risk consist of cash, short-term investments, accounts receivable, other assets and forward exchange contracts (with a positive fair value). As at August 31, 2014, the company's short-term investments consist of debt instruments issued by three (one as at August 31, 2013) high-credit quality corporations. These debt instruments are not expected to be affected by a significant liquidity risk. The company's cash and forward exchange contracts are held with or issued by high-credit quality financial institutions; therefore, the company considers the risk of non-performance on these instruments to be limited.

Generally, the company does not require collateral or other security from customers for trade accounts receivable; however, credit is extended to customers following an evaluation of creditworthiness. In addition, the company performs ongoing credit reviews of all its customers and establishes an allowance for doubtful accounts receivable when accounts are determined to be uncollectible. Allowance for doubtful accounts amounted to $766,000 and $396,000 as at August 31, 2013 and 2014, respectively.

For the years ended August 31, 2013 and 2014, no customer represented more than 10% of sales.

The following table summarizes the age of trade accounts receivable:

	As at August 31, 2014	As at August 31, 2013
Current	$ 36,700	$ 41,557
Past due, 0 to 30 days	5,508	6,210
Past due, 31 to 60 days	1,372	2,088
Past due, more than 60 days, net of allowance for doubtful accounts of $766 and $396 as at August 31, 2013 and 2014, respectively	2,451	262
	$ 46,031	$ 50,117

Changes in the allowance for doubtful accounts are as follows:

	Years ended August 31, 2014	Years ended August 31, 2013
Balance – Beginning of year	$ 766	$ 583
Addition charged to earnings	210	323
Write-off of uncollectible accounts	(580)	(140)
Balance – End of year	$ 396	$ 766

(tabular amounts in thousands of US dollars, except share and per share data and as otherwise noted)

Liquidity risk

Liquidity risk is defined as the potential that the company cannot meet its obligations as they become due.

The following tables summarize the contractual maturity of the company's derivative and non-derivative financial liabilities:

	As at August 31, 2014		
	0-12 months	13-24 months	25-36 months
Accounts payable and accrued liabilities	$ 28,990	$ –	$ –
Forward exchange contracts			
Outflow	25,000	13,400	3,400
Inflow	(24,675)	(13,480)	(3,464)
Total	$ 29,315	$ (80)	$ (64)

	As at August 31, 2013		
	0-12 months	13-24 months	25-36 months
Accounts payable and accrued liabilities	$ 25,679	$ –	$ –
Long-term debt	296	–	–
Forward exchange contracts			
Outflow	22,200	15,000	5,000
Inflow	(21,673)	(14,999)	(5,088)
Total	$ 26,502	$ 1	$ (88)

As at August 31, 2014, the company had $59,847,000 in cash and short-term investments and $48,032,000 in accounts receivable. In addition to these financial assets, the company has unused available lines of credit totaling $15,407,000 for working capital and other general corporate purposes, including potential acquisitions and its share repurchase program as well as unused lines of credit totaling $21,993,000 for foreign currency exposure related to its forward exchange contracts (note 9).

6 Inventories

	As at August 31,	
	2014	2013
Raw materials	$ 16,464	$ 16,645
Work in progress	1,100	1,179
Finished goods	17,668	17,881
	$ 35,232	$ 35,705

(tabular amounts in thousands of US dollars, except share and per share data and as otherwise noted)

The cost of sales comprised almost exclusively the amount of inventory recognized as an expense during the reporting years, and amounts to $98,147,000 and $90,445,000 as at August 31, 2013 and 2014 respectively, including related depreciation and amortization, which are shown separately in operating expenses (note 16).

Inventory write-down amounted to $3,838,000, $4,120,000 and $4,600,000 for the years ended August 31, 2012, 2013 and 2014 respectively.

7 Property, Plant and Equipment

	Land and land improvements	Buildings	Equipment	Leasehold improvements	Total
Cost as at September 1, 2012	$ 5,585	$ 38,355	$ 47,962	$ 2,367	$ 94,269
Additions	5	866	3,824	167	4,862
Disposals	–	–	(6,569)	–	(6,569)
Foreign currency translation adjustment	(358)	(2,439)	(2,661)	(171)	(5,629)
Cost as at August 31, 2013	5,232	36,782	42,556	2,363	86,933
Additions	148	18	3,550	164	3,880
Disposals	–	–	(5,799)	(34)	(5,833)
Foreign currency translation adjustment	(158)	(1,203)	(1,337)	(51)	(2,749)
Cost as at August 31, 2014	$ 5,222	$ 35,597	$ 38,970	$ 2,442	$ 82,231
Accumulated depreciation as at September 1, 2012	$ 1,317	$ 6,242	$ 36,171	$ 691	$ 44,421
Depreciation for the year	62	664	4,935	367	6,028
Disposals	–	–	(6,423)	–	(6,423)
Foreign currency translation adjustment	(71)	(437)	(2,033)	(75)	(2,616)
Accumulated depreciation as at August 31, 2013	1,308	6,469	32,650	983	41,410
Depreciation for the year	58	697	3,891	349	4,995
Disposals	–	–	(5,633)	(40)	(5,673)
Foreign currency translation adjustment	(39)	(182)	(1,020)	(40)	(1,281)
Accumulated depreciation as at August 31, 2014	$ 1,327	$ 6,984	$ 29,888	$ 1,252	$ 39,451
Net carrying value as at:					
August 31, 2013	$ 3,924	$ 30,313	$ 9,906	$ 1,380	$ 45,523
August 31, 2014	$ 3,895	$ 28,613	$ 9,082	$ 1,190	$ 42,780

As at August 31, 2013 and 2014, unpaid purchases of property, plant and equipment amounted to $231,000 and $356,000 respectively.

(tabular amounts in thousands of US dollars, except share and per share data and as otherwise noted)

8 Intangible Assets and Goodwill

Intangible assets

	Core technology	Customer relationships	Brand name	Software	Total
Cost as at September 1, 2012	$ 26,077	$ 6,582	$ 656	$ 14,069	$ 47,384
Additions	145	–	–	515	660
Disposals	–	–	–	(66)	(66)
Foreign currency translation adjustment	(1,349)	(416)	(42)	(1,509)	(3,316)
Cost as at August 31, 2013	24,873	6,166	614	13,009	44,662
Additions	3,582	–	–	754	4,336
Disposals	(15,281)	–	–	(193)	(15,474)
Foreign currency translation adjustment	(488)	(187)	(18)	(645)	(1,338)
Cost as at August 31, 2014	$ 12,686	$ 5,979	$ 596	$ 12,925	$ 32,186
Accumulated amortization as at September 1, 2012	$ 19,122	$ 3,252	$ 324	$ 10,554	$ 33,252
Amortization for the year	4,068	1,285	128	1,162	6,643
Disposals	–	–	–	(51)	(51)
Foreign currency translation adjustment	(1,334)	(258)	(26)	(1,107)	(2,725)
Accumulated amortization as at August 31, 2013	21,856	4,279	426	10,558	37,119
Amortization for the year	2,046	1,204	120	1,028	4,398
Disposals	(15,281)	–	–	(193)	(15,474)
Foreign currency translation adjustment	(559)	(137)	(12)	(442)	(1,150)
Accumulated amortization as at August 31, 2014	$ 8,062	$ 5,346	$ 534	$ 10,951	$ 24,893
Net carrying value as at:					
August 31, 2013	$ 3,017	$ 1,887	$ 188	$ 2,451	$ 7,543
August 31, 2014	$ 4,624	$ 633	$ 62	$ 1,974	$ 7,293
Remaining amortization period as at August 31, 2014	4 years	1 year	1 year	2 years	

Goodwill

	Years ended August 31,	
	2014	2013
Balance – Beginning of year	$ 27,313	$ 29,160
Foreign currency translation adjustment	(825)	(1,847)
Balance – End of year	$ 26,488	$ 27,313

In the fourth quarter of fiscal 2014, the company performed its annual goodwill impairment test for its two CGUs, EXFO and Brix. For the purposes of the impairment test, goodwill was allocated as follows to the two CGUs:

	As at August 31,	
	2014	2013
EXFO CGU	$ 10,465	$ 10,791
Brix CGU	16,023	16,522
Total	$ 26,488	$ 27,313

The company used a market-based approach (sales multiples) based on recent comparable transactions in its industry, supplemented by an analysis of its enterprise value derived from its market capitalization to assess the recoverable amount of the EXFO CGU. To assess the recoverable amount of the Brix CGU, the company used a combination of a market-based approach (sales multiples), based on recent comparable transactions in its industry, and discounted cash flows. The recoverable amount of the company's CGUs is classified within level 3 of the fair value hierarchy.

The sales multiple of recent comparable transactions for both CGUs ranged between 1.9 and 5 times sales. These comparable transactions occurred in calendar 2013 and 2014.

Discounted cash flows for the Brix CGU were based on five-year management projections, using five-year sales compound annual growth rate (CAGR) of 23% and a perpetual growth rate of 2% thereafter. The company used a discount rate of 18%. Based on these assumptions (used in the discounted cash flows calculations) as well as a sales multiple of 2.0 times fiscal 2014 sales, the recoverable amount of the Brix CGU exceeds its carrying amount by 49%. The five-year sales CAGR used in the discounted cash flows calculations differs from past experience; management has determined the five-year sales CAGR based on recent market studies, the impact of recently launched and to be launched solutions, as well as its sales funnel.

The Brix CGU's recoverable amount would equal its carrying value using five-year sales CAGR of 8%, which is below management's expected market growth of 10% to 15% (excluding market share gains) over the five-year period used in the discounted cash flows calculations for that CGU, or a sales multiple of 1 time fiscal 2014 sales.

As at August 31, 2014, the recoverable amount for both CGUs exceeded their carrying value.

9 Credit Facilities

The company has lines of credit that provide for advances of up to CA$15,000,000 (US$13,815,000) and up to US$2,000,000. These lines of credit bear interest at the Canadian prime rate. As at August 31, 2014, an amount of CA$443,000 (US$408,000) was drawn from these lines of credit for letters of guarantee in the normal course of the company's operations for its own selling and purchasing requirements. These lines of credit are subject to a negative pledge whereby the company has agreed with the bank not to pledge its assets to any other party without its consent.

In addition, the company has lines of credit totaling $25,681,000 for the foreign currency risk exposure related to its US dollar – Canadian dollar forward exchange contracts (note 5). As at August 31, 2014, an amount of $4,114,000 was reserved from these lines of credit. These lines of credit are unsecured.

Finally, the company has a line of credit of INR 47,000,000 ($775,000) for the foreign currency risk exposure related to its US dollar – Indian rupee forward exchange contracts (note 5). As at August 31, 2014, an amount of INR 21,180,000 ($349,000) was reserved from this line of credit. This line of credit is secured by term deposits totaling INR 25,000,000 ($427,000) (note 5).

(tabular amounts in thousands of US dollars, except share and per share data and as otherwise noted)

10 Accounts Payable and Accrued Liabilities and Provisions

Accounts payable and accrued liabilities

	As at August 31, 2014	2013
Trade	$ 11,848	$ 10,002
Salaries and social benefits	13,353	12,883
Forward exchange contracts (note 5)	563	574
Other	3,789	2,794
	$ 29,553	$ 26,253

Provisions

	As at August 31, 2014	2013
Warranty	$ 500	$ 721
Other	32	35
	$ 532	$ 756

Changes in the warranty provision are as follows:

	Years ended August 31, 2014	2013
Balance – Beginning of year	$ 721	$ 675
Provision	513	650
Settlements	(734)	(604)
Balance – End of year	$ 500	$ 721

11 Commitments

The company entered into operating leases for certain of its premises and equipment, which expire at various dates through 2020. Minimum rentals payable under operating leases are as follows:

	As at August 31 2014	2013
No later than 1 year	$ 2,390	$ 2,514
Later than 1 year and no later than 5 years	1,993	3,479
Later than 5 years	398	517
	$ 4,781	$ 6,510

For the years ended August 31, 2012, 2013 and 2014, rental expenses amounted to $4,308,000, $3,533,000 and $2,892,000 respectively.

(tabular amounts in thousands of US dollars, except share and per share data and as otherwise noted)

12 Share Capital

Authorized – unlimited as to number, without par value

Subordinate voting and participating, bearing a non-cumulative dividend to be determined by the Board of Directors, ranking *pari passu* with multiple voting shares

Multiple voting and participating, entitling to 10 votes each, bearing a non-cumulative dividend to be determined by the Board of Directors, convertible at the holder's option into subordinate voting shares on a one-for-one basis, ranking *pari passu* with subordinate voting shares

The following table summarizes the share capital activity:

	Multiple voting shares		**Subordinate voting shares**		
	Number	**Amount**	**Number**	**Amount**	**Total amount**
Balance as at September 1, 2011	31,643,000	$ 1	28,621,999	$ 110,340	$ 110,341
Exercise of stock options (note 14)	–	–	109,700	310	310
Redemption of restricted share units (note 14)	–	–	418,086	–	–
Redemption of share capital	–	–	(438,894)	(1,696)	(1,696)
Reclassification of stock-based compensation costs to share capital upon exercise of stock awards	–	–	–	2,010	2,010
Balance as at August 31, 2012	31,643,000	1	28,710,891	110,964	110,965
Exercise of stock options (note 14)	–	–	30,675	87	87
Redemption of restricted share units (note 14)	–	–	286,426	–	–
Redemption of deferred share units (note 14)	–	–	37,054	–	–
Redemption of share capital	–	–	(663,256)	(2,565)	(2,565)
Reclassification of stock-based compensation costs to share capital upon exercise of stock awards	–	–	–	1,350	1,350
Balance as at August 31, 2013	31,643,000	1	28,401,790	109,836	109,837
Exercise of stock options (note 14)	–	–	52,800	225	225
Redemption of restricted share units (note 14)	–	–	425,620	–	–
Redemption of deferred share units (note 14)	–	–	38,010	–	–
Redemption of share capital	–	–	(214,470)	(831)	(831)
Reclassification of stock-based compensation costs to share capital upon exercise of stock awards	–	–	–	2,260	2,260
Balance as at August 31, 2014	31,643,000	$ 1	28,703,750	$ 111,490	$ 111,491

(tabular amounts in thousands of US dollars, except share and per share data and as otherwise noted)

a) On November 7, 2012, the company announced that its Board of Directors had approved the renewal of its share repurchase program, by way of a normal course issuer bid on the open market of up to 10% of its issued and outstanding subordinate voting shares, representing 2,072,721 subordinate voting shares at the prevailing market price. The normal course issuer bid started on November 12, 2012, and ended on November 11, 2013. All shares repurchased under the bid were cancelled.

b) On January 8, 2014, the company announced that its Board of Directors had approved the renewal of its share repurchase program, by way of a normal course issuer bid on the open market of up to 10% of the issued and outstanding subordinate voting shares, representing 2,043,101 subordinate voting shares at the prevailing market price. The normal course issuer bid started on January 13, 2014, and will end on January 12, 2015. All shares repurchased under the bid are cancelled.

13 Accumulated Other Comprehensive Income (loss)

Changes in accumulated other comprehensive incomes (loss) are as follows:

	Foreign currency translation adjustment	Cash-flow hedge	Accumulate other comprehensive income (loss)
Balance as at September 1, 2011	$ 19,123	$ 1,926	$ 21,049
Foreign currency translation adjustment	(6,875)	–	(6,875)
Changes in unrealized gains on forward exchange contracts, net of deferred income taxes	–	(667)	(667)
Balance as at August 31, 2012	12,248	1,259	13,507
Foreign currency translation adjustment	(15,830)	–	(15,830)
Changes in unrealized gains/losses on forward exchange contracts, net of deferred income taxes	–	(1,100)	(1,100)
Balance as at August 31, 2013	(3,582)	159	(3,423)
Foreign currency translation adjustment	(7,086)	–	(7,086)
Changes in unrealized losses on forward exchange contracts, net of deferred income taxes	–	250	250
Balance as at August 31, 2014	$ (10,668)	$ 409	$ (10,259)

(tabular amounts in thousands of US dollars, except share and per share data and as otherwise noted)

14 Stock-Based Compensation Plans

The following table summarizes the stock-based compensation costs recognized for employee services received during the years ended August 31, 2012, 2013 and 2014:

	Years ended August 31,		
	2014	2013	2012
Stock-based compensation costs arising from equity-settled awards	$ 1,683	$ 1,769	$ 1,831
Stock-based compensation costs arising from cash-settled awards	13	(1)	31
	$ 1,696	$ 1,768	$ 1,862

The maximum number of additional subordinate voting shares issuable under the Long-Term Incentive Plan and the Deferred Share Unit Plan cannot exceed 6,306,153 shares. The maximum number of subordinate voting shares that may be granted to any individual on an annual basis cannot exceed 5% of the number of outstanding subordinate voting shares. The company settles stock options and redeems restricted share units and deferred share units through the issuance of common shares from treasury.

Long-Term Incentive Plan

The company established the Long-Term Incentive Plan for its directors, executive officers and employees and those of its subsidiaries, as determined by the Board of Directors. The plan, which includes stock options and restricted share units, was approved by the shareholders of the company.

Stock Options

The exercise price of stock options granted under the Long-Term Incentive Plan is the market price of the common shares on the date of grant. Stock options granted under the plan expire 10 years from the date of grant and generally vest over a four-year period, being the required period of service from employees, generally with 25% vesting on an annual basis commencing on the first anniversary of the date of grant. As at August 31, 2013 and 2014, all stock options outstanding were vested.

The following table summarizes stock option activity for the years ended August 31, 2012, 2013 and 2014:

	Years ended August 31,					
	2014		2013		2012	
	Number	Weighted average exercise price (CA$)	Number	Weighted average exercise price (CA$)	Number	Weighted average exercise price (CA$)
Outstanding – Beginning of year	201,254	$ 6	244,354	$ 5	641,357	$ 9
Exercised	(52,800)	5	(30,675)	3	(109,700)	3
Forfeited	(4,500)	6	(2,000)	6	(1,500)	5
Expired	(56,500)	6	(10,425)	5	(285,803)	15
Outstanding – End of year	87,454	$ 6	201,254	$ 6	244,354	$ 5
Exercisable – End of year	87,454	$ 6	201,254	$ 6	244,354	$ 5

(tabular amounts in thousands of US dollars, except share and per share data and as otherwise noted)

The weighted-average market price of the shares at the date of exercise of stock options for the years ended August 31, 2012, 2013 and 2014, was $5.84, $5.08 and $5.08 respectively.

The following table summarizes information about stock options as at August 31, 2014:

	Stock options outstanding and exercisable		
Exercise price (CA$)	**Number**	**Weighted average exercise price (CA$)**	**Weighted average remaining contractual life**
$5.50 to $6.28	87,454	$ 5,64	6 months

Restricted Share Units (RSUs)

RSUs are stock awards that rise and fall in value based on the market price of the company's subordinate voting shares and are redeemable for actual subordinate voting shares or cash at the discretion of the Board of Directors as determined on the date of grant. Vesting dates are also established by the Board of Directors on the date of grant. The vesting dates are subject to a minimum term of three years and a maximum term of 10 years from the award date, being the required period of service from employees. Fair value of RSUs equals the market price of the common shares on the date of grant.

The following table summarizes RSU activity for the years ended August 31, 2012, 2013 and 2014:

	Years ended August 31,		
	2014	**2013**	**2012**
Outstanding – Beginning of year	1,333,092	1,337,730	1,551,658
Granted	336,685	316,160	334,878
Redeemed	(425,620)	(286,426)	(418,086)
Forfeited	(19,022)	(34,372)	(130,720)
Outstanding – End of year	1,225,135	1,333,092	1,337,730

None of the RSUs outstanding as at August 31, 2013 and 2014, were redeemable. The weighted average grant-date fair value of RSUs granted during the years ended August 31, 2012, 2013 and 2014, amounted to $5.90, $5.31 and $4.84 respectively.

The weighted-average market price of the shares at the date of redemption of RSUs redeemed during the years ended August 31, 2012, 2013 and 2014 was $6.07, $5.15 and $5.21 respectively.

Deferred Share Unit Plan

The company established a Deferred Share Unit (DSU) Plan for the members of the Board of Directors as part of their annual retainer fees. Each DSU entitles the Board members to receive one subordinate voting share. DSUs are acquired on the date of grant and are redeemed in subordinate voting shares when the Board member ceases to be Director of the company. This plan was approved by the shareholders of the company.

(tabular amounts in thousands of US dollars, except share and per share data and as otherwise noted)

The following table summarizes DSU activity for the years ended August 31, 2012, 2013 and 2014:

	Years ended August 31,		
	2014	**2013**	**2012**
Outstanding – Beginning of year	119,908	133,090	110,298
Granted	35,803	23,872	22,792
Redeemed	(38,010)	(37,054)	–
Outstanding – End of year	117,701	119,908	133,090

As at August 31, 2014, none of the DSUs outstanding were redeemable. As at August 31, 2013, 38,010 DSUs were redeemable. The weighted average grant-date fair value of DSUs granted during the years ended August 31, 2012, 2013 and 2014, amounted to $5.86, $4.84 and $4.59 respectively.

The weighted-average market price of the shares at the date of redemption of DSUs redeemed during the years ended August 31, 2013 and 2014, was $4.94 and $5.21 respectively.

Stock Appreciation Rights Plan

The company established the Stock Appreciation Rights Plan for certain employees. Under that plan, eligible employees are entitled to receive a cash amount equivalent to the difference between the market price of the common shares on the date of exercise and the exercise price determined on the date of grant. Stock appreciation rights granted under the plan expire 10 years from the date of grant and generally vest over a four-year period, being the required period of service from employees, generally with 25% vesting on an annual basis commencing on the first anniversary of the date of grant. This plan was approved by the shareholders of the company.

The following table summarizes stock appreciation rights activity for the years ended August 31, 2012, 2013 and 2014:

	Years ended August 31,					
	2014		**2013**		**2012**	
	Number	**Weighted average exercise price**	**Number**	**Weighted average exercise price**	**Number**	**Weighted average exercise price**
Outstanding – Beginning of year	37,224	$ 3	33,124	$ 3	29,124	$ 3
Granted	7,150	–	4,100	–	4,000	–
Expired	(4,500)	5	–	–	–	–
Outstanding – End of year	39,874	$ 2	37,224	$ 3	33,124	$ 3
Exercisable – End of year	22,374	$ 3	22,624	$ 4	15,787	$ 4

The liability arising from stock appreciation rights as at August 31, 2013 and 2014, amounted to $107,000 and $119,000 respectively and is recorded in accounts payable and accrued liabilities in the balance sheets.

(tabular amounts in thousands of US dollars, except share and per share data and as otherwise noted)

The following table summarizes information about stock appreciation rights as at August 31, 2014:

	Stock appreciation rights outstanding		Stock appreciation rights exercisable
Exercise price	**Number**	**Weighted average remaining contractual life**	**Number**
$ –	19,750	8 years	2,250
$2.36	9,674	4 years	9,674
$3.74 to $4.51	6,000	4 years	6,000
$6.28 to $6.50	4,450	2 years	4,450
	39,874	6 years	22,374

15 Related Party Disclosures

Ultimate controlling party

Mr. Germain Lamonde, the company's Chairman, President and Chief Executive Officer, is the company's ultimate controlling party.

Compensation of key management personnel

	Years ended August 31, 2014	2013	2012
Salaries and short-term employee benefits	$ 3,627	$ 3,442	$ 3,398
Restructuring charges	–	–	177
Stock-based compensation costs	906	907	793
	$ 4,533	$ 4,349	$ 4,368

Key management personnel includes senior management and directors.

16 Statements of earnings

Net research and development

Net research and development expenses comprise the following:

	Years ended August 31, 2014	2013	2012
Gross research and development expenses	$ 52,423	$ 54,334	$ 59,282
Research and development tax credits and grants	(7,577)	(8,890)	(9,428)
	$ 44,846	$ 45,444	$ 49,854

(tabular amounts in thousands of US dollars, except share and per share data and as otherwise noted)

Depreciation and amortization

Depreciation and amortization expenses by functional area are as follows:

	Years ended August 31, 2014	2013	2012
Cost of sales			
Depreciation of property, plant and equipment	$ 1,522	$ 1,651	$ 2,009
Amortization of intangible assets	2,087	4,027	5,076
	3,609	5,678	7,085
Selling and administrative expenses			
Depreciation of property, plant and equipment	951	1,100	1,037
Amortization of intangible assets	1,534	1,687	1,806
	2,485	2,787	2,843
Net research and development expenses			
Depreciation of property, plant and equipment	2,522	3,277	3,123
Amortization of intangible assets	777	929	937
	3,299	4,206	4,060
	$ 9,393	$ 12,671	$ 13,988
Depreciation of property, plant and equipment	$ 4,995	$ 6,028	$ 6,169
Amortization of intangible assets	4,398	6,643	7,819
	$ 9,393	$ 12,671	$ 13,988

Employee compensation

Employee compensation comprises the following:

	Years ended August 31, 2014	2013	2012
Salaries and benefits	$ 121,515	$ 122,433	$ 127,007
Restructuring charges	–	89	2,329
Stock-based compensation costs	1,696	1,768	1,862
	$ 123,211	$ 124,290	$ 131,198

Restructuring charges by functional area are as follows:

	Years ended August 31, 2014	2013	2012
Cost of sales	$ –	$ –	$ 264
Selling and administrative expenses	–	–	1,181
Net research and development costs	–	89	884
	$ –	$ 89	$ 2,329

(tabular amounts in thousands of US dollars, except share and per share data and as otherwise noted)

Stock-based compensation costs by functional area are as follows:

	Years ended August 31,		
	2014	2013	2012
Cost of sales	$ 191	$ 226	$ 248
Selling and administrative expenses	1,140	1,160	1,145
Net research and development expenses	365	382	469
	$ 1,696	$ 1,768	$ 1,862

17 Other Disclosures

Government grants

The company is entitled to receive grants on certain eligible research and development projects conducted in Finland from TEKES, a Finnish technology organization, which funds Finnish companies' high technology, research and innovations. The company's eligible research and development projects must be pre-approved by TEKES and the grant is subject to certain conditions. In the event that a condition is not met, TEKES can require reimbursement of a portion or the entire amount of the grant received. A liability to repay the funding is recognized in the period in which conditions arise that will cause the funding to be repayable. As at August 31, 2014, the company was in compliance with the conditions of the funding. This funding is accounted for as a reduction of gross research and development expenses in the statements of earnings. For the years ended August 31, 2012, 2013 and 2014, the company recorded $1,903,000, $1,498,000 and $1,348,000 respectively, under that program in the statements of earnings.

Defined contribution pension plans

The company maintains separate defined contribution pension plans for certain eligible employees. These plans, which are accounted for on an accrual basis, are summarized as follows:

- Canadian defined contribution pension plan

  The company maintains a plan for certain eligible employees residing in Canada, under which the company may elect to match the employees' contributions up to a maximum of 4% (3% prior to January 1, 2014) of an employee's gross salary. Cash contributions to this plan and expenses for the years ended August 31, 2012, 2013 and 2014, amounted to $1,178,000, $1,165,000 and $1,451,000 respectively.

- US defined contribution pension plan (401K plan)

  The company maintains a 401K plan for eligible employees residing in the U.S. Under this plan, the company must contribute an amount equal to 3% of an employee's current compensation. In addition, eligible employees may contribute up to the lesser of 1% of eligible compensation or the statutorily prescribed annual limit to the 401K plan. The 401K plan permits but does not require the company to make additional matching contributions to the 401K plan on behalf of the eligible participants, subject to a maximum of 50% of the first 6% of the participant's current compensation subject to certain legislated maximum contribution limits. During the years ended August 31, 2012, 2013 and 2014, the company recorded cash contributions and expenses totaling $693,000, $632,000 and $616,000 respectively.

(tabular amounts in thousands of US dollars, except share and per share data and as otherwise noted)

18 Income Taxes

The reconciliation of the income tax provision calculated using the combined Canadian federal and provincial statutory income tax rate with the income tax provision in the financial statements is as follows:

	Years ended August 31,		
	2014	2013	2012
Income tax provision (recovery) at combined Canadian federal and provincial statutory tax rate (27%)	$ 1,421	$ 1,891	$ (6)
Increase (decrease) due to:			
Foreign income taxed at different rates	(20)	(249)	285
Non-taxable (income)/loss	(540)	(2,077)	535
Non-deductible expenses	1,011	792	1,028
Foreign exchange effect of translation of foreign subsidiaries	(547)	148	(2,205)
Recognition of previously unrecognized deferred income tax assets	–	–	(557)
Unrecognized deferred income tax assets on temporary deductible differences and unused tax losses	3,013	4,385	4,509
Other	141	774	(18)
Income tax provision for the year	$ 4,479	$ 5,664	$ 3,571

	Years ended August 31,		
	2014	2013	2012
The income tax provision consists of the following:			
Current			
Current income taxes	$ 3,588	$ 2,713	$ 1,521
Deferred			
Deferred income taxes relating to the origination and reversal of temporary differences	(2,122)	(1,434)	(1,902)
Benefit arising from previously unrecognized tax losses and deductible temporary differences	–	–	(557)
	(2,122)	(1,434)	(2,459)
Unrecognized deferred income tax assets on temporary deductible differences and unused tax losses	3,013	4,385	4,509
	891	2,951	2,050
Income tax provision for the year	$ 4,479	$ 5,664	$ 3,571

(tabular amounts in thousands of US dollars, except share and per share data and as otherwise noted)

Deferred taxes

	As at August 31, 2014	As at August 31, 2013
Deferred income tax assets		
Deferred income tax assets recoverable within 12 months	$ 3,142	$ 3,193
Deferred income tax assets recoverable after 12 months	6,674	7,614
	9,816	10,807
Deferred income tax liabilities		
Deferred income tax liabilities payable within 12 months	529	252
Deferred income tax liabilities payable after 12 months	2,558	2,974
	3,087	3,226
Deferred income tax assets net	$ 6,729	$ 7,581

The changes in deferred income tax assets and liabilities for the year ended August 31, 2013 are as follows:

	Balance as at September 1, 2012	Credited (charged) to the statement of earnings	Credited (charged) to shareholders' equity	Foreign currency translation adjustment	Balance as at August 31, 2013
Deferred income tax assets					
Long-lived assets	$ 4,389	$ (449)	$ –	$ (201)	$ 3,739
Provisions and accruals	3,431	213	403	(197)	3,850
Deferred revenue	2,044	(164)	–	(85)	1,795
Research and development expenses	2,362	(608)	–	(125)	1,629
Losses carried forward	9,207	(808)	–	(8)	8,391
Deferred income tax liabilities					
Long-lived assets	(494)	45	–	28	(421)
Research and development tax credits	(10,964)	(1,180)	–	742	(11,402)
Total	$ 9,975	$ (2,951)	$ 403	$ 154	$ 7,581
Classified as follows:					
Deferred income tax assets	$ 12,080				$ 10,807
Deferred income tax liabilities	(2,105)				(3,226)
	$ 9,975				$ 7,581

(tabular amounts in thousands of US dollars, except share and per share data and as otherwise noted)

The changes in deferred income tax assets and liabilities for the year ended August 31, 2014 are as follows:

	Balance as at September 1, 2013	Credited (charged) to the statement of earnings	Credited (charged) to shareholders' equity	Foreign currency translation adjustment	Balance as at August 31, 2014
Deferred income tax assets					
Long-lived assets	$ 3,739	$ (812)	$ –	$ (90)	$ 2,837
Provisions and accruals	3,850	229	(91)	(50)	3,938
Deferred revenue	1,795	(120)	–	(37)	1,638
Research and development expenses	1,629	1,160	–	(57)	2,732
Losses carried forward	8,391	(991)	–	6	7,406
Deferred income tax liabilities					
Long-lived assets	(421)	371	–	9	(41)
Research and development tax credits	(11,402)	(728)	–	349	(11,781)
Total	$ 7,581	$ (891)	$ (91)	$ 130	$ 6,729
Classified as follows:					
Deferred income tax assets	$ 10,807				$ 9,816
Deferred income tax liabilities	(3,226)				(3,087)
	$ 7,581				$ 6,729

Unrecognized deferred income tax assets on temporary deductible differences, unused tax losses and research and development expenses are as follows:

	As at August 31	
	2014	**2013**
Temporary deductible differences	$ 1,050	$ 205
Losses carried forward	35,806	35,914
Research and development expenses	641	1,370
	$ 37,497	$ 37,489

(tabular amounts in thousands of US dollars, except share and per share data and as otherwise noted)

As at August 31, 2014, the year of expiry of operating losses and research and development expenses for which no deferred income tax assets were recognized in the balance sheets are as follows, presented by tax jurisdiction:

	Canada				
Year of expiry	**Federal**	**Provincial**	**Finland**	**United States**	**Other**
2015	$ –	$ 1,096	$ 1,539	$ 997	$ –
2016	–	–	–	553	–
2017	–	–	4	–	–
2018	–	–	382	–	–
2019	–	–	–	741	–
2020	–	–	8,747	3,470	–
2021	–	–	7,582	10,202	–
2022	–	–	13,145	7,435	–
2023	–	–	8,516	1,972	–
2024	–	–	2,269	1,351	–
2025	–	–	–	1,351	–
2026	–	990	–	1,351	–
2027	–	1,256	–	1,351	–
2028	–	–	–	2,447	–
2030	11	11	–	2,713	–
2031	35	35	–	109	–
2032	8	8	–	–	–
2033	44	44	–	4,681	–
2034	17	17	–	4,684	–
Indefinite	–	–	–	–	2,216
	$ 115	$ 3,457	$ 42,184	$ 45,408	$ 2,216

Furthermore, as at August 31, 2014, the company had available capital losses in Canada amounting to $62,818,000 at the federal level and $66,827,000 at the provincial level for which no deferred income tax assets were recognized. These losses can be carried forward indefinitely against capital gains.

As at August 31, 2014, non-refundable research and development tax credits recognized in the balance sheet amounted to $42,864,000. In order to recover these non-refundable research and development tax credits, the company needs to generate approximately $277,000,000 (CA$301,000,000) in pre-tax earnings at the Canadian federal level and approximately $13,000,000 at the Canadian provincial level. In order to generate $277,000,000 in pre-tax earnings at the Canadian Federal level over the estimated recovery period of 18 years, the company must generate a pre-tax earnings compound annual growth rate (CAGR) of 4%, which the company believes is probable. The company's non-refundable research and development tax credits can be carried forward over a twenty-year period.

In addition, as at August 31, 2014, the company had deferred income tax assets in the balance sheet in the amount of $9,816,000 mainly for operating losses in the United States. In order to recover these deferred income tax assets, the company needs to generate approximately $25,000,000 in pre-tax earnings at the United States, and in order to do so over the estimated recovery period of six years, the company must generate pre-tax earnings CAGR of 9%, which the company believes is probable. The company's operating losses in the United States can be carried forward over a twenty-year period.

(tabular amounts in thousands of US dollars, except share and per share data and as otherwise noted)

As at August 31, 2014, taxable temporary differences of $9,393,000 were not recognized for taxes that would be payable on the unremitted earnings of certain of the company's subsidiaries, as the company has determined that:

(1) Undistributed profits of its foreign subsidiaries will not be distributed in the foreseeable future; and
(2) Undistributed profits of its domestic subsidiaries will not be taxable when distributed.

19 Earnings per Share

The following table summarizes the reconciliation of the basic weighted average number of shares outstanding and the diluted weighted average number of shares outstanding:

	Years ended August 31,		
	2014	**2013**	**2012**
Basic weighted average number of shares outstanding (000's)	60,329	60,323	60,453
Plus dilutive effect of (000's):			
Stock options	9	24	149
Restricted share units	574	648	910
Deferred share units	103	115	118
Diluted weighted average number of shares outstanding (000's)	61,015	61,110	61,630
Stock awards excluded from the calculation of the diluted weighted average number of shares outstanding because their exercise price was greater than the average market price of the common shares (000's)	77	75	54

For the year ended August 31, 2012, the diluted amount per share was the same amount as the basic amount per share since the dilutive effect of stock options, restricted share units and deferred share units was not included in the calculation; otherwise, the effect would have been antidilutive. Accordingly, the diluted amount per share for that year was calculated using the basic weighted average number of shares outstanding.

20 Segment Information

Sales for products and services are detailed as follows:

	Years ended August 31,		
	2014	**2013**	**2012**
Products	$ 201,724	$ 213,042	$ 220,356
Services	29,082	29,108	29,610
	$ 230,806	$ 242,150	$ 249,966

(tabular amounts in thousands of US dollars, except share and per share data and as otherwise noted)

Sales to external customers by geographic region are detailed as follows:

	Years ended August 31,		
	2014	2013	2012
United States	$ 83,172	$ 87,145	$ 83,401
Canada	19,482	26,073	29,944
Other	19,195	14,910	17,838
Americas	121,849	128,128	131,183
United Kingdom	12,736	13,206	9,862
Other	51,243	53,802	61,449
Europe, Middle-East and Africa	63,979	67,008	71,311
China	22,468	21,778	21,802
Other	22,510	25,236	25,670
Asia-Pacific	44,978	47,014	47,472
	$ 230,806	$ 242,150	$ 249,966

Sales were allocated to geographic regions based on the country of residence of the related customers.

Long-lived assets by geographic region are detailed as follows:

	As at August 31, 2014			As at August 31, 2013		
	Property, plant and equipment	Intangible assets	Goodwill	Property, plant and equipment	Intangible assets	Goodwill
Canada	$ 33,094	$ 2,006	$ –	$ 34,833	$ 2,274	$ –
United States	1,333	1,960	16,023	1,305	186	16,522
Finland	448	3,231	10,465	589	4,762	10,791
India	5,479	56	–	6,190	42	–
China	1,397	32	–	1,517	25	–
Other	1,029	8	–	1,089	254	–
	$ 42,780	$ 7,293	$ 26,488	$ 45,523	$ 7,543	$ 27,313