MANAGEMENT'S DISCUSSION AND ANALYSIS

ON FORM 51-102F1

THREE AND NINE MONTHS ENDED

MAY 31, 2017

July 13, 2017

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INTRODUCTION

This management's discussion and analysis (MD&A) relates to the unaudited interim consolidated financial condition, results of operations, comprehensive income and cash flows for the three and nine months ended May 31, 2017 (Q3 fiscal 2017) of NAV CANADA and its subsidiaries (also referred to in this MD&A as we, our, us or the Company). It should be read in conjunction with our unaudited interim condensed consolidated financial statements for Q3 fiscal 2017 (Q3 fiscal 2017 financial statements), our audited annual consolidated financial statements and the accompanying notes for the year ended August 31, 2016 (fiscal 2016), our fiscal 2016 annual MD&A, as well as our 2016 Annual Information Form dated October 27, 2016 (fiscal 2016 AIF). Additional information about NAV CANADA, including our consolidated financial statements for Q3 fiscal 2017 and fiscal 2016, our fiscal 2016 annual MD&A, and our fiscal 2016 AIF are filed on the System for Electronic Document Analysis and Retrieval (SEDAR) at www.sedar.com.

Our financial statements are prepared in Canadian dollars (CDN) and in accordance with International Financial Reporting Standards (IFRS). Our Q3 fiscal 2017 financial statements have been prepared in accordance with International Accounting Standards (IAS) 34 *Interim Financial Reporting*. Our Audit & Finance Committee reviewed this MD&A and our Board of Directors (the Board) approved it before it was filed.

Caution Concerning Forward-Looking Information

This MD&A and, in particular, but without limitation, sections "INTRODUCTION – Significant Financial Matters: Air Traffic and Customer Service Charges", "RESULTS OF OPERATIONS – Revenue: Customer Service Charges" and "RESULTS OF OPERATIONS – Financial Outlook" of this MD&A, contain certain statements about NAV CANADA's future expectations. These statements are generally identified by words like "anticipate", "plan", "believe", "intend", "expect", "estimate", "approximate" and the like, as well as future or conditional verbs such as "will", "should", "would" and "could", or negative versions thereof. Because forward-looking statements involve future risks and uncertainties, actual results may be quite different from those expressed or implied in these statements. Examples include geopolitical unrest, terrorist attacks and the threat of terrorist attacks, war, epidemics or pandemics, natural disasters, weather patterns, environmental concerns, cyber security attacks, labour negotiations, arbitrations, workforce recruitment, training and retention, general aviation industry conditions, air traffic levels, the use of telecommunications and ground transportation as alternatives to air travel, capital market and economic conditions, the ability to collect customer service charges and reduce operating costs, the satisfaction of criteria for the remaining Aireon LLC (Aireon) investment tranche, the success of our investment in space-based aircraft surveillance through Aireon, credit losses on investments, changes in interest rates, changes in laws, tax changes, adverse regulatory developments or proceedings and lawsuits. Some of these risks and uncertainties are explained under "Risk Factors" in our fiscal 2016 AIF. The forward-looking statements contained in this MD&A represent our expectations as of July 13, 2017 and are subject to change after this date. Readers of this MD&A are cautioned not to place undue reliance on any forward-looking statement. We disclaim any intention or obligation to update or revise any forward-looking statements included in this document whether as a result of new information, future events or for any other reason, except as required by applicable securities legislation.

Our Business

NAV CANADA is the private sector, non-share capital company that operates Canada's civil air navigation system (ANS). With operations across Canada, we provide air navigation services to aircraft owners and operators within Canadian–controlled airspace. These services include air traffic control, flight information, weather briefings, airport advisories, aeronautical information and electronic navigation aids.

The core business of the Company is to manage and operate the ANS and related services in a safe, efficient and cost effective manner. Our mandate covers both Canadian airspace and airspace delegated to Canada under international agreements.

Financial Strategy and Rate Regulation

In establishing new customer service charges or revising existing charges, we must follow the charging principles set out in our governing legislation, the *Civil Air Navigation Services Commercialization Act* (ANS Act), which prevents us from setting customer service charges higher than what is needed to meet our financial requirements for the provision of air navigation services. Pursuant to these principles, the Board approves the amount and timing of changes to customer service charges. The Board also approves the Company's annual budget where the amounts to be recovered through customer service charges for the ensuing year are determined. Our aim is essentially to achieve breakeven financial results on an annual basis. Due to seasonal and other fluctuations in air traffic and given that our costs are predominantly fixed in nature, our quarterly financial results may not achieve a breakeven position, after recording adjustments to the rate stabilization account. This is illustrated in the table under the heading "SUMMARY OF QUARTERLY RESULTS – Quarterly Financial Information (unaudited)".

As noted above, customer service charges are set based on the Company's financial requirements, which take into account estimated air traffic volumes and planned expenses. Since actual revenue and expenses will differ from these estimates, methods to accumulate the variances are required so that they may be taken into account when setting future customer service charges. There is also a need to absorb the immediate effect of unpredictable factors – mainly fluctuations in air traffic volumes resulting from unforeseen events. We meet these objectives through a "rate stabilization" mechanism, as explained hereafter.

In preparing our consolidated financial statements, the timing of recognition of certain revenue and expenses differs from what would otherwise be expected for companies that are not subject to regulatory statutes governing the level of charges. For example, we adjust our net income (loss) through transfers to or from the rate stabilization account, based on variations from the amounts that were used when establishing customer service charges. If our actual revenue exceeds actual expenses, the excess is reflected as a credit to the rate stabilization account and is returnable to customers through future customer service charges. Similarly, if actual revenue turns out to be less than actual expenses, the revenue shortfall is reflected as a debit to the rate stabilization account and is recoverable from customers through future customer service charges (see "RESULTS OF OPERATIONS – Movements in Rate Stabilization Account").

In addition, for certain transactions where the timing of the cash flows differs significantly from the accounting recognition, the Company recognizes regulatory deferral account debits and credits in order to adjust the accounting recognition to the period in which they will be considered for rate setting. These transactions are generally considered for rate setting when the amounts are expected to be realized in cash.

When determining the level of customer service charges, we consider the Company's current and future financial requirements (see "RESULTS OF OPERATIONS – Net Movement in Regulatory Deferral Accounts Related to Net Income (Loss)" and "RESULTS OF OPERATIONS – Amounts Considered for Rate Setting Purposes").

Our financial strategy is to fulfil our essential services mandate based on a sound financial foundation, reflected in part through high credit ratings in the financial markets. Maintaining this strong foundation requires a prudent approach that balances the interests of our key stakeholders while complying with our statutory and contractual obligations.

(in millions of dollars)

Financial Highlights

Results of operations for the three months ended May 31, 2017

The Company recorded a net loss of $8 in Q3 fiscal 2017 (Q3 fiscal 2016 - net loss of $8). Excluding rate stabilization and other regulatory deferral account adjustments, the Company recorded a net loss of $35 (Q3 fiscal 2016 - net loss of $16). Given the normal seasonality of air traffic and the fact that our costs are predominantly fixed in nature, a net loss is expected for this quarter.

The net loss was lower than planned as the Company has achieved positive financial performance compared to its approved budget, as reflected by the $8 of favourable variances from planned results shown below. This was due to regulatory deferrals of $17 and revenue $13 higher than planned, partially offset by operating expenses $21 higher than planned and other expenses $1 higher than planned.

	Three months ended May 31		
	2017	2016	Change
Revenue	$ 332	$ 337	$ (5)
Operating expenses	348	319	29
Other (income) and expenses	16	34	(18)
Income tax expense	3	-	3
Net income (loss), before rate stabilization and regulatory deferral account adjustments	(35)	(16)	(19)
Net movement in regulatory deferral accounts			
Rate stabilization adjustments:			
Favourable variances from planned results	(8)	(9)	1
Initial approved adjustment[(1)]	10	(7)	17
	2	(16)	18
Other regulatory deferral account adjustments:			
Employee benefit pension contributions	27	19	8
Other employee benefits	8	(1)	9
Investment in preferred interests, before tax	(8)	6	(14)
Investment in equity-accounted investee	(5)	-	(5)
Income tax	3	-	3
	25	24	1
	27	8	19
Net income (loss), after rate stabilization and regulatory deferral account adjustments	$ (8)	$ (8)	$ -

(1) In order to achieve breakeven results of operations, in the year ending August 31, 2017 (fiscal 2017), the Board approved a reduction of the rate stabilization account. As a result, $38 is being transferred out of the rate stabilization account evenly throughout the fiscal year. In fiscal 2016, the Board approved an increase of the rate stabilization account. Accordingly, $31 was transferred to the rate stabilization account evenly throughout the fiscal year. For the three months ended May 31, 2017, $10 has been transferred from the rate stabilization account (three months ended May 31, 2016 - $7 had been transferred to the rate stabilization account).

(in millions of dollars)

The Company is subject to legislation that regulates the level of its charges (see "INTRODUCTION – Financial Strategy and Rate Regulation"). The timing of the recognition of certain revenue and expenses recovered through charges is recorded through movements in regulatory deferral accounts. The net movement in regulatory deferral accounts for the three months ended May 31, 2017 was an income of $27 as compared to an income of $8 over the same period in fiscal 2016. This change in regulatory deferrals of $19 as compared to the same period in fiscal 2016 is due to lower deferrals of favourable results through rate stabilization adjustments of $18 and a $1 net increase in regulatory deferral adjustments to adjust the accounting recognition of certain transactions to the periods in which they will be considered for rate setting.

As shown below, cash and cash equivalents decreased by $58 during the three months ended May 31, 2017 and the Company experienced negative free cash flow of $34, which is a non-GAAP (Generally Accepted Accounting Principles) financial measure (see "LIQUIDITY AND CAPITAL RESOURCES – Cash flows for the three months ended May 31, 2017" for additional information on non-GAAP financial measures and a discussion of cash flows).

	Three months ended May 31		
	2017	2016	Change
Cash flows from:			
Operations[1]	$ (1)	$ 28	$ (29)
Investing[1]	(32)	(30)	(2)
Financing[1]	(25)	15	(40)
Increase (decrease) in cash and cash equivalents	(58)	13	(71)
Cash and cash equivalents, beginning of period	276	59	217
Cash and cash equivalents, end of period	$ 218	$ 72	$ 146
Free cash flow (non-GAAP financial measure):			
Cash flows from:			
Operations[2]	$ (1)	$ 28	$ (29)
Capital expenditures[2]	(37)	(30)	(7)
Proceeds from sale of investment in subsidiary[2]	4	-	4
Free cash flow	$ (34)	$ (2)	$ (32)

(1) See "LIQUIDITY AND CAPITAL RESOURCES – Cash flows for the three months ended May 31, 2017" for discussion of the changes in cash flows from the prior fiscal year.

(2) See the statement of cash flows in our Q3 fiscal 2017 financial statements.

(in millions of dollars)

Results of operations for the nine months ended May 31, 2017

The Company recorded a net loss of $42 for the nine months ended May 31, 2017 (nine months ended May 31, 2016 - net loss of $49). Excluding rate stabilization and other regulatory deferral account adjustments, the Company recorded a net loss of $99 (nine months ended May 31, 2016 - net loss of $24). This is primarily due to seasonally low air traffic volumes in Q3 compared to our predominantly fixed costs and the effect of the one-year temporary rate reduction averaging 3.9% in fiscal 2017.

The net loss was lower than planned as the Company has achieved positive financial performance in fiscal 2017 as compared to its approved budget, as reflected by the $37 of favourable variances from planned results shown below. This was primarily due to revenue $31 higher than planned and regulatory deferrals of $30, partially offset by operating expenses $18 higher than planned and other expenses $6 higher than planned.

	Nine months ended May 31		
	2017	2016	Change
Revenue	$ 960	$ 988	$ (28)
Operating expenses	997	922	75
Other (income) and expenses	53	89	(36)
Income tax expense	9	1	8
Net income (loss), before rate stabilization and regulatory deferral account adjustments	(99)	(24)	(75)
Net movement in regulatory deferral accounts			
Rate stabilization adjustments:			
Favourable variances from planned results	(37)	(33)	(4)
Initial approved adjustment[1]	29	(23)	52
	(8)	(56)	48
Other regulatory deferral account adjustments:			
Employee benefit pension contributions	89	40	49
Other employee benefits	5	(4)	9
Investment in preferred interests, before tax	(34)	(7)	(27)
Investment in equity-accounted investee	(5)	-	(5)
Income tax	9	1	8
Realized hedging transactions	1	1	-
	65	31	34
	57	(25)	82
Net income (loss), after rate stabilization and regulatory deferral account adjustments	$ (42)	$ (49)	$ 7

(1) The initial approved adjustment to reduce the rate stabilization account is being transferred evenly throughout the fiscal year. For the nine months ended May 31, 2017, $29 has been transferred from the rate stabilization account. In fiscal 2016, the Board approved an increase to the rate stabilization account. Accordingly, $23 had been transferred to the rate stabilization account for the nine months ended May 31, 2016.

(in millions of dollars)

The net movement in regulatory deferral accounts for the nine months ended May 31, 2017 was a loss of $57 as compared to an income of $25 over the same period in fiscal 2016. This change in regulatory deferrals of $82 is due to lower deferrals of favourable results through rate stabilization adjustments of $48 and a $34 net increase in regulatory deferral adjustments to adjust the accounting recognition of certain transactions to the periods in which they will be considered for rate setting.

As shown below, cash and cash equivalents increased by $99 during the nine months ended May 31, 2017 and the Company experienced negative free cash flow of $56, which is a non-GAAP financial measure (see "LIQUIDITY AND CAPITAL RESOURCES – Cash flows for the three months ended May 31, 2017" for additional information on non-GAAP financial measures and a discussion of cash flows).

	Nine months ended May 31		
	2017	2016	Change
Cash flows from:			
Operations[1]	$ 58	$ 124	$ (66)
Investing[1]	179	(65)	244
Financing[1]	(135)	(218)	83
Cash flows from operating, investing and financing activities	102	(159)	261
Effect of foreign exchange on cash and cash equivalents	(3)	1	(4)
Increase (decrease) in cash and cash equivalents	99	(158)	257
Cash and cash equivalents, beginning of period	119	230	(111)
Cash and cash equivalents, end of period	$ 218	$ 72	$ 146
Free cash flow (non-GAAP financial measure):			
Cash flows from:			
Operations[2]	$ 58	$ 124	$ (66)
Capital expenditures[2]	(97)	(93)	(4)
Investment in preferred interests[2]	(16)	-	(16)
Income tax payment on investment in preferred interests[2]	(5)	-	(5)
Proceeds from sale of investment in subsidiary[2]	4	-	4
Free cash flow	$ (56)	$ 31	$ (87)

(1) See "LIQUIDITY AND CAPITAL RESOURCES – Cash flows for the nine months ended May 31, 2017" for discussion of the changes in cash flows from the prior fiscal year.

(2) See the statement of cash flows in our Q3 fiscal 2017 financial statements.

(in millions of dollars)

Financial position as at May 31, 2017

The following table outlines significant changes in our assets and liabilities between August 31, 2016 and May 31, 2017:

	May 31 2017	August 31 2016	Change
Assets			
Current assets			
Cash and cash equivalents	$ 218	$ 119	$ 99
Accounts receivable and other	95	107	(12)
Investments	95	373	(278)
Other current assets	11	10	1
	419	609	(190)
Non-current assets			
Investment in preferred interests	342	291	51
Investment in equity-accounted investee	8	-	8
Property, plant and equipment	672	664	8
Intangible assets	933	953	(20)
Other non-current assets	5	-	5
	1,960	1,908	52
Total assets	2,379	2,517	(138)
Regulatory deferral account debit balances	1,433	1,708	(275)
Total assets and regulatory deferral account debit balances	$ 3,812	$ 4,225	$ (413)
Liabilities			
Current liabilities			
Trade and other payables	$ 201	$ 202	$ (1)
Current portion of long-term debt	375	25	350
Other current liabilities	5	6	(1)
	581	233	348
Non-current liabilities			
Long-term debt	1,220	1,694	(474)
Employee benefits	1,516	1,694	(178)
Deferred tax liability	53	45	8
Derivative liabilities	21	54	(33)
Other non-current liabilities	2	1	1
	2,812	3,488	(676)
Total liabilities	3,393	3,721	(328)
Equity			
Retained earnings (deficit)	(14)	28	(42)
Regulatory deferral account credit balances	433	476	(43)
Total liabilities, equity and regulatory deferral account credit balances	$ 3,812	$ 4,225	$ (413)

For a discussion of the changes in cash and cash equivalents from August 31, 2016, see "LIQUIDITY AND CAPITAL RESOURCES – Cash flows for the nine months ended May 31, 2017".

See "INTRODUCTION – Significant Financial Matters" for discussion of the significant changes in current and long-term investments, including the investment in preferred interests, the investment in equity-accounted investee, and long-term debt during the nine months ended May 31, 2017.

The change in non-current employee benefit liabilities are a result of the re-measurement gains of employee defined benefit plans recorded during the nine months ended May 31, 2017. The change in derivative liabilities is a result of positive fair value adjustments recorded on the Company's interest rate hedges. These changes along with the related changes in regulatory deferral account debit balances are discussed further in "RESULTS OF OPERATIONS – Other Comprehensive Income (Loss)".

The balance in retained earnings (deficit) as at May 31, 2017 reflects the earnings up to that date. We plan our operations to essentially result in an annual financial breakeven position after expenses are met through customer service charges and other revenue sources, and after adjustments are made to the rate stabilization account. As a result, the balance in the retained earnings (deficit) account at the end of each fiscal year has remained stable at $28. Any variation from this amount at the end of any interim period reflects seasonal or other planned fluctuations in revenue and expenses.

Significant Financial Matters

The following items have significant financial importance to the Company:

1. Rate Stabilization Account

As at May 31, 2017, the rate stabilization account (see "RESULTS OF OPERATIONS – Movements in Rate Stabilization Account") had a credit balance of $177, which is above its target of $101 for fiscal 2017 (see "RESULTS OF OPERATIONS – Amounts Considered for Rate Setting Purposes").

The rate stabilization account improved by $8 during fiscal 2017. This improvement was due to $37 of favourable variances from planned results, arising mainly from higher than planned revenue, partially offset by the $29 initially approved adjustment to the rate stabilization account. Rate stabilization adjustments are described under "RESULTS OF OPERATIONS – Movements in Rate Stabilization Account".

2. Air Traffic and Customer Service Charges[1]

During the first nine months of fiscal 2017, air traffic volumes increased by 5.1% year-over-year. Excluding the effect of the extra day for leap year in February 2016, year to date traffic was 5.5% higher than in the first nine months of fiscal 2016. The approved budget for the fiscal year had assumed growth of 1.1%. The Company's current forecast for air traffic growth for fiscal 2017 is 5.4%.

We continuously monitor our financial requirements and air traffic, and regularly update our financial forecasts to account for changes in the economic environment. On a quarterly basis, we review the most current information available from aviation industry sources as well as forecasts of macro-economic indicators; we then modify our forecasts accordingly and consider the need for a change in rates.

[1] Note: See "INTRODUCTION – Caution Concerning Forward-Looking Information", page 1

Based on the current strength of the rate stabilization account and our positive financial outlook for fiscal 2017 (see "RESULTS OF OPERATIONS – Financial Outlook") and for the fiscal year ending August 31, 2018 (fiscal 2018), the Company is proposing to decrease rates on average by 3.9% from existing base rates. If enacted, the lower rates would come into effect on September 1, 2017 just as the 3.9% temporary one-year rate reduction that is currently in place is set to expire, such that, on average, rates for fiscal 2017 and fiscal 2018 remain unchanged. The proposal includes base rate reductions on average of 3.5% intended to align revenues with costs and a temporary one-year 0.4% reduction to charges for all services. A one-time refund to customers of approximately $60, representing 4.6% of fiscal 2017 billings is also proposed. The refund is expected to be issued in fiscal 2018.

In accordance with the ANS Act, the Company issued a notice of revised service charges for consultation on May 30, 2017, providing details of the proposed revisions. The consultation period concludes on July 31, 2017.

3. Pension Plans

The Company funds its registered pension plans based on the January 1, 2016 actuarial valuations, as discussed in our fiscal 2016 annual MD&A. We use an annual measurement date of August 31 for determining the accounting surplus or deficit and establishing pension costs for the coming fiscal year. The Company's pension plans had an accounting deficit of $1,415 as at the annual measurement date of August 31, 2016 and an accounting deficit of $1,224 as at May 31, 2017. The $191 decrease in the deficit position during the nine months ended May 31, 2017 is primarily due to net actuarial gains of $257 and solvency deficiency contributions of $24, partially offset by actuarial accounting expense exceeding Company contributions by $89. The $257 of net actuarial gains are primarily due to a return on plan assets $239 greater than the expected return based on the discount rate at August 31, 2016 of 3.40%, and an $18 actuarial gain from a 10 basis point increase in the discount rate to 3.50% at May 31, 2017.

As at May 31, 2017, the Company has put in place letters of credit totalling $476 (representing 8% of registered pension plan assets as at May 31, 2017) to meet its cumulative pension solvency funding requirements. Commencing in April 2017, the Company began funding its remaining calendar 2017 solvency funding requirements of $45 with cash contributions. As at May 31, 2017, contributions of $24 have been made (see "RESULTS OF OPERATIONS – Net Movement in Regulatory Deferral Accounts Related to Net Income (Loss)").

Further information on the Company's pension plans is discussed under the heading "LIQUIDITY AND CAPITAL RESOURCES – Cash Requirements: Pension Plans".

4. Investment in Space-Based Aircraft Surveillance through Aireon:

As discussed in note 7 to the Q3 fiscal 2017 financial statements, as at May 31, 2017, the Company has invested $135 U.S. ($182 CDN) (August 31, 2016 - $120 U.S. ($157 CDN)). The Company is represented by four out of the eleven directors on Aireon's board of directors. The Company's investment in Aireon is in preferred interests, which are redeemable or convertible to common equity.

The Company completed its fourth tranche investment of $15 U.S. ($16 CDN) on December 21, 2016, increasing the fair value of its investment in preferred interests as well as its deferred tax liability. As at May 31, 2017, the Company's total fully diluted common equity interest on a post conversion basis is 38.1% (August 31, 2016 - 36.5%).

5. Collective Agreements

Approximately 87% of our workforce is unionized under eight collective agreements. During the quarter, the Company announced the ratification of a new collective agreement covering approximately 1,970 air traffic controllers, comprising approximately 45% of our represented workforce, following negotiations with the Canadian Air Traffic Control Association (CATCA) Unifor Local 5454. The two year agreement will run until March 31, 2019 and provides for wage increases, productivity enhancing changes and premium adjustments.

In addition, employees have the option to continue with the current severance provision or be paid out their accumulated severance with an additional incentive. Those who choose to have their severance paid out will no longer accrue severance. As a result, the Company recorded a curtailment loss on its defined severance benefits plan of $9 that is included in salaries and benefits expense. The cash settlement of $59 to curtail the severance benefits is expected to occur in fiscal 2018.

Subsequent to May 31, 2017, the Company has reached tentative agreements with two unions, comprising approximately 26% of our represented workforce. The agreements are now subject to each union's ratification process.

The Company is currently in negotiations with two unions, comprising approximately 7% of our represented workforce whose collective agreement expirations range from April 30, 2017 to June 30, 2017. The remaining three collective agreements (comprising 22% of our represented workforce) have contract expirations ranging from December 2017 to February 2018.

6. Investing and Financing Activities

During the nine months ended May 31, 2017, the Company received the remaining $285 principal balance of Master Asset Vehicle II (MAV II) Class A-1 and A-2 notes, the remaining $7 principal balance of the restructured asset-backed commercial paper (ABCP) and the remaining balance of its investment in other notes of $1 for total proceeds of $293.

On December 16, 2016, the Company redeemed $100 of the $350 Series MTN 2009-1 General Obligation Notes with proceeds from the MAV II notes and surplus cash.

7. Investment in Equity-Accounted Investee

Searidge Technologies Inc. (Searidge) is a privately-held corporation that provides software development and technology solutions in support of the air traffic control and airport operations market.

On April 28, 2017, the Company sold a portion of its investment in Searidge for proceeds of $4. As a result of the sale, the Company now owns 50% of the issued and outstanding shares of Searidge. The Company previously owned 70% as disclosed in note 3(a)(i) of the fiscal 2016 annual consolidated financial statements.

The Company has determined that its 50% interest in Searidge gives rise to joint control based on the contractual terms of the arrangement that require unanimous consent of all parties involved in key decisions over relevant activities. The Company has classified its investment as a joint venture as the Company has an interest in the net assets of Searidge based on the legal form and substance of the arrangement.

(in millions of dollars)

As a result of the sale, the Company has recorded a gain of $7 in the statement of operations (see "RESULTS OF OPERATIONS – Other (Income) and Expenses"). Of this gain, $2 is classified as realized representing the 20% sold, and $5 is classified as unrealized relating to the Company's remaining 50% interest. The $5 is being deferred for regulatory purposes until realized in cash (see RESULTS OF OPERATIONS – Net Movement in Regulatory Deferral Accounts Related to Net Income (Loss)).

RESULTS OF OPERATIONS

Revenue

The following table provides a breakdown of our revenue by category. Our fiscal 2016 AIF and the notes to our fiscal 2016 annual consolidated financial statements provide more information about the different categories of our customer service charges.

	Three months ended May 31			
	2017	2016	Change	%
Enroute	$ 165	$ 173	$ (8)	(5%)
Terminal	121	119	2	2%
Daily / annual / quarterly	21	21	-	- %
North Atlantic and international communication	12	13	(1)	(8%)
Total customer service charges	319	326	(7)	(2%)
Other	13	11	2	18%
	$ 332	$ 337	$ (5)	(1%)

Other revenue consists of service and development contracts, conference centre services at our facility in Cornwall (Ontario), the sale of civil aeronautical publications and other miscellaneous revenue.

Revenue for Q3 fiscal 2017 was $332 compared to $337 for Q3 fiscal 2016. The $5 decrease is primarily due to a $7 decrease in customer service charge revenue arising from lower revised service charges (7.6% on average) that became effective September 1, 2016, partially offset by a 5.9% growth in air traffic volumes during Q3 fiscal 2017.

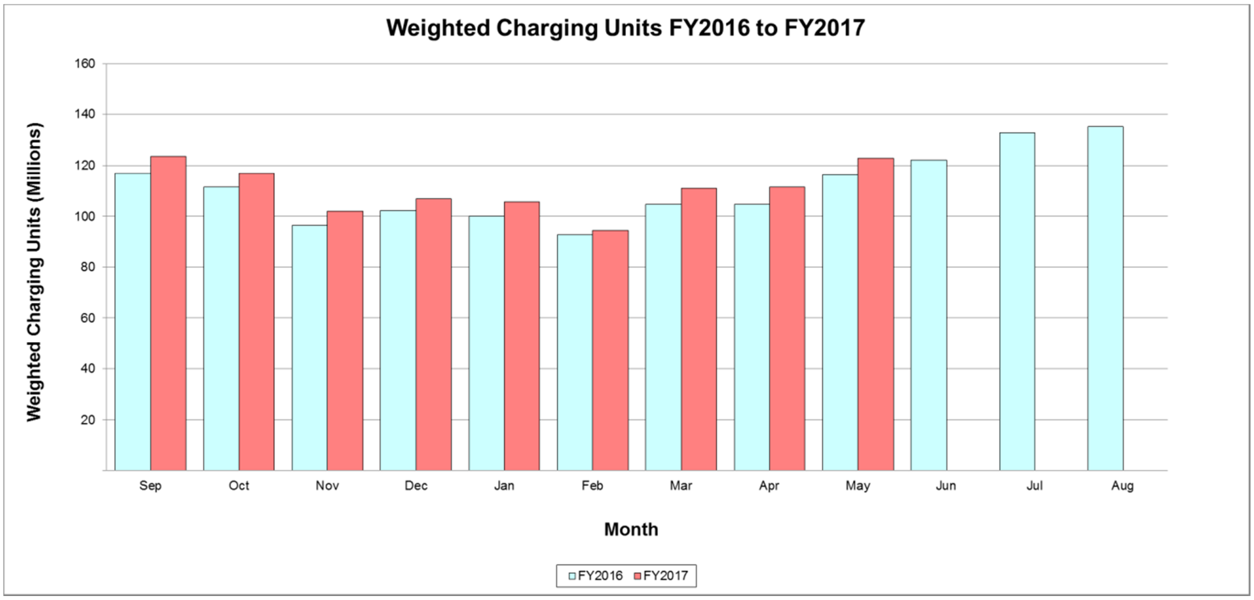
	Nine months ended May 31			
	2017	2016	Change	%
Enroute	$ 474	$ 499	$ (25)	(5%)
Terminal	351	350	1	- %
Daily / annual / quarterly	61	61	-	- %
North Atlantic and international communication	32	35	(3)	(9%)
Total customer service charges	918	945	(27)	(3%)
Other	42	43	(1)	(2%)
	$ 960	$ 988	$ (28)	(3%)

Revenue for the nine months ended May 31, 2017 was $960 compared to $988 for the nine months ended May 31, 2016. The $28 decrease is primarily due to a $27 decrease in customer service charge revenue arising from lower revised service charges (7.6% on average) that became effective September 1, 2016, partially offset by a 5.1% growth in air traffic volumes during fiscal 2017.

Air Traffic

Air traffic increased by 5.9% in Q3 fiscal 2017 when compared to Q3 fiscal 2016. In the first nine months of fiscal 2017, air traffic increased by 5.1% when compared to the first nine months of fiscal 2016 (5.5% higher when excluding the effect of the leap year in February 2016). This increase is illustrated in the following chart showing air traffic by month since September 2015.

The chart illustrates the seasonal variations in traffic. The chart shows traffic in "weighted charging units", which reflect the number of flights, aircraft size and distance flown.



Future air traffic volumes may be influenced by numerous factors, including the rate of economic growth or decline, changing air passenger demand, aircraft capacity utilization levels, fuel costs, changes in air carrier operations, air carrier competition, airline restructurings and insolvencies, terrorist activities, epidemics or pandemics, weather patterns, natural disasters, environmental concerns, demographic patterns and other factors.

Customer Service Charges[2]

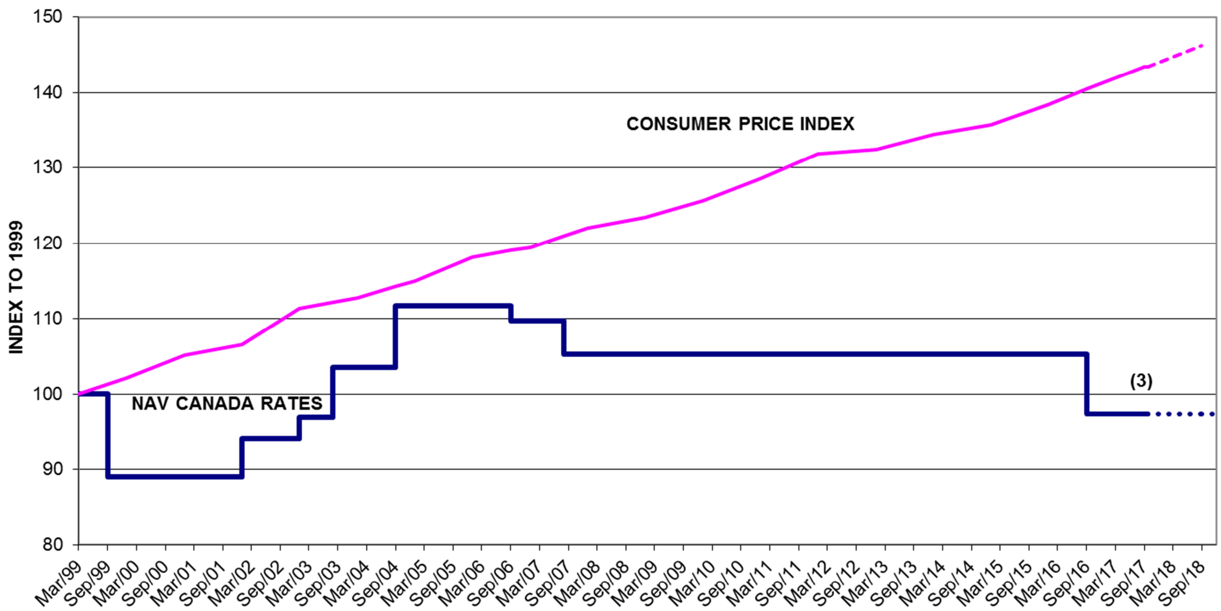
The levels of our customer service charges are a function of our costs, the required level of service, air traffic volumes and revenue from non-aeronautical sources (see "RESULTS OF OPERATIONS – Amounts Considered for Rate Setting Purposes").

Our business operates 24 hours a day, 365 days a year, providing an essential, national and international safety infrastructure. Given that the majority of our costs are predominantly fixed in nature and are directly related to service delivery, we have relatively few opportunities to significantly reduce these costs further without reducing service, which is not acceptable in most cases. We continue to focus on cost management, productivity improvements and opportunities for new revenue sources from licensing or sales of technology and other sources. This is assisting in keeping customer service charges as low as possible, while continuing to meet our safety and service obligations.

[2] Note: See "INTRODUCTION – Caution Concerning Forward-Looking Information", page 1

The following chart illustrates the evolution of our levels of customer service charges over time. The chart also depicts the revised customer service charges that became effective September 1, 2016. On average, customer service charges at August 31, 2016 were approximately 5% higher than they were when fully implemented in March 1999, which is approximately 35 percentage points less than the change in the Consumer Price Index since March 1999. Effective September 1, 2016, the revised customer service charges are on average 3% lower than when they were first implemented on a full cost recovery basis in March 1999.

HISTORY OF NAV CANADA RATE CHANGES(1)
VERSUS CONSUMER PRICE INDEX(2)



1. Average changes since charges were fully implemented on March 1, 1999
2. Consumer Price Index - Growth assumed to be 2.0 per cent for 2017 and beyond
3. NAV CANADA proposed a further refund of $60M in May 2017, equivalent to a reduction of 4.6% in rates. This is in addition to the 3.9% rate reductions proposed for September 1, 2017 which would come into effect just as the 3.9% temporary one-year rate reduction that is currently in place is set to expire.

As can be seen in the chart above, the Company has not had an overall rate increase since fiscal 2005, and has implemented four rate decreases since the rates were implemented in 1999. The chart also depicts the revised service charges that the Company has proposed effective September 1, 2017 (discussed below).

We continuously monitor our financial requirements and air traffic, and regularly update our financial forecasts to account for changes in the economic environment. On a quarterly basis, we consider the need for a change in rates.

Based on the current strength of the rate stabilization account and our positive financial outlook for fiscal 2017 (see "RESULTS OF OPERATIONS – Financial Outlook") and for fiscal 2018, the Company is proposing to decrease rates on average by 3.9% from existing base rates. If enacted, the lower rates would come into effect on September 1, 2017 just as the 3.9% temporary one-year rate reduction that is currently in place is set to expire, such that, on average, rates for fiscal 2017 and fiscal 2018 remain unchanged. The proposal includes base rate reductions on average of 3.5% intended to align revenues with costs and a temporary one-year 0.4% reduction to charges for all services. A one-time refund to customers of approximately $60, representing 4.6% of fiscal 2017 billings is also proposed. The refund is expected to be issued in fiscal 2018.

(in millions of dollars)

In accordance with the ANS Act, the Company issued a notice of revised service charges for consultation on May 30, 2017, providing details of the proposed revisions. The consultation period concludes on July 31, 2017.

Operating Expenses

	Three months ended May 31			
	2017	2016	Change	%
Salaries and benefits	$ 249	$ 220	$ 29	13%
Technical services	27	29	(2)	(7%)
Facilities and maintenance	17	17	-	- %
Depreciation and amortization	37	36	1	3%
Other	18	17	1	6%
	$ 348	$ 319	$ 29	9%

Salaries and benefits expense in Q3 fiscal 2017 increased by $29 compared to Q3 fiscal 2016 primarily due to the curtailment loss related to the voluntary elimination and settlement of severance benefits for employees represented by the CATCA collective agreement and increased pension current service costs, compensation levels and overtime costs.

	Nine months ended May 31			
	2017	2016	Change	%
Salaries and benefits	$ 696	$ 638	$ 58	9%
Technical services	83	87	(4)	(5%)
Facilities and maintenance	53	50	3	6%
Depreciation and amortization	110	106	4	4%
Other	55	41	14	34%
	$ 997	$ 922	$ 75	8%

Salaries and benefits expense for the nine months ended May 31, 2017 increased by $58 compared to the nine months ended May 31, 2016 due to increased pension current service costs, higher compensation levels and increased overtime as well as the curtailment loss incurred on the voluntary elimination and settlement of severance benefits for employees represented by the CATCA collective agreement. The Company uses a regulatory approach to determine the net impact charged to net income (loss) for its pension costs. The objective of this approach is to expense the cost of the Company's cash going concern and special payment contributions. Going concern pension contributions were lower for the nine months ended May 31, 2017 and this reduction in expense was recorded as a net increase in regulatory deferral adjustments (see "LIQUIDITY AND CAPITAL RESOURCES – Cash Requirements: Pension Plans").

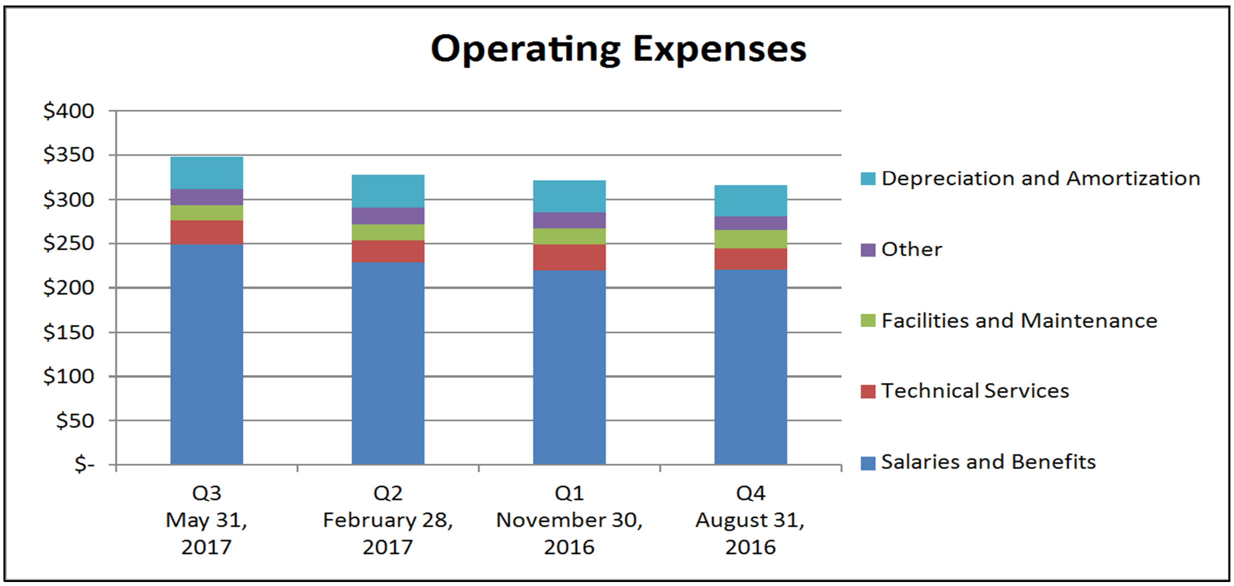
Technical services expenses decreased by $4 in fiscal 2017, mainly due to lower telecommunications and aeronautical information management costs.

Facilities and maintenance expenses increased by $3 in fiscal 2017 as a result of general increases in the underlying costs as compared to fiscal 2016.

Depreciation and amortization increased by $4 in fiscal 2017 as a result of an increased cost base of property, plant and equipment and intangible assets compared to fiscal 2016.

Other operating expenses for the nine months ended May 31, 2017 increased by $14 compared to the nine months ended May 31, 2016. The increase is primarily due to the Company receiving a refund of commodity taxes previously paid in fiscal 2016. In fiscal 2017, there is no refund offsetting expenses. Travel and relocation costs as well as professional fees also increased in fiscal 2017 compared to fiscal 2016.

As illustrated in the table below, the majority of our operating expenses are incurred evenly throughout the year.



The increase in salaries and benefits expense in Q3 fiscal 2017 compared to Q2 fiscal 2017 is primarily due to a $9 curtailment loss incurred as a result of the voluntary elimination and settlement of severance benefits for employees represented by the CATCA collective agreement.

(in millions of dollars)

Other (Income) and Expenses

	Three months ended May 31		
	2017	2016	Change
Finance income			
Interest income	$ (1)	$ (1)	$ -
Net change in fair value of financial assets at FVTPL[1]			
MAV II, ABCP and other investments	(1)	(2)	(1)
Investment in preferred interests	(2)	(2)	-
	(3)	(4)	(1)
Total finance income	(4)	(5)	(1)
Net interest costs relating to employee benefits	14	10	(4)
Other finance costs			
Interest expense	19	22	3
Other (gains) and losses			
Foreign exchange (gains) and losses	(6)	7	13
Realized gain on sale of investment in subsidiary	(2)	-	2
Unrealized gain on sale of investment in subsidiary	(5)	-	5
	(13)	7	20
	$ 16	$ 34	$ 18

(1) The net change in fair value of financial assets at fair value through profit or loss (FVTPL) includes interest and dividend income related to those financial assets.

The $4 increase in net interest costs relating to employee benefits in Q3 fiscal 2017 is primarily due to higher pension interest income than in Q3 fiscal 2016, partially offset by higher pension finance costs.

The $3 decrease in other finance costs in Q3 fiscal 2017 is primarily due to lower interest costs on long-term debt due to lower debt levels in Q3 fiscal 2017 compared to Q3 fiscal 2016.

Other gains of $13 were recorded in Q3 fiscal 2017 compared to a loss of $7 in Q3 fiscal 2016. The change is mainly due to recording realized gains of $2 and unrealized gains of $5 on the sale of a portion of the Company's investment in Searidge. As well, unrealized foreign exchange gains of $6, mainly related to the investment in Aireon, were recorded in Q3 fiscal 2017 due to the fluctuation of the Canadian dollar against the U.S. dollar, compared to unrealized foreign exchange losses of $7 in Q3 fiscal 2016.

(in millions of dollars)

	Nine months ended May 31		
	2017	2016	Change
Finance income			
Interest income	$ (2)	$ (2)	$ -
Net change in fair value of financial assets at FVTPL(1)			
MAV II, ABCP and other investments	(15)	(5)	10
Investment in preferred interests	(22)	(8)	14
	(37)	(13)	24
Total finance income	(39)	(15)	24
Net interest costs relating to employee benefits	41	31	(10)
Other finance costs			
Interest expense	60	72	12
Redemption premium	10	-	(10)
	70	72	2
Other (gains) and losses			
Foreign exchange (gains) and losses)	(12)	1	13
Realized gain on sale of investment in subsidiary	(2)	-	2
Unrealized gain on sale of investment in subsidiary	(5)	-	5
	(19)	1	20
	$ 53	$ 89	$ 36

(1) The net change in fair value of financial assets at FVTPL includes interest and dividend income related to those financial assets.

The net change in fair value of financial assets at FVTPL increased by $24 compared to fiscal 2016, as a result of recording positive fair value adjustments on MAV II, ABCP and other investments of $14 and interest income of $1 in fiscal 2017 compared to positive fair value adjustments of $4 and interest income of $1 in fiscal 2016. Positive fair value adjustments on the investment in preferred interests of $14, along with dividend income of $8 were recorded in fiscal 2017 compared to dividend income of $8 in fiscal 2016.

The $10 increase in net interest costs relating to employee benefits in fiscal 2017 is primarily due to higher pension interest income than in fiscal 2016, partially offset by higher pension finance costs.

The $2 decrease in other finance costs in fiscal 2017 is a result of $12 lower interest costs on long-term debt due to lower debt levels in fiscal 2017 compared to fiscal 2016, partially offset by the redemption premium of $10 related to the early redemption of $100 of the $350 Series MTN 2009-1 General Obligation Notes.

Other gains of $19 were recorced in fiscal 2017 compared to a loss of $1 in fiscal 2016. The change is mainly due to recording unrealized foreign exchange gains of $12 on the investment in Aireon in fiscal 2017 due to the fluctuation of the Canadian dollar against the U.S. dollar, compared to unrealized foreign exchange losses of $1 in fiscal 2016. As well, realized gains of $2 and unrealized gains of $5 on the sale of a portion of the Company's investment in Searidge were recorded in fiscal 2017.

(in millions of dollars)

Net Movement in Regulatory Deferral Accounts Related to Net Income (Loss)

The net movement in regulatory deferral accounts related to net income (loss) represents the regulatory accounting adjustments, including the rate stabilization mechanism, to adjust the accounting recognition of certain transactions to the periods in which they will be considered for rate setting. The Company's regulatory approach has not changed from that disclosed in the fiscal 2016 annual MD&A.

	Three months ended May 31		
	2017	2016	Change
Rate stabilization account	$ 2	$ (16)	$ 18
Other regulatory deferral accounts			
Employee benefit pension contributions	27	19	8
Other employee benefits	8	(1)	9
Investment in preferred interests, before tax	(8)	6	(14)
Investment in equity-accounted investee	(5)	-	(5)
Income tax	3	-	3
	$ 27	$ 8	$ 19

The movements in the rate stabilization account in Q3 fiscal 2017 of $2 are a result of favourable variances from planned results of $8 (Q3 fiscal 2016 - $9) more than offset by the initial approved transfer out of the rate stabilization account of $10 (Q3 fiscal 2016 - $7 transfer to the rate stabilization account).

The net movement in the employee benefit pension contributions regulatory deferral account for Q3 fiscal 2017 increased by $8 compared to Q3 fiscal 2016. Regulatory adjustments to adjust the total pension benefit expense to the level of pension contributions to be recovered through rate setting were $27 in Q3 fiscal 2017 compared to $19 in Q3 fiscal 2016. Included in the Q3 fiscal 2017 regulatory deferral related to pension contributions of $27 is $24 of solvency contributions which are expected to be recovered by the fiscal year ending August 31, 2020 (fiscal 2020).

The net movement in other employee benefits regulatory deferral accounts increased by $9 in Q3 fiscal 2017 compared to Q3 fiscal 2016. The increase is mainly a result of the curtailment loss of $9 incurred as a result of the voluntary elimination and settlement of severance benefits for employees represented by the CATCA collective agreement.

The $14 increase in the investment in preferred interests regulatory deferral account in Q3 fiscal 2017 was primarily due to the change in unrealized foreign exchange gains (losses) from a loss of $6 in Q3 fiscal 2016 to unrealized foreign exchange gains of $8 in Q3 fiscal 2017 due to the fluctuation of the Canadian dollar against the U.S. dollar.

The net movement in the investment in equity-accounted investee regulatory deferral account relates to the deferral of the unrealized gain of $5 on the Company's remaining 50% interest in Searidge. The impacts to net income (loss) related to the Company's investment in Searidge are deferred until realized in cash net of tax.

The net movement in the income tax regulatory deferral accounts includes the deferral of the deferred income tax liabilities related to the Company's investment in preferred interests of Aireon as well as its remaining 50% interest in Searidge. The increase in Q3 fiscal 2017 of $3 compared to Q3 fiscal 2016 includes an increase of $2 to the deferred income tax liability related to the investment in preferred interests of Aireon and $1 related to the investment in Searidge.

(in millions of dollars)

	Nine months ended May 31		
	2017	2016	Change
Rate stabilization account	$ (8)	$ (56)	$ 48
Other regulatory deferral accounts			
Employee benefit pension contributions	89	40	49
Other employee benefits	5	(4)	9
Investment in preferred interests, before tax	(34)	(7)	(27)
Investment in equity-accounted investee	(5)	-	(5)
Income tax	9	1	8
Realized hedging transactions	1	1	-
	$ 57	$ (25)	$ 82

The movements in the rate stabilization account are detailed in the table below under "RESULTS OF OPERATIONS – Movements in Rate Stabilization Account".

The net movement in the employee benefit pension contributions regulatory deferral account for the nine months ended May 31, 2017 increased by $49 compared to the same period in fiscal 2016. Regulatory adjustments to adjust the total pension benefit expense to the level of pension contributions to be recovered through rate setting were $89 in fiscal 2017 compared to $40 in fiscal 2016. Included in the fiscal 2017 regulatory deferral related to pension contributions of $89 is $24 of solvency contributions which are expected to be recovered by fiscal 2020.

The net movement in other employee benefits regulatory deferral accounts increased by $9 in fiscal 2017 compared fiscal 2016. The increase is primarily due to the curtailment loss of $9 incurred as a result of the voluntary elimination and settlement of severance benefits for employees represented by the CATCA collective agreement.

The $27 increase in the investment in preferred interests regulatory deferral account for the nine months ended May 31, 2017 was primarily due to the regulatory deferral of the $14 increase in fair value of the investment along with the change in unrealized foreign exchange gains of $12 compared to a loss of $1 in fiscal 2016 due to the fluctuation of the Canadian dollar against the U.S. dollar.

The net movement in the investment in equity-accounted investee regulatory deferral account relates to the deferral of the unrealized gain of $5 on the Company's remaining 50% interest in Searidge. The impacts to net income (loss) related to the Company's investment in Searidge are deferred until realized in cash net of tax.

The net movement in the income tax regulatory deferral accounts includes the deferral of the deferred income tax liabilities related to the Company's investment in preferred interests of Aireon as well as its remaining 50% interest in Searidge. The increase in fiscal 2017 of $8 compared to fiscal 2016 includes an increase of $7 to the deferred income tax liability related to the investment in preferred interests of Aireon and $1 related to the investment in Searidge.

(in millions of dollars)

Movements in Rate Stabilization Account

Our rate stabilization mechanism and accounting are described at the beginning of this MD&A and in notes 1 and 9 of our fiscal 2016 annual consolidated financial statements. The table below shows the movements in the rate stabilization account.

	Nine months ended May 31		
	2017	2016	Change
Credit balance on the statement of financial position, beginning of period	$ 169	$ 81	$ 88
Variances from planned results:			
Revenue higher than planned	31	16	15
Operating expenses (higher) lower than planned	(18)	27	(45)
Other (income) and expenses higher than planned	(6)	(2)	(4)
Net movement in other regulatory deferral accounts	30	(8)	38
Total variances from planned results	37	33	4
Initial approved adjustment	(29)	23	(52)
Net movement in rate stabilization account recorded in net income (loss)	8	56	(48)
Credit balance on the statement of financial position, end of period	$ 177	$ 137	$ 40

The $8 improvement in the rate stabilization account during the nine months ended May 31, 2017 is primarily due to:

- net movement of $30 in regulatory deferral accounts that was more favourable than planned primarily due to:
  - a regulatory deferral credit for pensions that was $20 higher than planned primarily due to a 50 basis point decrease in the discount rate from when the fiscal 2017 budget was approved; and
  - a regulatory deferral credit for retiring allowances of $9 that was not budgeted for due to the deferral of the curtailment loss related to the voluntary elimination and settlement of severance benefits for employees represented by the CATCA collective agreement;

  partially offset by:

  - a regulatory deferral debit of $5 to defer the impacts to net (income) loss related to the Company's investment in Searidge that was not budgeted for; and
- revenue that was $31 higher than planned mainly due to an increase in customer service charge revenue arising from higher air traffic;

(in millions of dollars)

partially offset by:

- operating expenses that were $18 higher than planned, mainly due to higher salaries and benefits expense of $9 for the curtailment loss related to the voluntary elimination and settlement of severance benefits for employees represented by the CATCA collective agreement and higher depreciation and amortization, partially offset by lower technical services, facilities and maintenance and other operating costs;

- other (income) and expense that was $6 higher than planned as a result of the redemption premium of $10, positive fair value adjustments $9 lower than planned and income taxes $7 higher than planned, partially offset by foreign exchange gains of $12 and gains of $7 on the sale of a portion of the Company's investment in Searidge;

- the planned adjustment of $29, representing three quarters of the anticipated net loss at the time the fiscal 2017 budget was approved.

Other Comprehensive Income (Loss)

The accounting recognition of other comprehensive income (loss) amounts are offset by regulatory deferrals in order to defer the accounting recognition to the periods in which they will be considered for rate setting. These transactions are generally considered for rate setting when the amounts are expected to be realized in cash, with the exception of the cash flows related to hedging instruments, which are considered for rate setting in the same period as the underlying hedged transaction, and re-measurements of unfunded defined employee benefit plans, which are considered for rate setting over the employees' average expected remaining service period.

	Three months ended May 31		
	2017	2016	Change
Items that will not be reclassified to income or (loss):			
Re-measurements of employee defined benefit plans	$ (219)	$ (155)	$ (64)
Net movement in regulatory deferral accounts	219	155	64
	-	-	-
Items that will be reclassified to income or (loss):			
Changes in fair value of cash flow hedges	(6)	6	(12)
Net movement in regulatory deferral accounts	6	(6)	12
	-	-	-
Total other comprehensive income (loss)	$ -	$ -	$ -

Re-measurement losses of employee defined benefit plans in Q3 fiscal 2017 of $219 are a result of actuarial losses of $550, primarily due to a 40 basis point decrease in the discount rates to 3.50%, partially offset by a return on plan assets $307 greater than the expected return based on the discount rate of 3.40% at August 31, 2016 and actuarial gains of $24 due to positive experience on the defined benefit obligation. In Q3 fiscal 2016, the re-measurement losses of $155 were mainly due to actuarial losses of $348 due to a 30 basis point decrease in the discount rate and $7 due to negative demographic changes, partially offset by a return on plan assets $176 greater than the expected return based on the discount rate, and $24 of actuarial gains due to positive experience on the defined benefit obligations.

(in millions of dollars)

During Q3 fiscal 2017, negative fair value adjustments of $6 were recorded on the Company's interest rate hedges related to the re-financing of debt instruments that will mature in the fiscal year ending August 31, 2019 (fiscal 2019). In Q3 fiscal 2016, positive fair value adjustments of $6 were recorded on the same interest rate hedges.

	Nine months ended May 31		
	2017	2016	Change
Items that will not be reclassified to income or (loss):			
Re-measurements of employee defined benefit plans	$ 257	$ (177)	$ 434
Net movement in regulatory deferral accounts	(257)	177	(434)
	-	-	-
Items that will be reclassified to income or (loss):			
Amortization of loss on cash flow hedge to net income (loss)	1	-	1
Changes in fair value of cash flow hedges	30	(68)	98
Net movement in regulatory deferral accounts	(31)	68	(99)
	-	-	-
Total other comprehensive income (loss)	$ -	$ -	$ -

Re-measurement gains of employee defined benefit plans in the nine months ended May 31, 2017 are primarily due to net actuarial gains of $257, primarily due to a return on plan assets $239 greater than the expected return based on the discount rate at August 31, 2016 of 3.40%, and actuarial gains of $18 due a 10 basis point increase in the discount rates to 3.50%. For fiscal 2016, the net re-measurement losses of $177 were mainly a result of actuarial losses of $357 due to a 30 basis point decrease in the discount rate, partially offset by a return on plan assets $93 greater than the expected return based on the discount rate, actuarial gains of $63 from demographic changes and $24 due to positive experience on the defined benefit obligations.

In fiscal 2017, positive fair value adjustments of $30 were recorded on the Company's interest rate hedges related to the re-financing of debt instruments that will mature in fiscal 2019. In fiscal 2016, negative fair value adjustments of $17 were recorded on the same interest rate hedges. In addition, during Q2 fiscal 2016, the Company cash-settled interest rate hedges related to the re-financing of debt instruments that matured in February 2016. A loss of $51 on the forward dated interest rate swap agreements was recognized in other comprehensive income (loss) and is being reclassified to net income (loss) using the effective interest rate method over the 30-year term of the hedged Series MTN 2016-1 General Obligation Notes.

(in millions of dollars)

Amounts Considered for Rate Setting Purposes

As discussed under "INTRODUCTION – Financial Strategy and Rate Regulation", when establishing customer service charges the Board considers the Company's current and future financial requirements as well as:

(a) the current and anticipated balance in the rate stabilization account as compared to its target balance; and

(b) the recovery of pension contributions on a cash basis.

The table below shows the balance of the rate stabilization account as compared to its target balance and the amount of regulatory pension expense cumulatively lower than contributions.

		May 31 2017	August 31 2016	Change
(a) Rate stabilization account credit balance		$ 177	$ 169	$ 8
Fair value variances on ABCP investments		-	11	(11)
Face value variance on MAV II Class A-2 notes when purchased in fiscal 2011		-	3	(3)
Credit loss provisions on ABCP investments		-	-	-
Net non-credit related fair value variances from face value		-	14	(14)
"Notional" balance of the rate stabilization account[1]		177	183	(6)
Target balance of the rate stabilization account[2]		(101)	(100)	(1)
Excess of the rate stabilization account from its target balance	(A)	$ 76	$ 83	$ (7)
(b) Pension contributions in excess of pension expense		(71)	(136)	65
Regulatory credit balance - recovery of contributions		47	136	(89)
Regulatory expense cumulatively lower than contributions	(B)	$ (24)	$ -	$ (24)
Amount to be returned over time through rate setting	(A + B)	$ 52	$ 83	$ (31)

As at August 31, 2016, the amount to be returned over time through rate setting was $83. There has been a decrease in the amount to be returned over time through rate setting by $31 to $52 during the nine months ended May 31, 2017.

(1) Due to the receipt of the remaining proceeds from the maturity of ABCP investments in Q2 fiscal 2017, there is no further requirement to "notionally" adjust the balance of the rate stabilization account.

(in millions of dollars)

(2) The long-term target credit balance of the rate stabilization account is 7.5% of total planned annual expenses net of other (income) and expenses, excluding non-recurring items, on an ongoing basis. For fiscal 2017, the target balance is $101.

Financial Outlook[3]

Presented below are the Company's current projected annual consolidated results before rate stabilization for fiscal 2017 compared to fiscal 2016 results.

	Fiscal 2017	Fiscal 2016	Change	%
Before rate stabilization				
Revenue	$ 1,292	$ 1,393	$ (101)	(7%)
Operating expenses and other (income) and expenses, including other regulatory adjustments	1,332	1,305	27	2%
Net income (loss) before rate stabilization adjustments	$ (40)	$ 88	$ (128)	

Revenue

Total revenue for fiscal 2017 is expected to decrease by approximately 7.2% or $101 from $1,393 in fiscal 2016 due to the lower revised service charges (7.6% on average) that became effective September 1, 2016, as well as the forecasted recognition of the proposed $60 refund to customers, representing 4.6% of fiscal 2017 billings, partially offset by forecasted air traffic growth of 5.4%.

In our Q2 fiscal 2017 MD&A, we had disclosed anticipated revenue of $1,357 for fiscal 2017. The $65 decrease in forecasted revenue is primarily due to the accrual of the proposed $60 refund to customers representing 4.6% of fiscal 2017 billings expected to be paid in fiscal 2018 and a slight decrease in air traffic, which grew by 5.1% in the first nine months of fiscal 2017 compared to the forecast of 5.2%.

Operating Expenses and Other (Income) and Expenses

Operating expenses and other (income) and expenses before rate stabilization for fiscal 2017 are expected to be $1,332. This is an increase of 2.1% or $27 compared to fiscal 2016 due to:

- higher compensation levels, including increased overtime;
- increased operational requirements in the areas of technical services and facilities and systems maintenance;
- increased other operating expenses, as refunds of $7 relating to commodity taxes paid in prior years were received in fiscal 2016 with no equivalent amount forecasted for fiscal 2017; and
- the effects of inflation;

[3] Note: See "INTRODUCTION – Caution Concerning Forward-Looking Information", page 1

partially offset by:

- lower expected regulatory pension expense, due to lower expected going concern pension contributions on which the regulatory pension expense is based (presented on the statement of comprehensive income as higher pension current service costs and net interest costs that are more than offset by the higher regulatory deferral); and
- higher positive fair value adjustments on investments.

Across the Company, we remain focused on cost saving measures that are consistent with safety, which is our top priority. Our efforts are aimed at managing staffing levels and discretionary expenses, as well as continuing to implement process improvement initiatives and efficiencies.

In our Q2 fiscal 2017 MD&A, we had disclosed anticipated operating expenses and other (income) and expenses, before rate stabilization of $1,331 for fiscal 2017. While this is comparable to the current forecast, the forecast at Q3 fiscal 2017 includes an increase in salaries and benefits expense of $9 due to the voluntary elimination and settlement of severance benefits for employees represented by the CATCA collective agreement and an increase in foreign exchange gains of $14 compared to the Q2 fiscal 2017 forecast. Both of these increases are offset by regulatory accounting.

Cash Flows

Given the expected net cash flows from operations and cash flows from investing and financing activities in fiscal 2017, the Company's cash position is currently expected to increase to $207 as at August 31, 2017 from $119 as at August 31, 2016. This cash outlook is based on anticipated annual cash inflows from operating and investing activities of $139 and $88 respectively, offset by cash outflows from financing activities of $135 for the repayment of long-term debt. Investing activities in fiscal 2017 include cash inflows of $293 from proceeds from the maturity of ABCP investments and proceeds of $4 from the sale of a portion of the Company's investment in Searidge, partially offset by forecasted cash outflows for projected capital expenditures of $167, investments in preferred interests of Aireon of $36 and an income tax payment of $5. As discussed below, the Company has adequate existing sources of financing to cover all of its anticipated cash flow requirements.

In our Q2 fiscal 2017 MD&A, we had disclosed an anticipated cash position of $203 by the end of fiscal 2017. The $4 increase in our cash position at the end of fiscal 2017 is due to the proceeds of $4 received on the sale of a portion of the Company's investment in Searidge. The Q3 fiscal 2017 forecast includes the accrual of the proposed $60 refund to customers; this refund is not expected to be issued until fiscal 2018.

Rate Stabilization Account

As noted previously, in May 2017 the Company proposed to implement revisions to its customer service charges that if approved will be effective September 1, 2017. A one-time refund to customers of approximately $60, representing 4.6% of fiscal 2017 billings is also proposed (see "RESULTS OF OPERATIONS – Revenue: Customer Service Charges").

The Company currently anticipates that the rate stabilization account will have a credit balance of $129 at the end of fiscal 2017, resulting from estimated revenue of $1,292, after considering the proposed $60 refund to customers, and total operating expenses and other (income) and expense (including other regulatory adjustments) of $1,332 (before rate stabilization). The target balance of the rate stabilization account in fiscal 2017 is $101.

In our Q2 fiscal 2017 MD&A, we had forecast an anticipated rate stabilization account credit balance of $195 at the end of fiscal 2017. The decrease in the rate stabilization account outlook to $129 at the end of fiscal 2017 is primarily due to the forecasted recognition of the proposed $60 refund to customers that is expected to be issued in fiscal 2018.

Earnings and Cash Flow Coverage

During a fiscal year, quarterly revenue will reflect seasonal or other fluctuations in the airline industry and therefore our net results vary from quarter to quarter. Our mandate to operate on essentially a financial breakeven basis results in a planned earnings coverage ratio – calculated on the basis of earnings before interest divided by interest expense – that is close to one-to-one. However, the seasonal nature of our revenue may result in an earnings coverage ratio of less than one-to-one for any interim period.

For the twelve months ended May 31, 2017, the Company achieved net income of $7. Our interest cost was $91. Consolidated earnings (after rate stabilization) before interest were $98, which is 1.08 times our interest requirement for the fiscal year and just above our one-to-one target. Depreciation and amortization expense for this period was $145. Our cash flow coverage was 2.67 times our interest requirement for this period.

Earnings coverage ratio and cash flow coverage are non-GAAP financial measures and do not have any standardized meaning prescribed by IFRS. The earnings coverage ratio and cash flow coverage are provided pursuant to and in compliance with National Instrument 44-102 *Shelf Distributions* of the Canadian Securities Administrators. The Company calculates the earnings coverage ratio on the basis of earnings before interest expense on financial liabilities at amortized cost (interest expense) divided by interest expense. Cash flow coverage is calculated on the basis of earnings (after rate stabilization) before interest expense, depreciation and amortization divided by interest expense. Under the *Income Tax Act* (Canada), NAV CANADA, excluding its subsidiaries, is not subject to income taxes and accordingly, no deduction for income taxes has been made. After the application of rate regulated accounting, the provision for income taxes related to our taxable subsidiaries is insignificant.

We maintain a debt service reserve fund and an operations and maintenance reserve fund under our Master Trust Indenture and we are subject to liquidity covenants under our General Obligation Indenture, designed to cover 12 months interest on borrowings and 25% of our annual operating and maintenance expenses. As at May 31, 2017, we were in full compliance with our debt indentures, including the Master Trust Indenture's requirements regarding the reserve funds, the flow of funds and with the rate covenants, as well as the liquidity and other provisions of the General Obligation Indenture.

Related Party Transactions

The Company's related parties include its key management personnel, subsidiaries, joint ventures and registered pension plans for its employees. The transactions with these related parties are not materially different from what was reported in the fiscal 2016 annual MD&A with the exception of the Company's accounting for its investment in Searidge (see section "INTRODUCTION – Significant Financial Matters: Investment in Equity-Accounted Investee"). There were no significant related party transactions with Searidge from the time of sale through May 31, 2017.

(in millions of dollars)

SUMMARY OF QUARTERLY RESULTS

Quarterly Financial Information (unaudited)

	Three months ended			
	Q3 May 31 2017	Q2 February 28 2017	Q1 November 30 2016	Q4 August 31 2016
Revenue	$ 332	$ 296	$ 332	$ 405
Operating expenses	348	328	321	316
Other (income) and expenses	16	15	22	27
	(32)	(47)	(11)	62
Income tax expense	3	5	1	1
Net income (loss) before net movement in regulatory deferral accounts	(35)	(52)	(12)	61
Net movement in regulatory deferral accounts related to net income (loss), net of tax				
Rate stabilization adjustments	2	(3)	(7)	(32)
Other regulatory deferral account adjustments	25	21	19	20
	27	18	12	(12)
Net income (loss) after net movement in regulatory deferral accounts	$ (8)	$ (34)	$ -	$ 49

	Three months ended			
	Q3 May 31 2016	Q2 February 29 2016	Q1 November 30 2015	Q4 August 31 2015
Revenue	$ 337	$ 309	$ 342	$ 384
Operating expenses	319	307	$ 296	$ 305
Other (income) and expenses	34	25	$ 30	$ 24
	(16)	(23)	16	55
Income tax expense	-	1	$ -	$ 1
Net income (loss) before net movement in regulatory deferral accounts	(16)	(24)	16	54
Net movement in regulatory deferral accounts related to net income (loss), net of tax				
Rate stabilization adjustments	(16)	(19)	$ (21)	$ 2
Other regulatory deferral account adjustments	24	4	$ 3	$ (14)
	8	(15)	(18)	(12)
Net income (loss) after net movement in regulatory deferral accounts	$ (8)	$ (39)	$ (2)	$ 42

Discussion of Quarterly Results

The quarterly variations in revenue mainly reflect seasonal fluctuations. Typically, revenue is highest in our fourth quarter (June to August) as a result of increased air traffic in the summer months. The second quarter (December to February) typically has the lowest air traffic volumes. Air traffic for Q3 fiscal 2017 was 5.9% higher on average than in Q3 fiscal 2016. Effective September 1, 2016, the Company implemented revisions to its service charges resulting in reductions on average of 7.6%.

The majority of our operating expenses are incurred evenly throughout the year. The increase in operating expenses in Q3 fiscal 2017 is primarily due to the curtailment loss recorded to salaries and benefits incurred as a result of the voluntary elimination and settlement of severance benefits for employees represented by the CATCA collective agreement.

Other (income) and expenses fluctuate primarily due to:

- fair value adjustments on investments which change based on market factors and changes in expectations of credit losses;
- changes in net interest costs relating to employee benefits as a result of changes in discount rates; and
- changes in foreign exchange (gains) or losses as a result of the strengthening or weakening of the Canadian dollar compared to foreign currencies in which the Company transacts, mainly the U.S. dollar.

Net movement in regulatory deferral accounts related to net income (loss) fluctuates due to:

- changes in the rate stabilization account based on variances from planned results and the initial approved adjustment;
- changes in employee benefit pension contributions and expense;
- changes in other employee benefits, including long-term disability (LTD) funding requirements;
- changes in the investment in preferred interests of Aireon, before tax;
- changes in the investment in equity-accounted investee;
- changes in income taxes; and
- changes in realized hedging transactions.

LIQUIDITY AND CAPITAL RESOURCES

Our fiscal 2016 annual MD&A explains how we manage our cash and capital resources. There have been no changes in that approach for the nine months ended May 31, 2017. The following sections discuss changes in our cash and capital resources since August 31, 2016.

As at May 31, 2017, we had $218 of cash and cash equivalents and committed credit facilities of $1,190, of which $430 was available for unrestricted use (see "LIQUIDITY AND CAPITAL RESOURCES – Liquidity and Financing Strategy").

(in millions of dollars)

Cash flows for the three months ended May 31, 2017

	Three months ended May 31		
	2017	2016	Change
Cash flows from:			
Operations	$ (1)	$ 28	$ (29)
Investing	(32)	(30)	(2)
Financing	(25)	15	(40)
Increase (decrease) in cash and cash equivalents	(58)	13	(71)
Cash and cash equivalents, beginning of period	276	59	217
Cash and cash equivalents, end of period	$ 218	$ 72	$ 146
Free cash flow (non-GAAP financial measure):			
Cash flows from:			
Operations	$ (1)	$ 28	$ (29)
Capital expenditures[(1)]	(37)	(30)	(7)
Proceeds from sale of investment in subsidiary[(1)]	4	-	4
Free cash flow	$ (34)	$ (2)	$ (32)

[(1)] See the statement of cash flows in our Q3 fiscal 2017 financial statements.

As shown above, cash and cash equivalents decreased by $58 for the three months ended May 31, 2017 and the Company experienced negative free cash flow of $34, which is a non-GAAP financial measure. Non-GAAP financial measures do not have any standardized meaning prescribed by IFRS and therefore may not be comparable to similar measures presented by other issuers. The Company defines free cash flow as cash generated from operations, less capital expenditures and investments in Aireon and equity related investments. Management places importance on this indicator as it assists in measuring the impact of its investment program on the Company's financial resources.

Cash flows from operations for the three months ended May 31, 2017 decreased by $29 from the three months ended May 31, 2016, primarily due to solvency deficiency payments of $24 and higher payments to employees and suppliers of $21, partially offset by $11 higher other receipts.

Cash outflows from investing activities for the three months ended May 31, 2017 were comparable to the three months ended May 31, 2016. In Q3 fiscal 2017, investment in capital projects was $40 (cash outflows of $37) compared to $32 in Q3 fiscal 2016 (cash outflows of $30). The cash outflows in Q3 fiscal 2017 were partially offset by proceeds from the sale of the Company's investment in Searidge of $4 and the receipt of the $1 remaining principal balance of related to the Company's investment in other notes.

Cash outflows from financing activities for the three months ended May 31, 2017 were $25 compared to inflows of $15 for the three months ended May 31, 2016. The outflow was a result of the annual $25 principal repayment of the Series 97-2 amortizing revenue bonds. In the three months ended May 31, 2016 the Company also had net proceeds from bank loans of $40.

For the three months ended May 31, 2016, our cash and cash equivalents balance increased by $13. This was primarily due to net proceeds from bank loans of $40 and cash inflows from operations of $28, partially offset by cash outflows for capital projects of $30 and the annual $25 principal repayment of the Series 97-2 amortizing revenue bonds.

(in millions of dollars)

Cash flows for the nine months ended May 31, 2017

	Nine months ended May		
	2017	2016	Change
Cash flows from:			
Operations	$ 58	$ 124	$ (66)
Investing	179	(65)	244
Financing	(135)	(218)	83
Cash flows from operating, investing and financing activities	102	(159)	261
Effect of foreign exchange on cash and cash equivalents	(3)	1	(4)
Increase (decrease) in cash and cash equivalents	99	(158)	257
Cash and cash equivalents, beginning of period	119	230	(111)
Cash and cash equivalents, end of period	$ 218	$ 72	$ 146
Free cash flow (non-GAAP financial measure):			
Cash flows from:			
Operations	$ 58	$ 124	$ (66)
Capital expenditures[(1)]	(97)	(93)	(4)
Investment in preferred interests[(1)]	(16)	-	(16)
Income tax payment on investment in preferred interests[(1)]	(5)	-	(5)
Proceeds from sale of investment in subsidiary[(1)]	4	-	4
Free cash flow	$ (56)	$ 31	$ (87)

(1) See the statements of cash flows of our Q3 fiscal 2017 financial statements.

As shown above, cash and cash equivalents increased by $99 for the nine months ended May 31, 2017 and the Company experienced negative free cash flow of $56, which is a non-GAAP financial measure as discussed in "LIQUIDITY AND CAPITAL RESOURCES – Cash flows for the three months ended May 31, 2017".

Cash flows from operations for the nine months ended May 31, 2017 decreased by $66 from the nine months ended May 31, 2016, primarily due to higher payments to employees and suppliers of $41, lower receipts from customer service charges of $36 and solvency deficiency payments of $24, partially offset by lower pension special payment contributions of $18, lower interest payments of $10 and higher other receipts of $7.

Cash flows from investing activities for the nine months ended May 31, 2017 were inflows of $179 compared to outflows of $65 in the nine months ended May 31, 2016. During the nine months ended May 31, 2017, we received $293 of proceeds from MAV II notes, other notes and restructured ABCP compared to $2 received in the nine months ended May 31, 2016. Additionally, proceeds of $4 were received from the sale of a portion of the Company's investment in Searidge. These cash inflows were partially offset by an investment of $102 in capital projects (cash outflows of $97) compared to $94 in the nine months ended May 31, 2016 (cash outflows of $93). In addition, we invested an additional $16 in investments in preferred interests and made an income tax payment of $5 related to that investment. In fiscal 2016, the Company received recoverable input tax payments of $26 on termination of the cross border transaction. No similar payment was received in fiscal 2017.

(in millions of dollars)

Cash outflows from financing activities for the nine months ended May 31, 2017 were $135 compared to $218 for the nine months ended May 31, 2016. The outflows were a result of the early redemption of $100 of the $350 Series MTN 2009-1 General Obligation Notes at a redemption price of $110 and the annual $25 principal repayment of the Series 97-2 amortizing revenue bonds.

For the nine months ended May 31, 2016, our cash and cash equivalents balance decreased by $158. This was primarily due to repayment of the $450 Series MTN 2006-1 General Obligation Notes, the payment of $51 to settle the interest rate swap agreements, investment in capital projects of $93 (excluding capitalized interest) and the annual $25 principal repayment of the Series 97-2 amortizing revenue bonds. These cash outflows were partially offset by the issuance of the $250 Series MTN 2016-1 General Obligation Notes ($248 net of transaction costs), cash inflows from operations of $124, net proceeds from bank loans of $40, the receipt of $26 in recoverable input tax payments on termination of the cross border transaction and a $20 drawdown of surplus funds from the debt service reserve fund.

Liquidity and Financing Strategy

Our liquidity and financing strategy remains unchanged from that disclosed in our fiscal 2016 annual MD&A.

During the nine months ended May 31, 2017, the Company redeemed $100 of the $350 Series MTN 2009-1 General Obligation Notes with proceeds from the MAV II notes and surplus cash.

We are exposed to re-financing risk with respect to our bond and note maturities, including the $25 annual amortizing payment due on the Series 97-2 amortizing revenue bonds. We mitigate this risk by maintaining committed credit facilities in an amount sufficient to meet our refinancing needs in the event of temporary capital market disruptions or lack of access to the market for any reason. The Company also has a Base Shelf Prospectus in place that is valid until December 6, 2017.

The Company has a revolving credit facility with a syndicate of Canadian financial institutions and separate letter of credit facilities for pension funding purposes. As at May 31, 2017, the credit facilities are utilized as follows:

Credit facilities:	
Credit facility with a syndicate of Canadian financial institutions[(1)]	$ 675
Letter of credit facilities for pension funding purposes[(2)]	515
Total available credit facilities	1,190
Less: Outstanding letters of credit[(2)]	490
Undrawn committed borrowing capacity	700
Less: Operations and maintenance reserve fund allocation[(3)]	270
Credit facilities available for unrestricted use	$ 430

(1) The Company's credit facility with a syndicate of Canadian financial institutions in the amount of $675 is comprised of two equal tranches maturing on September 12, 2019 and September 12, 2021. The credit facility agreement provides for loans at varying rates of interest based on certain benchmark interest rates, specifically the Canadian prime rate and the Canadian bankers' acceptance rate, and on the Company's credit rating at the time of drawdown. A utilization fee is also payable on borrowings in excess of 25% of the available facility. The Company is required to pay commitment fees, which are dependent on the Company's credit rating. The Company is in compliance with the credit facility covenants as at May 31, 2017.

(in millions of dollars)

(2) The letter of credit facilities for pension funding purposes are comprised of four facilities with Canadian financial institutions totalling $515, which will mature on December 31, 2017, unless extended. The Company intends to seek extensions of the maturity dates. Of the $490 in letters of credit shown above as outstanding as at May 31, 2017, $476 was drawn for pension solvency funding purposes. The remaining $14 includes letters of credit with a value of $3 issued on behalf of Searidge.

(3) The operations and maintenance reserve fund may be used to pay operating and maintenance expenses, if required (see also "LIQUIDITY AND CAPITAL RESOURCES – Financial Instruments and Risk Management: Reserve Funds and Financial Instruments").

The table below shows our long-term debt, liquidity and investments profile.

	May 31 2017	August 31 2016
LONG-TERM DEBT:		
Bonds and notes payable		
Under the Master Trust Indenture	$ 500	$ 525
Under the General Obligation Indenture	1,100	1,200
	1,600	1,725
Adjusted for deferred financing costs and discounts	(5)	(6)
Total bonds and notes payable	1,595	1,719
Less: current portion	(375)	(25)
Total non-current loans and borrowings	$ 1,220	$ 1,694
LIQUIDITY (excludes MAV II, restructured ABCP and other notes shown below):		
Cash and cash equivalents	$ 218	$ 119
Debt service reserve fund	95	94
	$ 313	$ 213
Undrawn committed borrowing capacity(1)	$ 700	$ 716
MAV II, RESTRUCTURED ABCP AND OTHER NOTES:		
Face value(2)	$ -	$ 293
Fair value variance from face value	-	(14)
	$ -	$ 279

(1) $430 of this borrowing capacity is available as described in the previous table (August 31, 2016 - $446).

(2) Proceeds of $293 were received during the nine months ended May 31, 2017.

Credit Ratings

The Company's debt obligations have been assigned the following credit ratings:

Rating Agency	Senior Debt	General Obligation Notes	Outlook
DBRS Limited (DBRS)	AA	AA (low)	Stable
Moody's Investors Service (Moody's)	Aa2	Aa2	Stable
Standard & Poor's (S&P)	AA	AA-	Stable

On March 27, 2017, Standard & Poor's (S&P) issued a press release affirming the Company's ratings and stable outlook. The press release noted the Company's credit strengths as holding a monopoly over an essential transportation service, legislated ability to levy user charges on airlines to meet financial requirements and sound debt service coverage ratios (DSCRs). They noted that the Company's weaknesses are a high but declining debt burden, air traffic demand exposure and a large solvency-based pension deficit.

S&P stated that "they expect the Company's rate reductions to erode its financial metrics temporarily." They went on to state, "nevertheless, we expect its financial profile to improve beginning in fiscal 2019, thanks to growing traffic and steady rate levels." They stated that they believe the Company has adequate liquidity but noted their expectation that "NAV CANADA will secure additional letter of credit capacity to fund any incremental pension funding requirements, thereby keeping its unrestricted borrowing capacity relatively stable over the next two years."

S&P noted that the Company's legislated perpetual monopoly is over civil air navigation in Canadian-controlled airspace and stated "accordingly, its air traffic volumes depend not on any one region, but the entire country and international airspace assigned to Canada by treaty. S&P therefore consider the Company's service area to be more diversified than that of airport operators, pointing to greater cash flow stability in support of debt service obligations."

On February 27, 2017, Moody's issued a credit opinion affirming NAV CANADA's base line credit assessment at aa2 and its senior and subordinated ratings at Aa2. Moody's noted the Company's following credit strengths:

- Essential infrastructure asset for the Canadian air transportation system;
- Monopoly provider of civil air navigation services over a very large airspace;
- Legislated right to establish and levy rates and charges as needed to meet financial requirements resulting in good degree of cash flow predictability;
- Continued strong traffic growth;
- Manageable capital expenditure program.

They also noted the following credit challenges:

- Defined benefit pension plan creates recurring calls on cash;
- Periods of weak debt service coverage ratio when the Company depletes its rate stabilization account.

They stated that "the rating outlook is stable, reflecting our expectation that NAV CANADA will be prudent and take into account its overall financial position and upcoming obligations when contemplating a rate decrease and vice versa that it will implement the necessary rate increases if traffic growth does not materialize."

(in millions of dollars)

Our credit ratings provided by DBRS remain unchanged from those described in our fiscal 2016 annual MD&A.

Cash Requirements

The following information about our contractual obligations and other commitments summarizes certain of our liquidity and capital resource requirements.

Pension Plans

Required pension contributions to the Company's pension plans are determined by annual actuarial valuations for funding purposes performed as at January 1 (see below under "Pension Contributions (Going Concern and Solvency)"). Our latest actuarial valuations (for funding purposes) as at January 1, 2016 were completed and filed with the Office of the Superintendent of Financial Institutions Canada in June 2016.

Pension Plans' Accounting Deficit: The Company's pension plans had an accounting deficit of $1,415 as at the annual measurement date of August 31, 2016 and an accounting deficit of $1,224 as at May 31, 2017. The $191 decrease in the deficit position during the nine months ended May 31, 2017 is primarily due to net actuarial gains of $257 and solvency deficiency contributions of $24, partially offset by actuarial accounting expense exceeding Company contributions by $89. The $257 of net actuarial gains are primarily due to a return on plan assets $239 greater than the expected return based on the discount rate at August 31, 2016 of 3.40%, and an $18 actuarial gain from a 10 basis point increase in the discount rate to 3.50% at May 31, 2017.

Regulatory Recovery of Pension Costs: As described in our fiscal 2016 annual MD&A, the Company uses a regulatory approach for pension costs to determine the net impact charged to net income (loss). The objective of this approach is to expense the cost of the Company's going concern cash contributions to the funded pension plans. In fiscal 2017, the Company made solvency contributions of $24 which are being deferred and are expected to be recovered by fiscal 2020.

The recovery of pension benefit costs was determined as follows:

	Nine months ended May 31 2017	Nine months ended May 31 2016
Funded pension plan contributions	$ 98	$ 90
Less: Solvency contributions	(24)	-
Unfunded pension plan expense	3	3
Recovery of pension benefit costs	$ 77	$ 93

(in millions of dollars)

The recovery of pension benefit costs is presented in the statement of operations as follows:

	Nine months ended May 31 2017	Nine months ended May 31 2016
Pension benefit costs (Per IAS 19 *Employee Benefits*)		
Current service costs	$ 132	$ 109
Net interest costs related to employee benefits	34	24
Net movement in regulatory deferral account related to pensions		
Regulatory decrease	(89)	(40)
Recovery of pension benefit costs	$ 77	$ 93

Pension Contributions (Going Concern and Solvency): The actuarial valuations for funding purposes of the pension plans performed as at January 1, 2016 reported a going concern deficit of $76 (January 1, 2015 – a deficit of $268).

The regulations governing the funding of federally regulated pension plans include a solvency test, which assumes the plans are terminated as at the valuation date. The actuarial valuations performed as at January 1, 2016 reported a statutory solvency deficiency of $306 (January 1, 2015 – a statutory solvency deficiency of $556).

Pension funding regulations came into effect in April 2011 permitting solvency special payments to be replaced by letters of credit, provided the total value of the letters of credit does not exceed 15% of the pension plan's assets. As of May 31, 2017, the Company has put in place letters of credit totaling $476 (representing 8% of registered pension plan assets as at May 31, 2017) to meet its cumulative pension solvency funding requirements. Commencing in April 2017, the Company began funding its remaining calendar 2017 solvency funding requirements of $45 with cash contributions. As at May 31, 2017, solvency contributions of $24 have been made. For the annual period beginning July 1, 2017, solvency funding requirements will be based on the January 1, 2017 actuarial valuations.

The amount of required Company contributions and additional letters of credit for future years will be dependent on the investment experience of plan assets, the discount rates and other assumptions that will be used in future actuarial valuations to determine plan liabilities, as well as any changes in pension plan design or funding requirements that may be enacted.

(in millions of dollars)

Contractual Obligations

A breakdown of contractual obligations for the next five fiscal years and thereafter is presented in the following table.

	Remaining payments – for years ending August 31						
	Total	2017	2018	2019	2020	2021	Thereafter
Derivative liabilities	$ 21	$ -	$ -	$ 21	$ -	$ -	$ -
Long-term debt (including current portion)(1), (2)	1,600	-	375	275	25	275	650
Interest payments(2)	628	16	77	69	53	46	367
Capital commitments(3)	155	46	49	13	15	6	26
Operating leases	39	2	8	7	7	6	9
Investment in preferred interests in Aireon(4)	20	-	20	-	-	-	-
Total contractual obligations	$ 2,463	$ 64	$ 529	$ 385	$ 100	$ 333	$ 1,052

Total contractual obligations exclude commitments for goods and services in the ordinary course of business. Also excluded are other long-term liabilities mainly due to reasons of uncertainty of timing of cash flows and items that are non-cash in-nature.

(1) Payments represent principal of $1,600. The Company intends to refinance principal maturities at their maturity dates. The Company may choose to repay a portion of these maturities with available cash, and/or may increase the size of a re-financing to generate additional liquidity or for other purposes, and/or may choose to redeem, in whole or in part, an issue in advance of its scheduled maturity date.

(2) Further details on interest rates and maturity dates on long-term debt are provided in note 21 to our fiscal 2016 annual consolidated financial statements.

(3) The Company has firm commitments for the acquisition of property, plant and equipment and intangible assets amounting to $155 as at May 31, 2017 (August 31, 2016 - $118).

(4) Payments represent contractual obligations to invest in preferred interests of Aireon, subject to conditions pursuant to the agreements the Company entered into in November 2012 which set out the terms of its participation in Aireon, as amended. Amounts are presented in CDN translated using the hedged rate for the remaining tranche investment. This payment is expected to be made by July 31, 2017.

The Company's letters of credit are discussed under the heading "LIQUIDITY AND CAPITAL RESOURCES – Liquidity and Financing Strategy".

The Company's contributions to its pension plans are discussed under the heading "LIQUIDITY AND CAPITAL RESOURCES – Cash Requirements: Pension Plans".

(in millions of dollars)

Capital Management

The Company views capital as the sum of its issued long-term debt, retained earnings (deficit) and accumulated other comprehensive income, regulatory deferral accounts and certain employee benefits, as depicted in the following table. This definition of capital is used by management and may not be comparable to measures presented by other companies.

	May 31 2017	August 31 2016
Bonds and notes payable	$ 1,595	$ 1,719
Equity:		
Retained earnings (deficit)	(14)	28
Regulatory deferral accounts:		
Debit balances	(1,433)	(1,708)
Credit balances	433	476
Employee benefits:		
LTD (asset) liability	(3)	1
Liability for funded pension benefits	1,126	1,346
Liability for accumulating sick leave	21	21
Total capital	$ 1,725	$ 1,883

Management's approach and objectives when managing capital remain unchanged from those described in our fiscal 2016 annual MD&A.

Financial Instruments and Risk Management

Restructured and Other Investments in ABCP[4]

(See also "LIQUIDITY AND CAPITAL RESOURCES – Liquidity and Financing Strategy").

During the nine months ended May 31, 2017, the Company received $293 which includes the remaining $285 principal balance of MAV II Class A-1 and Class A-2 notes, the remaining $7 balance of restructured ABCP and the remaining balance of its investments in other notes of $1. Fair value provisions of $14 related to the notes were released.

Reserve Funds and Financial Instruments

Under the Master Trust Indenture, we maintain a debt service reserve fund and an operations and maintenance reserve fund. We are also required to meet certain minimum liquidity levels under the General Obligation Indenture. The requirements of the debt service reserve fund and the operations and maintenance reserve fund remain unchanged from that described in our fiscal 2016 annual MD&A.

Financial Risk Management

The Company is exposed to several risks as a result of holding financial instruments, including interest rate risk, foreign exchange risk, price risk, credit risk and liquidity risk. The Company's exposure to financial risks and how the Company manages each of those risks are described in the Company's fiscal 2016 annual MD&A. There were no significant changes to those risks or to the Company's management of exposure to those risks during the nine months ended May 31, 2017, except as noted below.

[4] Note: See "INTRODUCTION – Caution Concerning Forward-Looking Information", page 1

Interest Rate Risk: During the nine months ended May 31, 2017, the Company received the remaining principal relating to its investments in MAV II notes, investments in other notes, and the remaining principal balance of ABCP, decreasing the Company's financial assets exposed to interest rate risk. These investments had earned interest at variable rates. The receipt of these notes also reduced the Company's exposure to price and credit risk.

As at May 31, 2017, the Company has $313 invested in financial assets that bear interest at floating rates. If interest rates decline, earnings on these instruments will fall. A 100 basis point change in variable interest rates would result in an annual impact of approximately $3 in the Company's earnings before rate stabilization adjustments.

Foreign Exchange Risk: The Company designates certain of its forward contracts as cash flow hedging instruments to hedge the Company's exposure to the impact of exchange rate fluctuations. As at May 31, 2017, the Company has entered into a forward contract to purchase $15 U.S. ($20 CDN) to hedge the Canadian dollar cost related to its outstanding commitment to acquire additional preferred interests in Aireon.

The foreign exchange rate sensitivity is the net amount of foreign exchange rate exposure of the items at the reporting date, less foreign currency hedges. As at May 31, 2017, if the Canadian dollar strengthened or weakened by 10% against the U.S. dollar, all other variables remaining constant, net income (loss) before net movement in regulatory deferral accounts would have been impacted by $35 (August 31, 2016 - $29).

Other Price Risk: The fourth tranche investment in preferred interests of Aireon was made on December 21, 2016. As a result of the additional investment, the fair value of the investment in Aireon increased to $342 as at May 31, 2017 (August 31, 2016 - $291). A change of 5% in the fair value would impact finance income (other finance costs) by approximately $11 U.S. ($15 CDN) as at May 31, 2017 (August 31, 2016 - $10 U.S. ($13 CDN)).

Legal Proceedings

The Company is party to certain legal proceedings in the ordinary course of its business. Management does not expect the outcome of any of these proceedings to have a material adverse effect on the consolidated financial position or results of operations of the Company.

CHANGES IN ACCOUNTING POLICIES

The Company's Q3 fiscal 2017 financial statements were prepared in accordance with IAS 34 *Interim Financial Reporting* as issued by the International Accounting Standards Board (IASB). Except as described below, significant accounting policies used in the Q3 fiscal 2017 financial statements are disclosed in note 3 of the Company's fiscal 2016 annual consolidated financial statements, except for the application of new standards, amendments and interpretations effective September 1, 2016. The accounting policies have been applied consistently to all periods presented, unless otherwise indicated.

In December 2014, the IASB issued Disclosure Initiative (Amendments to IAS 1 *Presentation of Financial Statements*). These amendments improve the existing presentation and disclosure requirements and encourage entities to apply professional judgment regarding disclosure and presentation in their financial statements. These amendments were adopted effective September 1, 2016. The adoption of these amendments resulted in no change to the Q3 fiscal 2017 financial statements. Immaterial disclosures are expected to be removed from the Company's annual consolidated financial statements.

In April 2017, the Company sold a portion of its investment in Searidge which is owned through NAV CANADA ATM Inc. As a result of the sale, the Company now owns 50% (August 31, 2016 – 70%) of the issued and outstanding shares of Searidge.

The Company has classified its investment in Searidge as an investment in a joint venture. A joint venture exists when there is a contractual arrangement that establishes joint control over its activities and requires unanimous consent of the parties sharing control for strategic financial and operating decisions, and where the parties have rights to the net assets of the arrangement.

Interests in joint ventures are accounted for using the equity method. They are initially recognized at cost, which includes transaction costs. Subsequent to initial recognition, the consolidated financial statements include the participant's share of the net income (loss) and other comprehensive income of equity-accounted investees, until the date on which joint control ceases. The Company's investment in the equity-accounted investee is reduced for distributions received during the fiscal year.

If the Company's share of losses of the equity-accounted investee equals or exceeds its interest in the equity-accounted investee, the Company discontinues recognizing its share of further losses. Additional losses are provided for, and a liability is recognized only to the extent the Company has incurred legal or constructive obligations or made payments on behalf of the equity-accounted investee.

Future Accounting Pronouncements

The IASB has issued a number of standards and amendments that are not yet effective. The Company continues to analyze these standards and amendments to determine the extent of their impact on its consolidated financial statements.

The Company has commenced its analysis of IFRS 9 *Financial Instruments* (IFRS 9) and expects to early adopt the requirements of the new standard with a date of initial application of September 1, 2017, applying all of the requirements of IFRS 9 retrospectively (prospectively for hedging requirements) without restatement of comparatives. While the adoption of IFRS 9 is expected to change the classification of several of the Company's financial instruments, the changes in classification are not expected to result in any changes in measurement. The new impairment guidelines are expected to impact the Company's carrying value of financial assets at amortized cost. The impact of the loss allowance is currently being quantified but is not expected to be material. The Company also expects to increase disclosures related to its hedging relationships. These assessments were made based on an analysis of the Company's financial instruments as at May 31, 2017 and the facts and circumstances that existed at that date. As facts and circumstances may change during the period leading up to the initial date of application, the assessment of the potential impacts is subject to change.

The Company is in the process of assessing the anticipated impact of IFRS 15 *Revenue from Contracts with Customers* on its consolidated financial statements. The Company has formed a project team to evaluate and implement the standard and has begun a detailed review of its current contracts under the standard's five-step model.

At this time, the Company does not expect to adopt any of the other standards or amendments noted in our fiscal 2016 annual MD&A before their respective effective dates.

CRITICAL ACCOUNTING ESTIMATES AND JUDGMENTS

The preparation of financial statements in conformity with IFRS requires management to make estimates and judgments that affect the reported amounts of revenue and expenses during the period, the reported amounts of assets and liabilities, and the disclosure of commitments and contingencies at the date of the financial statements. These estimates and judgments are based on historical experience, current conditions and various other assumptions made by management that are believed to be reasonable under the circumstances. By their nature, these estimates and judgments are subject to uncertainty and the amounts currently reported in the Company's consolidated financial statements could, in future, prove to be inaccurate. Any changes from those estimates and judgments could have a material impact on our consolidated financial statements. The estimates and judgments are reviewed on an ongoing basis.

The Company's critical accounting estimates and judgments applied in the preparation of the Company's Q3 fiscal 2017 financial statements are consistent with those applied and disclosed in our fiscal 2016 annual consolidated financial statements and as described in the fiscal 2016 annual MD&A.

DISCLOSURE CONTROLS AND PROCEDURES AND INTERNAL CONTROL OVER FINANCIAL REPORTING

There have been no changes to the Company's internal control over financial reporting (ICFR) during the quarter ended May 31, 2017 that have materially affected or are reasonably likely to materially affect the Company's ICFR.