

EXFO Inc.
Condensed Unaudited Interim Consolidated Balance Sheets

(in thousands of US dollars)

	As at May 31, 2014	As at August 31, 2013
Assets		
Current assets		
Cash	\$ 47,423	\$ 45,386
Short-term investments	5,321	4,868
Accounts receivable		
Trade	52,930	50,117
Other	2,332	2,778
Income taxes and tax credits recoverable	6,326	6,525
Inventories	37,376	35,705
Prepaid expenses	2,612	2,561
	154,320	147,940
Tax credits recoverable	42,388	41,719
Property, plant and equipment	43,166	45,523
Intangible assets	6,745	7,543
Goodwill	26,527	27,313
Deferred income taxes	10,323	10,807
Other assets	786	693
	\$ 284,255	\$ 281,538
Liabilities		
Current liabilities		
Accounts payable and accrued liabilities	\$ 35,919	\$ 26,253
Provisions	572	756
Income taxes payable	777	679
Current portion of long-term debt	–	296
Deferred revenue	9,480	9,467
	46,748	37,451
Deferred revenue	3,131	3,932
Deferred income taxes	4,090	3,226
Other liabilities	452	477
	54,421	45,086
Shareholders' equity		
Share capital (note 4)	111,491	109,837
Contributed surplus	16,081	17,186
Retained earnings	112,431	112,852
Accumulated other comprehensive loss	(10,169)	(3,423)
	229,834	236,452
	\$ 284,255	\$ 281,538

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

EXFO Inc.

Condensed Unaudited Interim Consolidated Statements of Earnings

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

	Three months ended May 31, 2014	Nine months ended May 31, 2014	Three months ended May 31, 2013	Nine months ended May 31, 2013
Sales	\$ 63,882	\$ 171,064	\$ 58,865	\$ 181,262
Cost of sales ⁽¹⁾ (note 5)	23,469	64,727	22,574	69,895
Selling and administrative (note 5)	21,730	64,975	22,002	67,366
Net research and development (note 5)	11,745	33,999	11,573	35,135
Depreciation of property, plant and equipment (note 5)	1,219	3,737	1,473	4,582
Amortization of intangible assets (note 5)	1,025	3,281	1,586	5,470
Interest and other income	(220)	(296)	(68)	(76)
Foreign exchange (gain) loss	1,126	(1,968)	(314)	(2,770)
Earnings before income taxes	3,788	2,609	39	1,660
Income taxes (note 6)	2,123	3,030	901	4,121
Net earnings (loss) for the period	<u>\$ 1,665</u>	<u>\$ (421)</u>	<u>\$ (862)</u>	<u>\$ (2,461)</u>
Basic and diluted net earnings (loss) per share	\$ 0.03	\$ (0.01)	\$ (0.01)	\$ (0.04)
Basic weighted average number of shares outstanding (000's)	60,339	60,323	60,377	60,386
Diluted weighted average number of shares outstanding (000's) (note 7)	60,986	60,323	60,377	60,386

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

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

EXFO Inc.

Condensed Unaudited Interim Consolidated Statements of Comprehensive Income (Loss)

(in thousands of US dollars)

	Three months ended May 31, 2014	Nine months ended May 31, 2014	Three months ended May 31, 2013	Nine months ended May 31, 2013
Net earnings (loss) for the period	\$ 1,665	\$ (421)	\$ (862)	\$ (2,461)
Other comprehensive income (loss), net of income taxes				
Items that will not be reclassified subsequently to net earnings				
Foreign currency translation adjustment	4,736	(6,792)	(1,252)	(12,144)
Items that may be reclassified subsequently to net earnings				
Unrealized gains/losses on forward exchange contracts	835	(694)	(112)	(874)
Reclassification of realized gains/losses on forward exchange contracts in net earnings (loss)	391	756	48	(281)
Deferred income tax effect of gains/losses on forward exchange contracts	(328)	(16)	17	310
Other comprehensive income (loss)	<u>5,634</u>	<u>(6,746)</u>	<u>(1,299)</u>	<u>(12,989)</u>
Comprehensive income (loss) for the period	<u>\$ 7,299</u>	<u>\$ (7,167)</u>	<u>\$ (2,161)</u>	<u>\$ (15,450)</u>

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

EXFO Inc.

Condensed Unaudited Interim Consolidated Statements of Changes in Shareholders' Equity

(in thousands of US dollars)

	Nine months ended May 31, 2013				
	Share capital	Contributed surplus	Retained earnings	Accumulated other comprehensive income	Total shareholders' equity
Balance as at September 1, 2012	\$ 110,965	\$ 17,298	\$ 111,511	\$ 13,507	\$ 253,281
Exercise of stock options (note 4)	87	–	–	–	87
Redemption of share capital (note 4)	(1,892)	(409)	–	–	(2,301)
Reclassification of stock-based compensation costs (note 4)	1,350	(1,350)	–	–	–
Stock-based compensation costs	–	1,333	–	–	1,333
Net loss for the period	–	–	(2,461)	–	(2,461)
Other comprehensive loss					
Foreign currency translation adjustment	–	–	–	(12,144)	(12,144)
Changes in unrealized gains/losses on forward exchange contracts, net of deferred income taxes of \$310	–	–	–	(845)	(845)
Total comprehensive loss for the period	–	–	(2,461)	(12,989)	(15,450)
Balance as at May 31, 2013	<u>\$ 110,510</u>	<u>\$ 16,872</u>	<u>\$ 109,050</u>	<u>\$ 518</u>	<u>\$ 236,950</u>

	Nine months ended May 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 4)	225	–	–	–	225
Redemption of share capital (note 4)	(831)	(106)	–	–	(937)
Reclassification of stock-based compensation costs (note 4)	2,260	(2,260)	–	–	–
Stock-based compensation costs	–	1,261	–	–	1,261
Net loss for the period	–	–	(421)	–	(421)
Other comprehensive income (loss)					
Foreign currency translation adjustment	–	–	–	(6,792)	(6,792)
Changes in unrealized losses on forward exchange contracts, net of deferred income taxes of \$16	–	–	–	46	46
Total comprehensive loss for the period	–	–	(421)	(6,746)	(7,167)
Balance as at May 31, 2014	<u>\$ 111,491</u>	<u>\$ 16,081</u>	<u>\$ 112,431</u>	<u>\$ (10,169)</u>	<u>\$ 229,834</u>

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

EXFO Inc.

Condensed Unaudited Interim Consolidated Statements of Cash Flows

(in thousands of US dollars)

	Three months ended May 31, 2014	Nine months ended May 31, 2014	Three months ended May 31, 2013	Nine months ended May 31, 2013
Cash flows from operating activities				
Net earnings (loss) for the period	\$ 1,665	\$ (421)	\$ (862)	\$ (2,461)
Add (deduct) items not affecting cash				
Changes in discount on short-term investments	–	–	1	–
Stock-based compensation costs	407	1,272	415	1,331
Depreciation and amortization	2,244	7,018	3,059	10,052
Deferred revenue	209	(519)	1,661	241
Deferred income taxes	1,147	1,448	263	1,984
Changes in foreign exchange gain/loss	378	(523)	(78)	(876)
	<u>6,050</u>	<u>8,275</u>	<u>4,459</u>	<u>10,271</u>
Changes in non-cash operating items				
Accounts receivable	(8,208)	(3,683)	(4,569)	(10,657)
Income taxes and tax credits	(759)	(1,702)	985	(2,201)
Inventories	727	(2,806)	(262)	791
Prepaid expenses	492	(124)	(804)	(859)
Other assets	53	19	–	–
Accounts payable, accrued liabilities and provisions	4,565	9,956	1,553	1,503
Other liabilities	(35)	(78)	(25)	(235)
	<u>2,885</u>	<u>9,857</u>	<u>1,337</u>	<u>(1,387)</u>
Cash flows from investing activities				
Additions to short-term investments	(9,821)	(24,392)	(9,934)	(44,703)
Proceeds from disposal and maturity of short-term investments	9,244	23,806	9,921	47,731
Additions to capital assets	(2,750)	(5,146)	(1,459)	(5,952)
	<u>(3,327)</u>	<u>(5,732)</u>	<u>(1,472)</u>	<u>(2,924)</u>
Cash flows from financing activities				
Repayment of long-term debt	–	(307)	–	(293)
Exercise of stock options	30	225	–	87
Redemption of share capital	–	(937)	(1,161)	(2,301)
	<u>30</u>	<u>(1,019)</u>	<u>(1,161)</u>	<u>(2,507)</u>
Effect of foreign exchange rate changes on cash				
	<u>771</u>	<u>(1,069)</u>	<u>(271)</u>	<u>(2,192)</u>
Change in cash	359	2,037	(1,567)	(9,010)
Cash – Beginning of the period	<u>47,064</u>	<u>45,386</u>	<u>51,425</u>	<u>58,868</u>
Cash – End of the period	<u>\$ 47,423</u>	<u>\$ 47,423</u>	<u>\$ 49,858</u>	<u>\$ 49,858</u>
Supplementary information				
Interest paid	\$ 6	\$ 15	\$ 2	\$ 28
Income taxes paid	\$ 271	\$ 1,142	\$ 118	\$ 1,055
Additions to capital assets	\$ 2,734	\$ 5,414	\$ 1,088	\$ 3,335

As at May 31, 2013 and 2014, unpaid purchases of capital assets amounted to \$279 and \$499 respectively.

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

EXFO Inc.

Notes to Condensed Unaudited Interim 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 and service assurance solutions for wireless and wireline network operators and equipment manufacturers in the global telecommunications industry. The company offers core-to-edge solutions to 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 condensed interim consolidated financial statements were authorized for issue by the Board of Directors on June 25, 2014.

2 Basis of Presentation

These condensed interim consolidated financial statements have been prepared in accordance with the International Financial Reporting Standards (IFRS), as issued by the International Accounting Standards Board (IASB) applicable to the preparation of interim financial statements, including IAS 34, “*Interim Financial Reporting*”, and using the same accounting policies and methods used in the preparation of the company’s most recent annual consolidated financial statements except for the changes in accounting policies described below. Consequently, these condensed interim consolidated financial statements should be read in conjunction with the company’s most recent annual consolidated financial statements, which have been prepared in accordance with IFRS as issued by the IASB.

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.

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

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 3).

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

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 1st 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 Financial Instruments

Fair value of financial instruments

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.

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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 exchange rates at the balance sheet dates.

The fair value of forward exchange contract represents the amount at which they could be settled based on estimated current market rates.

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

	As at May 31, 2014		As at August 31, 2013	
	Level 1	Level 2	Level 1	Level 2
Financial assets				
Short-term investments	\$ 5,321	\$ –	\$ 4,868	\$ –
Forward exchange contracts	\$ –	\$ 139	\$ –	\$ –
Financial liabilities				
Forward exchange contracts	\$ –	\$ 800	\$ –	\$ 722

Derivative Financial Instruments

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 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 May 31, 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

<u>Expiry dates</u>	<u>Contractual amounts</u>	<u>Weighted average contractual forward rates</u>
June 2014 to August 2014	\$ 5,400	1.0346
September 2014 to August 2015	18,200	1.0589
September 2015 to August 2016	13,400	1.0923
September 2016 to December 2016	3,400	1.1063
Total	<u>\$ 40,400</u>	<u>1.0707</u>

US dollars – Indian rupees

<u>Expiry dates</u>	<u>Contractual amounts</u>	<u>Weighted average contractual forward rate</u>
September 2014 to March 2015	<u>\$ 1,750</u>	<u>62.22</u>

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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 as at August 31, 2013 and \$826,000 as at May 31, 2014.

Based on the portfolio of forward exchange contracts as at May 31, 2014, the company estimates that the portion of the 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 \$590,000.

As at May 31, 2014, forward exchange contracts in the amount of \$139,000 are presented as long-term assets in other assets, forward exchange contracts in the amount of \$590,000 are presented as current liabilities in accounts payable and accrued liabilities and forward exchange contracts of \$210,000 are presented as long-term liabilities in other liabilities in the balance sheet. These forward exchange contracts are not yet recorded in the statement of earnings.

During the three and nine months ended May 31, 2013 and 2014, the company recognized within its sales the following gains or losses on forward exchange contracts:

	Three months ended May 31, 2014	Nine months ended May 31, 2014	Three months ended May 31, 2013	Nine months ended May 31, 2013
Gains (losses) on forward exchange contracts	<u>\$ (352)</u>	<u>\$ (721)</u>	<u>\$ 44</u>	<u>\$ 399</u>

4 Share Capital

On January 8, 2014, the company announced that its Board of Directors 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 company expects to use cash, short-term investments or future cash flows from operations to fund the repurchase of shares. The normal course issuer bid started on January 13, 2014, and will end on January 12, 2015, or on an earlier date if the company repurchases the maximum number of shares permitted under the bid. The program does not require that the company repurchases any specific number of shares, and it may be modified, suspended or terminated at any time and without prior notice. All shares repurchased under the bid will be cancelled.

EXFO Inc.

Notes to Condensed Unaudited Interim Consolidated Financial Statements

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

The following tables summarize changes in share capital for the nine months ended May 31, 2013 and 2014.

	Nine months ended May 31, 2013				
	Multiple voting shares		Subordinate voting shares		Total amount
	Number	Amount	Number	Amount	
Balance as at September 1, 2012	31,643,000	\$ 1	28,710,891	\$ 110,964	\$ 110,965
Exercise of stock options	-	-	23,275	51	51
Redemption of restricted share units	-	-	127,949	-	-
Redemption of share capital	-	-	(205,123)	(793)	(793)
Reclassification of stock-based compensation costs to share capital upon exercise of stock awards	-	-	-	612	612
Balance as at November 30, 2012	31,643,000	1	28,656,992	110,834	110,835
Exercise of stock options	-	-	7,400	36	36
Redemption of restricted share units	-	-	141,725	-	-
Redemption of deferred share units	-	-	37,054	-	-
Redemption of share capital	-	-	(31,210)	(120)	(120)
Reclassification of stock-based compensation costs to share capital upon exercise of stock awards	-	-	-	649	649
Balance as at February 28, 2013	31,643,000	1	28,811,961	111,399	111,400
Redemption of restricted share units	-	-	16,752	-	-
Redemption of share capital	-	-	(252,974)	(979)	(979)
Reclassification of stock-based compensation costs to share capital upon exercise of stock awards	-	-	-	89	89
Balance as at May 31, 2013	<u>31,643,000</u>	<u>\$ 1</u>	<u>28,575,739</u>	<u>\$ 110,509</u>	<u>\$ 110,510</u>

EXFO Inc.

Notes to Condensed Unaudited Interim Consolidated Financial Statements

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

	Nine months ended May 31, 2014				
	Multiple voting shares		Subordinate voting shares		Total Amount
	Number	Amount	Number	Amount	
Balance as at September 1, 2013	31,643,000	\$ 1	28,401,790	\$ 109,836	\$ 109,837
Exercise of stock options	-	-	25,800	106	106
Redemption of restricted share units	-	-	315,583	-	-
Redemption of deferred share units	-	-	38,010	-	-
Reclassification of stock-based compensation costs to share capital upon exercise of stock awards	-	-	-	1,435	1,435
Balance as at November 30, 2013	31,643,000	1	28,781,183	111,377	111,378
Exercise of stock options	-	-	20,500	89	89
Redemption of restricted share units	-	-	95,882	-	-
Redemption of share capital	-	-	(214,470)	(831)	(831)
Reclassification of stock-based compensation costs to share capital upon exercise of stock awards	-	-	-	701	701
Balance as at February 28, 2014	31,643,000	1	28,683,095	111,336	111,337
Exercise of stock options	-	-	6,500	30	30
Redemption of restricted share units	-	-	14,155	-	-
Reclassification of stock-based compensation costs to share capital upon exercise of stock awards	-	-	-	124	124
Balance as at May 31, 2014	<u>31,643,000</u>	<u>\$ 1</u>	<u>28,703,750</u>	<u>\$ 111,490</u>	<u>\$ 111,491</u>

5 Statements of Earnings

Net research and development expenses comprise the following:

	Three months ended May 31, 2014	Nine months ended May 31, 2014	Three months ended May 31, 2013	Nine months ended May 31, 2013
Gross research and development expenses	\$ 13,616	\$ 39,971	\$ 13,782	\$ 41,806
Research and development tax credits and grants	(1,871)	(5,972)	(2,209)	(6,671)
	<u>\$ 11,745</u>	<u>\$ 33,999</u>	<u>\$ 11,573</u>	<u>\$ 35,135</u>

Gross research and development expenses for the nine months ended May 31, 2013 include \$89,000 in restructuring charges.

EXFO Inc.

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

Inventory write-down is as follows:

	Three months ended May 31, 2014	Nine months ended May 31, 2014	Three months ended May 31, 2013	Nine months ended May 31, 2013
Inventory write-down for the period	\$ 1,181	\$ 3,619	\$ 1,042	\$ 2,979

Depreciation and amortization expenses by functional area are as follows:

	Three months ended May 31, 2014	Nine months ended May 31, 2014	Three months ended May 31, 2013	Nine months ended May 31, 2013
Cost of sales				
Depreciation of property, plant and equipment	\$ 377	\$ 1,141	\$ 398	\$ 1,265
Amortization of intangible assets	465	1,527	938	3,469
	<u>842</u>	<u>2,668</u>	<u>1,336</u>	<u>4,734</u>
Selling and administrative expenses				
Depreciation of property, plant and equipment	234	715	272	844
Amortization of intangible assets	377	1,152	417	1,291
	<u>611</u>	<u>1,867</u>	<u>689</u>	<u>2,135</u>
Net research and development expenses				
Depreciation of property, plant and equipment	608	1,881	803	2,473
Amortization of intangible assets	183	602	231	710
	<u>791</u>	<u>2,483</u>	<u>1,034</u>	<u>3,183</u>
	<u>\$ 2,244</u>	<u>\$ 7,018</u>	<u>\$ 3,059</u>	<u>\$ 10,052</u>
Depreciation of property, plant and equipment	\$ 1,219	\$ 3,737	\$ 1,473	\$ 4,582
Amortization of intangible assets	<u>1,025</u>	<u>3,281</u>	<u>1,586</u>	<u>5,470</u>
	<u>\$ 2,244</u>	<u>\$ 7,018</u>	<u>\$ 3,059</u>	<u>\$ 10,052</u>

Employee compensation comprises the following:

	Three months ended May 31, 2014	Nine months ended May 31, 2014	Three months ended May 31, 2013	Nine months ended May 31, 2013
Salaries and benefits	\$ 31,133	\$ 91,853	\$ 30,732	\$ 93,962
Stock-based compensation costs	407	1,272	415	1,331
Total employee compensation for the period	<u>\$ 31,540</u>	<u>\$ 93,125</u>	<u>\$ 31,147</u>	<u>\$ 95,293</u>

EXFO Inc.

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(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:

	Three months ended May 31, 2014	Nine months ended May 31, 2014	Three months ended May 31, 2013	Nine months ended May 31, 2013
Cost of sales	\$ 45	\$ 145	\$ 58	\$ 170
Selling and administrative expenses	264	856	252	875
Net research and development expenses	98	271	105	286
Total stock-based compensation for the period	<u>\$ 407</u>	<u>\$ 1,272</u>	<u>\$ 415</u>	<u>\$ 1,331</u>

6 Income taxes

For the three months and the nine months ended May 31, 2013 and 2014, 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:

	Three months ended May 31, 2014	Nine months ended May 31, 2014	Three months ended May 31, 2013	Nine months ended May 31, 2013
Income tax provision at combined Canadian federal and provincial statutory tax rate (27%)	\$ 1,023	\$ 705	\$ 11	\$ 448
Increase (decrease) due to:				
Foreign income taxed at different rates	83	(27)	(45)	(323)
Non-taxable income	(187)	(1,080)	(227)	(1,391)
Non-deductible expenses	387	794	184	607
Foreign exchange effect of translation of foreign subsidiaries	(151)	61	(223)	61
Unrecognized deferred income tax assets on temporary deductible differences and unused tax losses	584	2,515	1,226	3,920
Other	384	62	(25)	799
Income tax provision for the period	<u>\$ 2,123</u>	<u>\$ 3,030</u>	<u>\$ 901</u>	<u>\$ 4,121</u>

EXFO Inc.

Notes to Condensed Unaudited Interim Consolidated Financial Statements

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

The income tax provision consists of the following:

	Three months ended May 31, 2014	Nine months ended May 31, 2014	Three months ended May 31, 2013	Nine months ended May 31, 2013
Current	\$ 976	\$ 1,582	\$ 638	\$ 2,137
Deferred	1,147	1,448	263	1,984
	<u>\$ 2,123</u>	<u>\$ 3,030</u>	<u>\$ 901</u>	<u>\$ 4,121</u>

7 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:

	Three months ended May 31, 2014	Nine months ended May 31, 2014	Three months ended May 31, 2013	Nine months ended May 31, 2013
Basic weighted average number of shares outstanding (000's)	60,339	60,323	60,377	60,386
Plus dilutive effect of (000's):				
Stock options	2	12	20	28
Restricted share units	546	570	619	640
Deferred share units	99	101	107	116
	<u>60,986</u>	<u>61,006</u>	<u>61,123</u>	<u>61,170</u>
Diluted weighted average number of shares outstanding (000's)				
Stock awards excluded from the calculation of diluted weighted average number of shares because their exercise price was greater than the average market price of the common shares (000's)	25	94	9	71

For the three and nine months ended May 31, 2013 and the nine months ended May 31, 2014, 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 these periods was calculated using the basic weighted average number of shares outstanding.