# TOROMONT WORKS

TOROMONT

**TOROMONT INDUSTRIES LTD.** employs approximately 4,400 people in over 115 locations, predominantly in Canada and the United States. Toromont is listed on the Toronto Stock Exchange under the symbol TIH. The Company serves its customers through two business groups.

## EQUIPMENT GROUP


Equipment Group sells, rents and services a broad range of mobile equipment and industrial engines. Our Caterpillar dealership – servicing Ontario, Manitoba, Newfoundland/eastern Labrador and Nunavut – is one of the world's largest in terms of revenue and geographic territory. Battlefield – The CAT Rental Store is a leading equipment rental operation also providing one-stop shopping for construction supplies.

## COMPRESSION GROUP

Compression Group is a North American leader in designing, engineering, fabricating, installing and servicing compression systems for natural gas, fuel gas, coal-bed methane, carbon dioxide and process systems, and industrial and recreational refrigeration. It specializes in delivering custom systems and maintaining them with its growing field service resources.

The past year has been good to Toromont. Compared to 2004, revenue was up 12% to $1.6 billion and net earnings also climbed 12% to $79 million. These records are milestones to mark, but we are focused on the future. With our strategic approach to business development at home and abroad, our innovative products and services, and our culture of ownership and action, 2006 promises to be an exciting year for our shareholders, customers and employees alike.

# 20 YEARS OF GROWTH

## 1985-2005

Since 1985, Toromont has employed a business model focused on balance, discipline and accountability. It has paid off. A 1985 investment of $100 in Toromont stock – with dividends reinvested – was worth $10,523 at December 31, 2005. The same amount invested in the S&P/TSX Composite Index was worth $635. This financial history, combined with prudent planning for the future, has earned us investor confidence, and a reputation as one of the TSX's top long-term performers.

**$100 INVESTED IN 1985...**

### 85

Robert Ogilvie and Wayne Hill join Toromont as President and Vice President Finance respectively

Toromont purchases 40% interest in Enerflex Systems Ltd. for $5 million

### 87

Robert Ogilvie appointed Chairman, President and CEO

### 88

Toromont increases interest in Enerflex to 51% and acquires and integrates PAMCO (a major competitor)

Acquisition of ScottPolar Corporation (Commercial Refrigeration) and integration with Kimmel-Motz

### 89

Toromont employment reaches 1,000

Return on Equity exceeds 15% for first time since 1981

### 90

Sale of Canada Forgings Division

Acquisition of J.H. Lock & Sons

### 91

Toromont declares special dividend

### 93

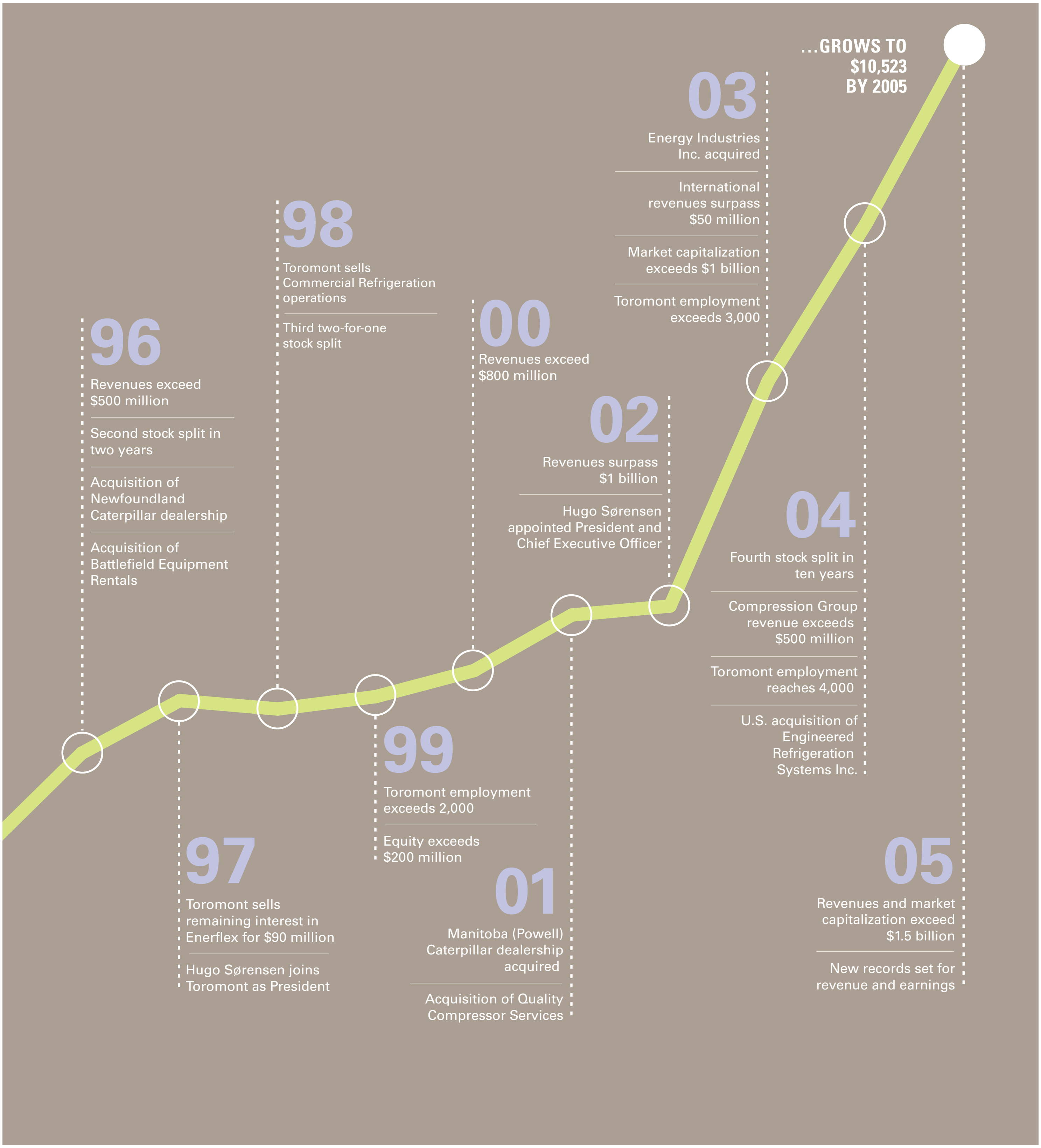
First underwriting of Toromont shares since going public in 1968

IPO of common shares of Enerflex and reduction of ownership position to 30%

Acquisition of Ontario Caterpillar dealership

### 94

Two-for-one subdivision of common shares of Toromont


…GROWS TO $10,523 BY 2005
96
Revenues exceed $500 million
Second stock split in two years
Acquisition of Newfoundland Caterpillar dealership
Acquisition of Battlefield Equipment Rentals
97
Toromont sells remaining interest in Enerflex for $90 million
Hugo Sørensen joins Toromont as President
98
Toromont sells Commercial Refrigeration operations
Third two-for-one stock split
99
Toromont employment exceeds 2,000
Equity exceeds $200 million
00
Revenues exceed $800 million
01
Manitoba (Powell) Caterpillar dealership acquired
Acquisition of Quality Compressor Services
02
Revenues surpass $1 billion
Hugo Sørensen appointed President and Chief Executive Officer
03
Energy Industries Inc. acquired
International revenues surpass $50 million
Market capitalization exceeds $1 billion
Toromont employment exceeds 3,000
04
Fourth stock split in ten years
Compression Group revenue exceeds $500 million
Toromont employment reaches 4,000
U.S. acquisition of Engineered Refrigeration Systems Inc.
05
Revenues and market capitalization exceed $1.5 billion
New records set for revenue and earnings

# FELLOW SHAREHOLDERS:

Our objective is to build a strong, sustainable company with a passionate focus on annual improvement and long-term performance. We have never wavered from this commitment. We never will.

In 2005, while preserving our solid financial foundation, Toromont's:

- revenue grew 12% over 2004 to a record $1.6 billion,
- net earnings increased 12% to a record $79 million,
- basic earnings per share of $1.25 were 13% higher than a year ago, and
- return on opening shareholders' equity was 18.9%.

With even greater satisfaction, Toromont marked several exceptional milestones. 2005 represented our:

- 37th consecutive year of dividend payments – and 16th consecutive year of higher dividend payouts, a record that will be sustained in 2006 with the 25% dividend increase announced by the Board effective with the April 3rd payout,
- 9th year of the last 10 that return on shareholders' equity has exceeded 15%, and
- 13th consecutive year of revenue growth from continuing operations.

Toromont's total 20 year return places it among the top performing investments on The Toronto Stock Exchange.

These achievements are not a matter of chance. They are the result of the constant application of long-term strategies driven by a proven business model and philosophy.

That 'Toromont works' and works well is as much a testimony to the strong efforts of our 4,400 employees today as it is to Toromont's discipline in staying the course set out many years ago.

### STAYING THE COURSE WORKS

For a business to 'work,' it must be guided by a strong set of principles and values that do not change with time. It must then give life to these principles through its business model and strategies. Toromont does.

We believe in diversification. To offset economic fluctuations, Toromont includes Compression and Equipment businesses, each with diverse economic drivers, markets, customers and profitability profiles as well as different capital needs.

Diversification also leads to balance – another key principle. Balance between Equipment and Compression, and balance between new product sales and ongoing customer support, the latter providing a long-term revenue 'annuity.'

By adhering to these principles, Toromont achieved greater diversification and balance than ever in 2005:

- The ratio of Equipment to Compression revenue was a healthy 57:43 (compared to 71:29 five years ago).
- Product support revenue increased 16% on a consolidated basis to a record $407 million.
- International revenue of $70 million represented 4% of consolidated revenue – up from 2% three years ago despite 52% growth over the period in domestic revenue.
- We served thousands of customers in a wide variety of industries.

We are also disciplined in consistently seeking strong Returns on Capital Employed (ROCE) to meet our long-term Return on Equity (ROE) target. This discipline manifests itself in our allocation of capital, and the choice of businesses in which we operate. We strive to be nothing less than the leader in our markets. Toromont businesses have meaningful competitive advantages that can be made stronger through increasing customer intimacy.

Within Equipment, we are proud of our long-term partnership with Caterpillar, the world's number one heavy equipment manufacturer. Over the past 13 years, Toromont has secured Caterpillar dealerships in Ontario, Newfoundland, eastern Labrador, Manitoba and Nunavut. This puts us in exclusive company as a member of a highly respected, competitively advantaged global fraternity of dealers.

Over the years, Toromont has increased the value of its Caterpillar business through customer-focused investments in e-commerce, in-field resources and branch networks. Each has strengthened the bonds of service and trust we have with customers, and created an additional competitive advantage: long-term service agreements. We now have 647 such agreements in our territories, up 91% from five years ago. Through the acquisition of Battlefield – The CAT Rental Store in 1996 and systematic growth in rental fleets and storefronts, we have enhanced our Equipment Group and added substantial rental revenue to our mix. Our investment in the Equipment Group continues to generate growth with revenues increasing 11% in the year.

The Company signed a Letter of Intent for a five-year agreement with the Ontario Power Authority for the sale of electricity produced at certain co-generation plants. Under the terms of this agreement, revenues generated will not be sufficient to cover costs and thus the assets were written down by $17.8 million in the fourth quarter of 2005. While we are extremely displeased with this outcome, we are, however, now able to put this matter behind us. Given the current regulatory environment in Ontario, no new power generation investments are anticipated.

The Compression Group's competitive advantages begin with the specialized engineering knowledge of its people. These skills enable us to win market share though the development of custom systems for multiple applications. Compression has added to its advantages by growing its extensive service and support resources – now including several hundred field personnel in addition to 52 locations – and aligning itself with many proven partners. Preferred supplier status with the National Hockey League is also a major differentiator. The Compression Group's advantages paid off with record revenue and earnings in each of the past five years. In 2005, Compression delivered 12% growth in revenue.

## A CONSERVATIVE FINANCIAL POSTURE WORKS

Our strong, conservative balance sheet is an important competitive advantage that allows us to fully support our growth opportunities, optimize cost of capital and reduce shareholder risk. Consequently, we maintain a solid financial foundation to ensure Toromont works well into the future. Our total debt, net of cash, as a ratio to shareholders' equity has averaged 0.5:1 over the past 12 years.

### OWNERSHIP WORKS

A primary reason 'Toromont works' is our talented, committed workforce. We have created a strong culture of ownership and lead by example.

Specific ownership guidelines have been in place for our directors and CEO for many years and we are proud to report that each member of the Board and the CEO own more than the prescribed levels. Our management team is also infused with the spirit of ownership. At December 31, 2005, the Board, management and employees owned over 7% of Toromont's common shares.

We have structured our businesses to be autonomous and fiercely competitive. Decentralized decision-making puts power where it belongs: at our customer's place of business.

We have high standards as outlined in our Code of Business Conduct found at www.toromont.com. We recognize – with pride – the accomplishments of our employees. This creates intrinsic motivation for all staff because they 'own' the decisions they make and are rewarded for good performance. We also take great pride in our customer relationships. In 2005, we were privileged to work far and wide with customers on important projects and prouder still of the fact that a large percentage of our customers are in fact long-term partners.

We continuously invest in leadership and skills training and have made succession preparation a high priority. This has paid off. We have promoted many Toromont people into senior positions in the past years, and as our financial performance demonstrates, we have not missed a beat.

In industries where turnover is often high and potential new hires scarce, our entrepreneurial ownership culture is a competitive advantage. Many of our employees have been with us for more than 10 years and our employment base grew 9% in 2005. The talent pool is large, thanks in part to our management trainee and apprenticeship programs.

### PRUDENCE WORKS

Across our operations, we have an intense focus on safety. Our goal is to be the safest company in our industries with zero lost time due to accidents. To this end, we have challenged our businesses to formulate specific action plans. They have. In 2006, we will launch a new formal safety initiative within our Caterpillar dealership and we will develop and roll out a new safety award and awareness program at Toromont Energy Systems. These complement ongoing activities in all divisions.

### THINKING AHEAD WORKS

We set annual and long-term objectives that are consistent with our strategies and principles. Currently, we are working toward our "*Seven by 7*" objectives – a journey focusing on the attainment by 2007 of seven aggressive corporate objectives for revenue growth and composition, earnings, dividends, succession planning, safety and employee pride.

We are in the middle year of this initiative, and while there are no guarantees we will achieve "*Seven by 7*," we are progressing well. More importantly, we are determined not to stop there. When 2007 comes, we will raise the performance bar once again and challenge ourselves to do more. This is the Toromont way, and it's another reason why Toromont works.

### 2006 COMPRESSION AGENDA

Looking ahead, growth prospects are strong. Compression is well positioned. Entering 2006, it sports record order backlogs and an aggressive operating agenda, which includes:

- Capitalizing on our expanded footprint of TESI service and sales offices – such as those opened in West Texas, Alberta and Wyoming in 2005 and early 2006,
- Adding skilled engineers and production staff at TESI to meet unprecedented demand in the energy sector,
- Gaining new efficiencies from the roll out of a comprehensive e-business system at TESI which will enhance quotation, material procurement and production,

- Improving working capital management, and
- Achieving better efficiencies and cost effectiveness at CIMCO which has internationalized its business in each of the last two years – in 2005, through the addition of an initial manufacturing facility in China and in 2004 through the acquisition of a refrigeration business in the U.S.

Compression has worked well to manage the challenges of unprecedented growth in the past year and seeks continuous improvement in 2006.

### 2006 EQUIPMENT AGENDA

Gross Domestic Product is a prime indicator for the equipment industry. Economists broadly forecast another good year in 2006. Our Equipment Group is ready. Among its key initiatives:

- Increase sales, service, market coverage and share in selected geographic regions,
- Enhance efficiencies, cost-effectiveness and responsiveness in delivering customer service and maintenance across our massive installed base,
- Further leverage Toromont CAT and Battlefield synergies by opening a second joint branch in Orillia, Ontario,
- Implement a new automated asset tracking system at Battlefield – The CAT Rental Store to increase product availability and usage, while investing in our rental fleets, and
- Support customers in the use of advanced technologies such as laser-GPS guided grading systems and prepare them for new 2007 emission requirements already met by Caterpillar's advanced ACERT engine.

### SPECIAL THANKS

We sincerely thank our shareholders for their loyalty, customers for their patronage and our partners for their support. Internally, we thank all members of our team including our dedicated Directors who continue to provide wise counsel. Special thanks also to Wayne Hill, who served with distinction as Chief Financial Officer of Toromont for 20 years. We are grateful that Wayne continues to apply his exceptional insight as Executive Vice President and as a member of our Board.

### CONCLUSION

Over time, the Toromont model has done well. We are confident it will continue to do so because it's built on sensible business principles: discipline, diversification, balance, leadership, ownership, accountability, conservative leverage, prudence and pride.

There are always economic challenges to face. We cannot control the economy, nor can we predict the future. Neither can we guarantee good results every year. What we do commit to is that we will stay the course that has made our Company a high value performer over the last two decades and to ensure Toromont works in the future as well as it has in the past.

Yours sincerely,

**Hugo T. Sørensen**
President and
Chief Executive Officer

**Robert M. Ogilvie**
Chairman of the Board

# GROWING MARKETS

Thanks to expanded markets, investment in resources, product innovation and great customer support, Toromont grew impressively in 2005. To ensure a strong 2006, we will stick to the plan and never falter in our rigorous attention to market change and competition.

We see opportunity ahead in many different markets. Prospects for both our Compression and Equipment businesses are strong.

Sustaining profitable growth requires more than recognizing opportunity. It takes a constant and critical assessment of market and competitive dynamics to seize, manage and fuel growth for the long term.

We understand these requirements and have committed each year to a disciplined planning process that allows us to make informed choices. Once made, we monitor leading indicators, often using our powerful e-business tools, to ensure our decisions remain sound.

In 2006, our planning tells us to once again focus on traditional areas within Compression and Equipment where we have significant opportunities, and to capitalize on attractive emerging markets.

facing **On-site service of compression equipment.**
top **A compression system for natural gas storage.**
bottom **Our equipment at work in land development.**

## GROWING COMPRESSION

For Toromont Energy Systems Inc. (TESI), compression and process refrigeration offer attractive growth prospects fueled by brisk activity in the energy sector.

In the compression market, we specialize in reciprocating and rotary screw technologies to recover natural gas and coal-bed methane. Coal-bed methane activity is a strong growth area for Toromont, and we are a leading supplier of CBM-compression. Approximately 38% of all 2005 orders placed with TESI were CBM-related.

In the compression market, the stage is set for another good year. Demand for gas compression is unprecedented. TESI enters 2006 with significant opportunities in many markets, including U.S. gas compression where it made substantial gains in 2005. But there are challenges. Customers need rapid delivery to meet aggressive exploration requirements. Manufacturers that can deliver in time get the order. Responsive service and the ability to maintain equipment are competitive advantages.

**TOROMONT ENERGY SYSTEMS**

**John Pauk,** President, Toromont Energy Services
**Ivan Heidecker,** Vice President, Canadian Operations
**Dave Duncan,** President, Toromont Energy Systems Inc.
**Jerry Fraelic,** Vice President, U.S. Operations

*"Energy industry growth prospects are unprecedented. Record drilling activity is expected. Our plan is to aggressively recruit and train skilled employees to meet demand, expand our rental market share, provide new customer support capabilities, capitalize on our growing presence in the northern Rocky Mountain states and international markets, and maintain our leadership in western Canada."*

Understanding these dynamics, we are emphasizing:

- sales and market coverage expansion where customer activity is strong and we can expand our packaging expertise,
- improved customer responsiveness and market share gains, in part through efficient manufacturing of pre-built, standardized modules that can be customized and ready for rapid delivery when opportunity calls, and
- alliances and preferred vendor relationships.

In process markets, we cover considerable territory. Our process technologies, screw compressors and refrigeration equipment are used by hydrocarbon processors, gas-fired power plants, the polyethylene industry, syngas plants and $CO_2$ facilities.

Opportunities in process vary. In 2006, we will concentrate on securing growth in fertile areas, including natural gas, alternative gas processing and the $CO_2$ market.

In all TESI markets, we will emphasize our leading service and maintenance capabilities. Investments in our growing network of branches (including our newest sales offices in Wyoming, west Texas and Alberta), in-field resources, our e-business iMACS initiative (see page 18) and an employee training centre will allow us to fuel and manage opportunities.

Growth doesn't stop with TESI. In industrial and recreational refrigeration, our CIMCO business is positioned to grow its markets using its specialized engineering talent, extensive regional coverage and its reputation as the industry leader. As a well-established business, CIMCO has some 7,000 accounts including leading food, beverage and cold storage companies in North America, as well as several well-known names in professional sports.

For CIMCO, Eco-Chill technology (see page 19) continues to gain momentum. For 2006, it factors prominently in growth plans, as does growth in international sales and customer support. Our focus is to continue to increase our installed base, capitalize on growth in new geographic markets and market segments, such as industrial process cooling for automotive and plastics, and cost-effectively provide total maintenance. CIMCO's ability to offer total service and maintenance is a competitive advantage that has grown over the years through organic investments and a U.S. acquisition in 2004.


## GROWING EQUIPMENT

Our Equipment businesses are in growth mode, fueled by brisk, broad-based activity in our territories and strong demand for Caterpillar equipment. We are ready.

Our dealership is organized into five regions so as to be customer and market focused. This allows us to effectively serve the specific needs of our broad customer base.

We also have a Power Systems division that secures opportunities for CAT® engine sales and service for the on-highway truck market, in alliance with our Truck Engine Product Support (TEPS) dealers. Power Systems is also a leader in providing engines and support to marine, industrial, standby and prime power markets. Add to this our autonomous rental operation, Battlefield – The Cat Rental Store, and its specialized industrial rental service operation, Jobsite, and we have a leading presence across our territory.

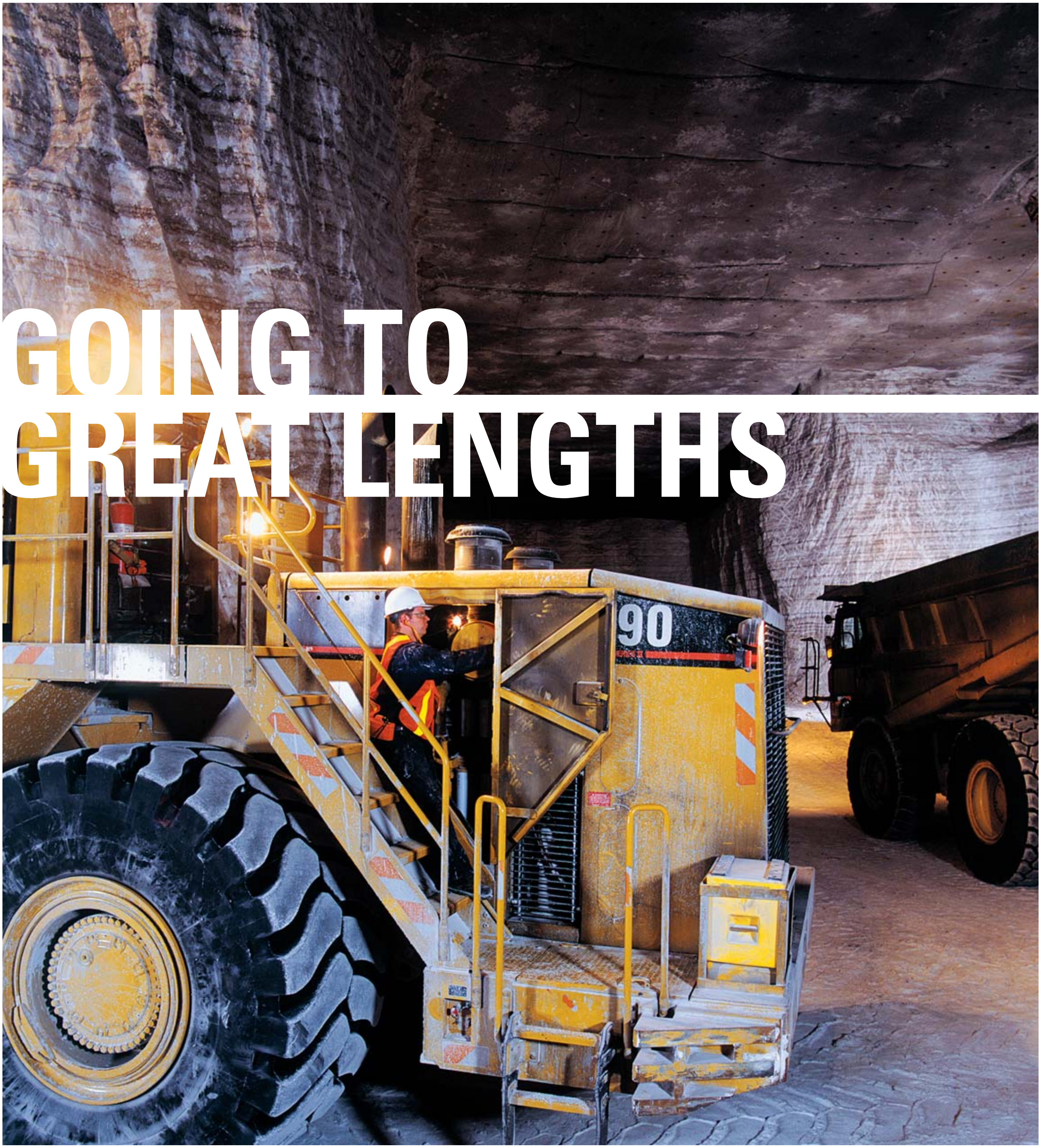
Operationally, we have intensified our market coverage for 2006 and will continue with a number of important initiatives, such as increasing our mobile service capabilities and further penetrating growing segments such as waste management. We have also stratified our service and maintenance offering to give customers more choice. Our Customer Support Centre (see page 18) is contributing to service responsiveness, as is our PartStore™, which enables on-line parts ordering.

The addition of a combined Toromont CAT-Battlefield store in Orillia later this year will allow us to better serve the needs of this high growth area of Ontario. Other Battlefield stores are planned in selected markets and Battlefield is positioning itself to better serve specialty trades contractors – another growing market segment. It also sees its representation of CAT Compact Construction Equipment as a principal growth opportunity. Within Power Systems, a second Mechron facility opened at the beginning of 2006 to meet demand for auxiliary power units. Power Systems is also gearing up for the introduction of the advanced Caterpillar ACERT™ engine in 2006 which will meet 2007 emission standards.

With leading products, a large installed base and growing markets in our territories, Toromont will continue to work in 2006.


top **Battlefield – The CAT Rental Store responds to customer needs.**
bottom **Working with Caterpillar on sales, rentals and support.**

# GOING TO GREAT LENGTHS



Our strategy of diversification takes us from sub-arctic mine shafts 6,000 feet underground to oil and gas vessels 80 miles off Mexico's shore. Equally at home in Zurich, Rabat or Changchun, Toromont has been active in 100 different countries, identifying growth opportunities in each.

facing **Miners depend on our equipment and expertise.**
top **Our infield support team works where our customers work.**
bottom **Sour fuel gas compression, a growing market.**

One of Toromont's long-term goals is to generate 10% of its total annual revenue from international markets. This objective is part of our belief in the value of diversification and balance.

In 2006, we expect to ratchet closer to this target. Major growth areas are the former Soviet republics (natural gas and fuel gas, upstream and refinery), Asia-Pacific (gas, refrigeration and $CO_2$), the Middle East and Europe (particularly process refrigeration and $CO_2$). Toromont Energy Systems Inc. (TESI) targets opportunities in each and in recent years has expanded its international footprint, adding sales offices in Moscow, Kuala Lumpur and Jakarta and sales presence in Thailand, India, Korea and Bangladesh. We will strengthen its international presence again in 2006.

Also high on the list is China, where in late 2005 CIMCO opened an initial small factory. This investment equips us with the capabilities necessary to competitively design and fabricate ice making equipment locally and allows us to participate in more domestic sports projects.

CIMCO's presence in China is small but meaningful. The Chinese government recognized this when they awarded us with a contract to build compression equipment packages for three Olympic-sized ice rinks and a Speed Oval which are now under construction for the 2007 Asia Winter Games in Changchun, China. This was the second major sports project awarded to Toromont since our entry into China in 2004.

Our new customer support centre increases efficiency.

**TOROMONT CAT**

**Larry Moffatt,** Vice President, Power Systems, Toromont CAT
**Scott Medhurst,** President, Equipment Division, Toromont CAT

*"We foresee the day when Toromont will become a $1 billion Caterpillar dealer. To achieve this milestone our agenda is sharply focused on penetrating growth segments including specialty trades, mining and site development, leveraging our industry-leading resources to set new standards for preventative maintenance and becoming one of Canada's leading employers."*

These are measured investments that do not require significant capital but allow us to gain better visibility before more resources are added and at the same time, win new international assignments.

A good example is the project we were awarded in 2005 to provide Eco-Chill all-weather snow-making equipment to an indoor ski dome in Busan, South Korea. Scheduled to open in 2006, it is larger than our first indoor ski installation, the Qiaobo Ice and Snow World in Beijing which opened in the summer of 2005. With the growing popularity of skiing in southeast Asia, we believe there are many more opportunities for Eco-Chill.

Another example is the equipment TESI is providing for a gas plant in Slovakia. Valued at $6 million, this custom-built process system will treat natural gas as it enters and exits an underground storage cavern. Since gas often picks up water and hydrocarbons while in storage, it must be treated prior to distribution. In 2005, we also built a number of shipboard gas compression systems to be used by our customers in the South China Sea, and off the coasts of Africa and Brazil. These systems are configured to work in rolling and pitching seas and meet special marine requirements. TESI also had good success by using its expertise to serve coal-bed methane fields in Australia. These are just a few examples of more than 500 projects TESI completed in the past year.

## GOING TO GREAT LENGTHS IN NORTH AMERICA

Just because a project is closer to home does not make it any less challenging. We are regularly called on to use our expertise to serve customer needs in our own backyard.

Maintaining equipment in a remote northern Canadian mine is a case in point. In these situations, the stakes are high. Our customers operate 24/7, 365 days a year and if equipment is down, it can mean millions of dollars in lost production. Unlike southern installations, customers cannot call for instant delivery of consumables – parts or oil – because roads do not exist and sea ports can be iced in for months. Working closely with customers, we use our logistics know-how to ensure that suffi-

**CIMCO REFRIGERATION**

**Steve McLeod,** President, CIMCO Refrigeration

*"Prospects are strong across our markets. We have more resources than ever to secure new business. To differentiate the CIMCO brand and enhance performance, we continue to focus on technology and innovation to deliver our promise of* Expect the Best."

**BATTLEFIELD**

**Randy Casson,** President, Battlefield – The CAT Rental Store

*"We're focused on continuous improvement and committed to customer-driven solutions that add market share. Our mission includes strategic growth in store locations, improved business processes and logistics, enhanced employee engagement and continuous improvement in utilization of our asset base."*

cient consumables are on site to last a full winter. We carefully prepare for overhauls so that we can ship remanufactured components in preparation for on-site equipment exchange and return the replaced components within one very short shipping season.

In recent years, we have stationed our own technicians full-time at mine sites to ensure the fastest response possible. Since underground mining equipment stays underground, our mine mechanics are called upon to work thousands of feet below the surface.

Mining is growing rapidly based on strong commodity prices. We are well positioned with special expertise and Caterpillar mining equipment, which meets industry-leading durability requirements and the tough emission standards of underground applications. We are also a recognized distributor of customized mining equipment for low profile underground applications.

Our technical and logistics support services, including our kidney loop technology (see page 17) and our extensive power and equipment offerings were all cited as reasons we are serving Canada's newest diamond mine, which is expected to open in 2008 in northern Ontario.

Similar everyday challenges are faced and met in other jurisdictions in North America. Our Compression equipment works flawlessly in northern Alberta where temperatures can fall to -50 Celsius. That is why we continue to win assignments such as providing five specialized compression units, with total output of 25,000 horsepower, that were installed in 2005 to inject or withdraw natural gas from an underground storage reservoir in western Canada.

Going to great lengths in North America to serve customers contributes profitable revenue growth. When that revenue growth occurs across all of North America, as it has in each of the last eight years, it furthers revenue diversification.

TESI has made great strides in U.S. gas compression and expects to become a force in this market. CIMCO also has exciting U.S. projects on the books for 2006 including the supply of ice rink technology at a practice facility that will be used by the New Jersey Devils and an NHL-style facility in Kansas City. These orders, as well as a four-pad ice rink installation in Oshawa awarded by Maple Leaf Sports and Entertainment, are all testimony to the value of being the preferred ice rink equipment supplier to the National Hockey League.

## DISTANCE IS NO OBJECT

Whether our customers are near or far, we strive to deliver consistent quality and responsive service. This commitment to achieve the highest standards requires us to invest in service and support resources, but these are calibrated to pay off quickly in the form of satisfied customers, a solid reputation in our markets and attractive service revenue.

# THINKING FORWARD

As our customers grow, we anticipate their needs and innovate our products and processes to match. From 'kidney loop' to 'Eco-Chill,' our creative response to market change continues to differentiate us from the competition.


facing **Working with customers on innovative solutions.**
top **Satellite tracking and laser guidance systems boost customer productivity.**
bottom **A mobile lube truck in our growing fleet.**

Toromont is a breeding ground of new ideas. Staying close to our markets allows us to discover many new product and service opportunities. These arise regularly because of growth in customer activity, technological advancements, and the implementation of new legislation. Partners are also a prime source of ingenious new products and services.

Before we act on a new idea, however, it must: add value to customers, generate a superior return on investment and differentiate Toromont while complementing our business model.

Kidney loop technology is an example. In 2005, we were the only Caterpillar dealer that had lubrication trucks equipped with on-board kidney loop systems. This Toromont first is not only a source of pride, the business case for the technology is outstanding. Using sophisticated filtration, kidney loop removes contaminants in oil as small as 1 micron. By cleansing oil to this exacting standard before it is added to drive trains and hydraulics, and then recycling the oil through the loop system after it has been used, we not only reduce wear, we lengthen the period (measured by machine hours) before an overhaul is required, in some cases by 30%.

Originally, we installed kidney loop technology in our Toromont CAT branches, but determined that it was best placed in the field. We made the technology mobile and added seven lubrication trucks with this capability to our fleet in 2005. We will add more in 2006.

**AERO TECH MANUFACTURING**

**Tim Riley,** President, Aero Tech Manufacturing Inc.

*"Our goal is to add sustainable and profitable custom manufacturing work that utilizes our metal fabrication and electro/mechanical capabilities. Water treatment, medical equipment, radiant ceiling panels and surface cleaning segments figure prominently in our future."*

The benefits are spreading. In 2006, Toromont Energy Systems (TESI) will share in the innovation by employing eight such systems for their field service trucks as part of their strong focus on preventative maintenance for customers. TESI's fleet will be operated by skilled technicians who can perform in-field oil changes (required every 1,000 hours on compression systems), vibration analysis and tune-ups. This capability is a competitive differentiator, and adds value to customers because it allows them to avoid holding lubricating fluids in inventory and disposing of waste fluids.

## THE MOTHER OF INVENTION

Sometimes necessity is the mother of invention. In recent years, TESI has experienced unprecedented demand for compression. This is a challenge because each compression package requires a degree of customization and often must be delivered within weeks to meet customer requirements. The solution was to standardize common components, and then pre-build compression packages based on sales and customer forecasts. The benefit of this approach is that we can commit to deliver small and large horsepower compression systems much faster, with all engineered options included.

A substantial increase in Customer Service Agreements (CSAs) within Toromont CAT also necessitated an innovative approach. To manage the delivery of service, we created the Toromont CAT Customer Support Centre. Using proprietary technology, this centre co-ordinates scheduled maintenance dealership-wide and provides telephone assistance to support electronic service offerings, from our on-line *PartStore* to *Product Link*.

*Product Link* is a satellite-powered tracking system installed on all Toromont CAT equipment covered by CSAs. Customers use it to track their equipment location and utilization. Also our Customer Support Centre uses it to alert our branches of real-time service issues and to proactively schedule maintenance based on actual equipment usage.

For Aero Tech Manufacturing, our custom fabricator in Salt Lake, Utah, innovation is a business mainstay made necessary by intensely competitive markets. Rather than relying solely on contract manufacturing for customers, it has used its knowledge and capabilities to create its own brand of surface cleaning trucks. These specialty vehicles serve the needs of the North American carpet cleaning industry. Along with a line of radiant ceiling panels, these proprietary products give Aero Tech additional revenue streams.

## E-BUSINESS

Technology allows us to manage growth. In 2006, TESI will implement iMACS, a manufacturing and planning system that will improve estimating, purchasing and project execution. It will give us visibility at every critical step in the project chain.

For a business that received requests for some 3,000 customer quotations last year alone, iMACS is a must. It was developed internally based on extensive interaction between TESI and our dedicated IT professionals who are the chief architects of business innovation at Toromont.


Another example of an internally-designed e-business tool is our new asset tracking system rolling out at Battlefield – The CAT Rental Store. This bar code-based system will substantially increase our insight into the location and utilization of Battlefield's extensive fleet of rental equipment, thereby increasing responsiveness to customer rental requests. We estimate the new system will improve efficiencies 10%. It also automates the entire rental transaction, thereby reducing costs.

top **Eco-Chill provides energy efficiency and environmental conservation.**
bottom **CCS powers a truck cab without engine idling.**

## TOROMONT FIRSTS

Eco-Chill is a Toromont first. Developed by the engineers at CIMCO, this patent-pending technology collects and recycles the energy used to maintain the ice surface, providing abundant heating for the building and hot water for showers, under-floor heating, ice resurfacing and snow melting. Utilizing all natural refrigerants and thermal energy storage, Eco-Chill also satisfies air conditioning needs while cutting greenhouse gas emissions. It gives our customers access to funding programs targeted at achieving the goals of the Kyoto protocol. Since developing this unique technology, we have already sold 26 systems. More opportunities lie ahead.

CCS Lightning Cab Comfort System is another Toromont first. Using knowledge gained in building auxiliary power units for military applications, CCS was developed to help on-highway truck owners comply with anti-idling legislation. CCS is a discrete power unit that consumes just 21 inches of frame rail space and supplies 6 kilowatts of power that can be used for heating, air conditioning or onboard electronics. We believe the opportunity for CCS is substantial and we are adding OEM and aftermarket partners to expand availability.

## PARTNERS IN PERFORMANCE

Leveraging the inventions of our partners is another reason Toromont works. Caterpillar, a powerhouse of innovation, is well ahead of the curve on 2007 emission standards for on-highway trucks due to developments with the revolutionary ACERT engine.

There's also our new relationship with Trimble, a global leader in laser and GPS-powered control equipment. Toromont CAT became a Trimble dealer in 2005 because their technology directly complements Caterpillar equipment. With Trimble's new GPS and laser-guided Grade Control Systems, we dramatically improve customer productivity and profitability by eliminating the need for repeat grading and physical surveying. Customers report cost savings as high as 30%.

These and many other innovations make Toromont work.

# MANAGEMENT'S DISCUSSION AND ANALYSIS

of Financial Results for the year ended December 31, 2005

Management's Discussion and Analysis, or "MD&A", for Toromont Industries Ltd. ("Toromont" or the "Company") should be read in conjunction with the consolidated financial statements, management's report and auditors' report included in this Annual Report. The consolidated financial statements reported herein have been prepared in accordance with Canadian generally accepted accounting principles ("GAAP") and are reported in Canadian dollars. The information in this MD&A is current to February 14, 2006. Additional information, including the Annual Information Form, is available on SEDAR at www.Sedar.com and on the Company's website at www.Toromont.com.

## ADVISORY

Certain statements contained herein constitute "forward-looking statements". Words such as "plans", "intends", "outlook", "expects", "anticipates", "estimates", "believes", "should" and similar expressions are intended to identify forward-looking statements. Forward-looking statements are based on current expectations and are influenced by management's historical experience, perception of trends and current business conditions, expected future developments and other factors which management considers appropriate. These statements entail various risks and uncertainties as more fully described in the "Risks and Uncertainties" and the "Outlook" sections of this MD&A. These risks and uncertainties could cause or contribute to actual results that are materially different from those expressed or implied. The Company disclaims any obligation or intention to update or revise any forward-looking statement, whether the result of new information, future events or otherwise.

## RESPONSIBILITY OF MANAGEMENT AND THE BOARD OF DIRECTORS

Management is responsible for the information disclosed in this MD&A and the accompanying consolidated financial statements, and has in place appropriate information systems, procedures and controls to ensure that information used internally by management and disclosed externally is materially complete and reliable. In addition, the Company's Audit Committee, on behalf of the Board of Directors, provides an oversight role with respect to all public financial disclosures made by the Company, and has reviewed and approved this MD&A and the accompanying consolidated financial statements.

The Chief Executive Officer and the Chief Financial Officer have evaluated the effectiveness of the Company's disclosure controls and procedures as of December 31, 2005 and have concluded that the Company's disclosure controls and procedures provide reasonable assurance that material information relating to the Company, including its consolidated subsidiaries, would be made known to them by others within those entities, particularly during the period in which this report was being prepared.

## CORPORATE PROFILE AND BUSINESS SEGMENTATION

Toromont Industries Ltd. is a leading provider of specialized capital equipment and comprehensive product support to a number of diverse markets. Toromont employs approximately 4,400 people in more than 115 locations. While Canada is the primary source of revenues, the Company has a solid presence in the United States and offshore markets are of growing significance. Major customers participate in a broad range of industries including construction, infrastructure, aggregates, steel, waste management, equipment rentals, agriculture, forestry and mining, oil and gas, petrochemicals, food and beverage processing, cold storage, recreation and co-generation.

The Equipment Group is engaged in selling, renting and servicing a broad range of construction equipment and industrial engines. The Equipment Group generated 57% of the Company's revenues in 2005 from one of the world's largest Caterpillar dealerships by revenue and geographic territory and from industry-leading rental operations. Performance in this business segment results from activity relating to the residential and commercial construction, infrastructure projects, road building, aggregates, waste management, steel, forestry, mining and agriculture industries. Other significant activities of the Equipment Group include sales and product support activities for Caterpillar engines used in a variety of applications including on-highway trucks, industrial, commercial, marine and power generation applications.

The Compression Group is a leading North American business specializing in the design, engineering, fabrication and installation of compression systems for natural gas, fuel gas and carbon dioxide in addition to process systems and industrial and recreational refrigeration systems. These activities, which all involve the compression of gases, generated 43% of the Company's revenues in 2005. Results in the Compression Group are influenced by conditions in the primary market segments served, spanning the chemical, petrochemical, natural gas and co-generation industries in addition to industrial markets including food and beverage processing, cold storage, food distribution and ice rink construction.

## PRIMARY OBJECTIVE AND MAJOR STRATEGIES

A primary objective is to build shareholder value through sustainable and profitable growth, founded on a strong financial position. Toromont's operating groups employ the following broad strategies in pursuit of this objective:

### Expanding Markets

Toromont serves a diverse and increasing number of markets that offer significant potential for profitable expansion. Each operating group strives to achieve or maintain leading positions in served markets. Incremental revenues are derived from geographic expansion, improved coverage and market share gains. Expansion of the installed base of equipment provides the foundation for future product support growth and leverages the fixed costs associated with the Company's infrastructure.

### Strengthening Product Support

The parts and service business is a significant contributor to overall profitability and serves to stabilize results through economic downturns. Product support activities also represent opportunities to develop closer relationships with customers and differentiate our product and service offering. The ability to consistently meet or exceed customers' expectations for service efficiency and quality is critical, as after market support is an integral part of the customer's decision-making process when purchasing equipment.

### Broadening Product Offerings

Toromont delivers specialized capital equipment to a diverse range of customers and industries. Collectively, we offer thousands of different parts through our distribution channels. The Company expands its customer base through selectively extending product lines and capabilities. In support of this strategy, Toromont represents product lines that are considered leading, if not best in class offerings from suppliers that are continually expanding and complementing their products. Strong relationships with suppliers are critical in achieving growth objectives.

### Investing in Our Resources

People are our most valuable resource. The combined knowledge and experience of management and staff is a key competitive advantage. Our growth is dependent on attracting, retaining and developing employees with values that are consistent with Toromont's. Incentive programs, a strong share ownership and highly principled culture result in a close alignment with Company and shareholder interests. By investing in employee training and development, the capabilities and productivity of employees continually improve to better serve customers, business partners and shareholders.

Toromont's information technology represents another competitive differentiator in the marketplace. We make selective investments in technology, inclusive of e-commerce initiatives, to strengthen customer service capabilities, generate new opportunities for growth, drive efficiency and increase returns to our shareholders.

### Strong Financial Position

A strong, well-capitalized balance sheet creates financial flexibility, has contributed to the Company's long-term track record of profitable growth and is fundamental to the Company's future success.

## KEY PERFORMANCE MEASURES

The Company continuously reviews and monitors its activities and the performance indicators it believes are critical to measuring success. Some of the key financial performance measures are summarized in the following table. Others include, but are not limited to, measures such as market share, fleet utilization, and customer and employee satisfaction.

| Years ended December 31 | 2005 | 2004 | 2003 | 2002 | 2001 |
|---|---|---|---|---|---|
| **Expanding Markets and Broadening Product Offerings** | | | | | |
| Revenue growth (1) | 11.5% | 14.9% | 20.6% | 16.1% | 11.3% |
| Revenue generated internationally ($ millions) | $ 70.0 | $ 79.0 | $ 55.4 | $ 22.5 | $ 16.1 |
| Revenues – Equipment Group to Compression Group | 57:43 | 57:43 | 63:37 | 69:31 | 68:32 |
| **Strengthening Product Support** | | | | | |
| Product support revenue growth | 15.8% | 10.7% | 12.1% | 14.7% | 22.6% |
| **Investing in Our Resources** | | | | | |
| Revenue per employee ($ thousands) | $ 384 | $ 381 | $ 373 | $ 359 | $ 345 |
| Investment in information technology ($ millions) | $ 13.2 | $ 11.7 | $ 11.2 | $ 8.8 | $ 8.0 |
| **Strong Financial Position** | | | | | |
| Working capital ($ thousands) | $ 411 | $ 263 | $ 204 | $ 213 | $ 218 |
| Net debt to equity ratio | .42:1 | .45:1 | .47:1 | .41:1 | .48:1 |
| Book value per share | $ 7.57 | $ 6.59 | $ 5.93 | $ 5.28 | $ 4.90 |
| **Build Shareholder Value** | | | | | |
| Basic earnings per common share growth (1) | 12.6% | 19.4% | 47.6% | 16.7% | (3.6%) |
| Dividends per common share growth | 23.1% | 23.8% | 16.7% | 5.9% | 6.3% |
| Return on opening shareholders' equity | 18.9% | 18.7% | 17.5% | 12.9% | 17.1% |

(1) Excluding gain on sale of investments in 2001

The performance measures indicate successful execution of our strategies. Revenues have increased at an average annual rate of 15% since 2001. Product support revenues have also increased at an average annual growth rate of 15% over the same period. Over the past two years, revenue and product support growth has been adversely impacted by the strengthening Canadian dollar which has resulted in lower selling prices. We estimate the impact on our revenues was approximately $83 million or 5% of revenues in 2005. However, given that there is a corresponding impact on cost of goods sold, margins have not been negatively affected. Exchange affects our product support revenues as the Company imports many of its parts from the United States. We estimate that the impact of exchange movement on our product support revenues was approximately $20 million or 5% of product support revenues in 2005. Additionally, revenue growth in 2004 and 2005 has been affected by supply constraints on certain equipment, resulting in some delays in deliveries to customers.

Significant investments have been made in the area of information technology over the past five years. These investments have provided a competitive advantage in the marketplace and increase productivity levels. Revenue per employee has increased 11.6% since 2001.

Toromont continues to maintain a strong balance sheet. In 2005, working capital and book value per share both increased over prior year levels. The Company's leverage, as represented by its net debt to equity ratio, was also improved over the prior year. Earnings per share increased in each year since 2002. Book value per share increased in each of the past five years.

## CHANGE IN ACCOUNTING POLICY

Toromont generates a significant portion of its revenue from assembly or manufacturing of customer-specified equipment packages. These projects, typically in the Compression Group, include the supply of natural gas compression packages, industrial or recreational refrigeration packages and components used in the processing of hydrocarbons.

In the fourth quarter of 2005, the Company adopted the percentage-of-completion approach of accounting for performance of production-type contracts. The consideration of this change was triggered due to the growing contribution of projects in the Compression Group to the Company's overall performance. In the past, the completed contract method was used as revenues and earnings determined under that approach were consistent with those that would have been calculated using the percentage-of-completion method. Under the new method, revenues and cost of goods sold are recognized in income at each period end, based on the total costs incurred to period end as a percentage of expected total costs of the project. Revenues and costs are not recognized until progress reaches a stage of completion sufficient to reasonably determine the probable results. Any foreseeable losses on projects are charged to income at the time they become evident. This method of revenue recognition matches revenues and cost of goods sold to the period in which the projects occurred and promotes a clearer understanding of the underlying activities of the Company.

Results for each of the first three quarters of the year ended December 31, 2005 have been restated to reflect the percentage-of-completion method of revenue recognition. The impact of the restatements made to the reported quarterly results for 2005 are summarized in the following table.

| ($ thousands except per share amounts) | Q1 2005 (1) | | Q2 2005 (1) | | Q3 2005 (1) | | Q4 2005 (2) | |
|---|---|---|---|---|---|---|---|---|
| | Reported | Restated | Reported | Restated | Reported | Restated | Pro-forma | Reported |
| Revenues | $ 301,111 | $ 306,289 | $ 390,034 | $ 390,127 | $ 422,952 | $ 427,888 | $ 451,399 | $ 475,488 |
| Net income | $ 7,388 | $ 8,177 | $ 18,410 | $ 18,804 | $ 24,191 | $ 24,685 | $ 24,055 | $ 27,296 |
| EPS – basic | $ 0.12 | $ 0.13 | $ 0.29 | $ 0.30 | $ 0.38 | $ 0.39 | $ 0.38 | $ 0.43 |

(1) For Q1, Q2 and Q3, the "Reported" column portrays the results as reported in the unaudited interim financial statements, with the relevant revenues recognized using the completed contract approach. The "Restated" column reflects those revenues restated to conform with the percentage-of-completion method.

(2) For Q4, the "Pro-forma" column portrays the results as they would have been utilizing the completed contract approach. The "Reported" column shows the results determined by the application of the percentage-of-completion method of revenue recognition.

As a result of the adoption of this policy, the Company has adjusted retained earnings as at January 1, 2005 to reflect the percentage of completion of work in progress at December 31, 2004. Periods prior to January 1, 2005 have not been restated. The components of this adjustment are summarized in the following table. The adjustment is attributable to the Compression Group; there is no impact on reported results for the Equipment Group.

| ($ thousands) | |
|---|---|
| Revenues | $ 22,493 |
| Cost of goods sold | 19,860 |
| Income taxes | 937 |
| Increase to retained earnings at January 1, 2005 | $ 1,696 |

Had this change in accounting policy not occurred, revenue recognized in the year would have been reduced by $34.3 million, cost of goods sold would have been reduced by $26.7 million and income taxes would have been reduced by $2.7 million, resulting in a decrease in net income of $4.9 million.

## BUSINESS DISPOSITION

Effective August 31, 2005, the assets of the Ontario Sterling Division were sold. Ontario Sterling was a Sterling Truck franchise in the Greater Toronto Area selling and servicing medium and heavy duty Class 5 to Class 8 trucks. It was determined that this business was not core to the growth of the Company and that it was not generating returns commensurate with expectations. Total proceeds on sale were $18.9 million consisting of $17.7 million for working capital and $1.2 million for other, including capital assets. The after-tax gain on the sale of these operations was $745,000 (one cent per share). The Ontario Sterling operations, previously included with those of the Equipment Group, accounted for approximately 3% of annual consolidated revenues. The accompanying consolidated financial statements have been restated to reflect Ontario Sterling as a discontinued operation. This MD&A has been prepared on a continuing operations basis.

## IMPAIRMENT OF LONG-LIVED ASSETS

During the period of 1998 to 2001, Toromont built five power generation facilities, with the anticipation that the then provincial government would deliver on its promise of deregulation of the electricity supply market. Unfortunately, two factors coincided to adversely affect the profitability of these ventures. First, the promise of deregulation was not delivered, thereby capping the rates derived from the supply of electricity. Second, significant increases in the price of natural gas have increased the cost of supply.

Toromont recently signed a Letter of Intent for a five-year agreement with the Ontario Power Authority. Based on the terms of this agreement, the Company has concluded that the revenues generated will not be sufficient to cover the fixed operating costs and depreciation of the assets. The Company has recorded a pre-tax charge of $17.8 million to reflect impairment of these long-lived assets. After recording this charge, the net book value of the Company's power generation assets has been reduced to $14.9 million.

## CONSOLIDATED RESULTS OF OPERATIONS

| ($ thousands except per share amounts) | 2005 | 2004 | % change |
|---|---|---|---|
| **Revenues** | $ 1,599,792 | $ 1,434,756 | 12% |
| Cost of goods sold | 1,250,714 | 1,130,516 | 11% |
| Gross profit | 349,078 | 304,240 | 15% |
| Selling and administrative expenses | 211,899 | 184,883 | 15% |
| Asset impairment charge | 17,800 | – | n/m |
| **Operating income** | 119,379 | 119,357 | – |
| Interest expense | 12,977 | 12,138 | 7% |
| Interest and investment income | (2,785) | (1,936) | 44% |
| Income before income taxes | 109,187 | 109,155 | – |
| Income taxes | 30,795 | 39,015 | (21%) |
| **Earnings from continuing operations** | 78,392 | 70,140 | 12% |
| Gain on disposal of discontinued operations | 745 | – | n/m |
| Earnings (loss) from discontinued operations | (175) | 378 | n/m |
| **Net earnings** | $ 78,962 | $ 70,518 | 12% |
| **Earnings per share – basic** | $ 1.25 | $ 1.11 | 13% |

Year-over-year growth in both operating groups led revenue to increase 12% to $1.6 billion in the year. Compression Group package revenues were higher on increased natural gas and coal-bed methane compression activity. Equipment Group revenues were higher on increased new and used machine sales and brisk rental activity. Product support continued to improve, with double-digit increases in both Groups. The strengthening of the Canadian dollar relative to the U.S. currency, increasing 7.5%, reduced reported revenues year-over-year by an estimated $83 million.

Gross profit increased 15% on higher sales volumes and improved margins. Gross profit margin was 21.8%, up from 21.2% last year largely on improvements in the Equipment Group and an increased mix of product support business, which generates a higher margin.

Selling and administrative expenses increased $27.0 million or 15% in the year, principally due to compensation increases initiated at the beginning of the year and higher sales activity. Salaries and benefits were up $13.0 million in the year, reflecting aforementioned compensation adjustments and increased headcount. Profit-sharing was also higher by $2.4 million in the year as a result of the improved earnings. Additional expenses at companies acquired in late 2004 amounted to $3.0 million. Other expense increases included sales-related expenses, up $3.5 million, occupancy costs, up $1.4 million, and information technology, up $1.9 million. Selling and administrative expenses as a percentage of revenue were 13.2% for the year compared to 12.9% in 2004.

Operating income included a $17.8 million pre-tax charge related to the impairment of Toromont's long-lived power generation assets, previously discussed. As a result of this charge, operating income was unchanged for the year versus 2004. Excluding the asset impairment charge, operating income was up 15% for the year over last, on higher sales and margins, offset by higher relative expense levels. Operating margin, excluding asset impairment charges, was 8.6%, up 0.3% from the prior year on improved gross margins in the Equipment Group, partially offset by weaker results from the industrial and recreational refrigeration operations.

Interest expense increased $0.8 million or 7%, for the year due to higher average debt balances carried to fund investments in working capital. Interest income varies due to timing of rental conversions and level of short-term investing of daily cash flows from operations.

The effective income tax rate for the year ended December 31, 2005 was 28.2% compared to 35.7% for the year ended December 31, 2004. The reduction in the effective tax rate was principally due to an $8.7 million reduction of the Company's tax reserves following a comprehensive review of current items. This review was triggered by the successful closure of several outstanding matters including the completion by federal, provincial and state taxing authorities of their review of filings for the three successive tax years up to and including the period ended December 31, 2002.

## BUSINESS SEGMENT OPERATING RESULTS

The accounting policies of the segments are the same as those of the consolidated entity. Management evaluates overall business segment performance based on top line revenue growth and operating income (earnings before interest expense, interest and investment income and income taxes) relative to revenues. Corporate expenses are allocated based on each segment's operating income. Interest expense and interest and investment income are not allocated.

## RESULTS OF OPERATIONS IN THE EQUIPMENT GROUP

| Years ended December 31 ($ thousands) | 2005 | 2004 | % change |
|---|---|---|---|
| Equipment sales and rentals | | | |
| New | $ 389,787 | $ 358,631 | 9% |
| Used | 123,531 | 117,969 | 5% |
| Rental | 126,250 | 106,178 | 19% |
| Total equipment sales and rentals | 639,568 | 582,778 | 10% |
| Power generation | 14,723 | 11,175 | 32% |
| Product support | 259,654 | 227,086 | 14% |
| Total revenues | $ 913,945 | $ 821,039 | 11% |
| Operating income | $ 62,796 | $ 65,842 | (5%) |
| % of revenues | 6.9% | 8.0% | |
| Capital expenditures | $ 65,312 | $ 52,349 | 25% |

The Equipment Group delivered record revenues for the year with strong growth across all segments of the business. Excluding the impairment charge on power generation assets discussed previously in this MD&A, operating income also reached record levels with a year-over-year increase of 22%.

New machine sales were up 9% in the year on higher unit tractor sales. Growth was seen across several market segments, most notably heavy and general construction.

Used equipment sales were up 5% in the year. Sales of used equipment vary depending on customer buying preferences, exchange rate considerations and product availability. Used equipment inventories were 6% higher than at this time last year, primarily due to higher trade-in activity.

Rental revenues were up 19% in the year on improved utilization, one new location and the late 2004 acquisition of Access Rentals in Sudbury, Ontario. Same store activity was 15% higher this year compared to the prior year.

Power generation revenues from Toromont-owned plants increased $3.5 million, 32%, in the year on increased operating hours, higher average electricity prices and strong summer demand. Prior to recording the charge for asset impairment, the increased revenues were not sufficient to cover the fixed operating costs and depreciation of the assets as previously discussed.

Product support revenue continued to benefit from strong customer demand for service, largely from increased construction activity, and the growth in the installed base of Caterpillar equipment. Product support revenues increased 14% in the year, with excellent growth reported in both parts and service.

Operating income decreased 5% in the year as a result of the $17.8 million asset impairment charge. Excluding this charge, operating income increased 22% in the year on higher volumes and gross margins. Net of this charge, operating income increased to 8.8% of revenues for the year compared with 8.0% in 2004. This represents a record level of profitability for the Equipment Group and was attributable to business mix and some improvement in gross margins on machine sales.

Although overall deliveries have improved somewhat from this time last year, the supply of new equipment models remains on managed distribution. Booking activity was strong in the year, considering the impact of the stronger Canadian dollar. Backlogs entering 2006 were at record levels.

Capital expenditures within the Equipment Group increased $13.0 million in 2005. Capital expenditures included investments in new branch openings and expansions as well as significant additions to the rental fleet. Capital expenditures for 2006 are expected to be comparable to 2005.

## RESULTS OF OPERATIONS IN THE COMPRESSION GROUP

| Years ended December 31 ($ thousands) | 2005 | 2004 | % change |
|---|---|---|---|
| Equipment package sales and rentals | $ 538,357 | $ 489,178 | 10% |
| Product support | 147,490 | 124,539 | 18% |
| Total revenues | $ 685,847 | $ 613,717 | 12% |
| Operating income | $ 56,583 | $ 53,515 | 6% |
| % of revenues | 8.3% | 8.7% | |
| Capital expenditures | $ 7,501 | $ 13,259 | (43%) |

The Compression Group reported record results due to significant activity in the natural gas and coal-bed methane compression markets and strong product support revenues. Growth was partially offset by weaker than expected project activity in the industrial and recreational refrigeration business.

Package revenues were up 10% in the year. The process business continues to benefit from increased market activity, as evidenced by record bookings and backlogs. Momentum within the natural gas/coal-bed methane compression market continued, with bookings up substantially and backlogs up threefold from this time last year.

Product support revenues were up 18% in the year, with solid increases in both the process and industrial categories. Industrial product support revenues have benefited from the 2004 acquisition of Alabama-based Engineering Refrigeration Systems. Increased natural gas compression activity and the growing installed base have strengthened the product support business at Toromont Energy Systems.

Operating income for the Compression Group increased 6% in the year on increased gas compression activity partially offset by declines in industrial and recreational refrigeration. At Toromont Energy Systems, operating income increased 19% for the year on higher package sales and product support, coupled with lower relative expenses.

At CIMCO, operating income decreased 72% for the year as higher revenues on product support were offset by lower package sales due to project delays. Operating income was also negatively impacted by increased operating expenses, notably travel, relocation and consulting costs related to international expansion.

Subsequent to year-end, the Company purchased land, plant and equipment in Casper, Wyoming for $5.5 million. The newly acquired assets include 40,000 sq. ft. of production capacity and will provide a basis for further expansion of Toromont's gas compression fabrication and support services into the northwestern U.S. market.

Capital expenditures of $7.5 million were lower than the prior year. Expenditures in 2004 included the investment in a new manufacturing facility.

## CONSOLIDATED FINANCIAL CONDITION

The Company has maintained a strong financial position. Net debt to equity at December 31, 2005 was 0.42:1 compared to 0.45:1 in the prior year. Total assets were $1.1 billion at December 31, 2005 compared with $1.0 billion at the end of 2004. Working capital increased to $411.0 million principally on higher cash balances and paid for inventories.

### Outstanding Share Data

As at the date of this MD&A, the Company had 63,632,936 common shares outstanding.

### Dividends

Toromont's practice is to maintain a quarterly dividend on its outstanding common shares that annualized, approximates 30% of the prior year's net earnings, giving consideration to earnings prospects, financial requirements and general economic circumstances. The Board of Directors and management review the dividend payout ratio on an ongoing basis. During 2005, dividends of 32 cents per common share were declared, representing 29% of 2004 net earnings per share. Subsequent to year-end, the Board declared a quarterly dividend of 10 cents per common share, an increase of 25%, payable April 3, 2006.

## LIQUIDITY AND CAPITAL RESOURCES

### Sources of Liquidity

Toromont obtains short-term financing through a combination of cash from operating activities and committed long-term credit facilities. Combined unsecured credit facilities amounted to $231 million at year-end, of which $191 million was unutilized.

The Company obtains long-term financing through a variety of senior debentures and notes payable. At December 31, 2005, $206.2 million in term debt carried interest at fixed rates, at a weighted average rate of 5.82%, with varying maturities through to 2019, and $17.9 million carried interest at variable rates, averaging 2.21%, with maturities through 2008.

### Principal Components of Cash Flow

| Years ended December 31 ($ thousands) | 2005 | 2004 | % change |
|---|---|---|---|
| Cash provided by operating activities | $ 24,614 | $ 60,309 | (59%) |
| Cash used in investing activities | (25,123) | (38,937) | 35% |
| Cash provided by (used in) financing activities | 51,225 | (21,372) | n/m |
| Total increase in cash | $ 50,716 | $ – | n/m |

### Cash Flows from Operating Activities

Operating activities provided $24.6 million compared to $60.3 million last year. While cash flow from operating activities before changes in working capital was up $16.0 million, 15%, this was mostly offset by higher non-cash working capital, primarily due to increased inventories and higher accounts receivable on increased sales.

Accounts receivable of $337.4 million at December 31, 2005 were higher than last year on higher revenues. Days sales outstanding are at the same level as this time last year.

Inventories were $379.8 million at the end of the year, higher than at December 2004 on increases in both Groups. The Equipment Group machine inventory at year-end, while down from record levels reported earlier in the year, increased in anticipation of continued allocation in supply of some high demand products. Product support growth resulted in a 16% increase year-over-year in both parts inventories and work-in-process. In Compression, inventories increased as a result of additional stock units held due to heightened market activity and accelerated purchasing to secure supply on certain major components. We anticipate a continued requirement to carry higher inventory levels across our businesses until there is an easing of prime product supply constraints.

The Company expects that continued cash flows from operations in 2006, together with currently available credit facilities, will be more than sufficient to fund its requirements, including working capital, dividends, capital investments and other uses of cash.

### Cash Flows from Investing Activities

Cash flows from investing activities in 2005 included proceeds of $18.9 million received on sale of Ontario Sterling. The prior year's investing activities included the acquisition of two businesses for a total of $6.8 million. Excluding these two items, cash used in investing activities was comparable year-over-year. To support and generate growth in this area of the business, net additions to rental fleet were $13.5 million higher in 2005. Property, plant and equipment additions of $20.5 million included additions to the service vehicle fleet of $6.5 million, facility renovations of $5.2 million, computer technology upgrades for $4.5 million and land purchased for a new Battlefield – The CAT Rental Store facility in Barrie, Ontario for $1.0 million.

Spending in property, plant and equipment will continue as new branches are opened and current branches remodelled. Investments in rental fleet are expected to continue at the current pace given current market conditions. There will be no new spending in power generation assets in light of current market conditions.

### Cash Flows from Financing Activities

Financing activities provided $51.2 million in the year as the issuance of $125 million in senior debentures exceeded cash required for other financing activities. Principal repayments of $31.0 million were made during the year on senior debentures and other notes payable. Dividends of $20.3 million were paid in 2005, 23% higher than the prior year, reflecting the increase in the dividend rate per share. No shares were purchased under the normal course issuer bid in 2005. In 2004, the Company purchased and cancelled 1,054,300 shares for $19.5 million at an average price of $18.46 per share.

The issuer bid was renewed effective August 31, 2005, allowing the Company to purchase up to 3,167,284 of its common shares during the 12-month period commencing at that date.

## OUTLOOK

The Equipment Group reported another year of record results. Demand remains strong across most markets. Continued growth in the Canadian economy is expected to benefit our key markets.

Market conditions and commodity prices are expected to continue to support the current activity level in our Compression Group. The new fiscal year started with a healthy backlog. Subject to continued robust bookings, another strong year is expected.

The product support businesses in both operating groups have experienced excellent growth through 2005 and we should continue to benefit from increased market activity and the larger machine population across all of our businesses.

Overall, we are relatively positive that 2006 should be another successful year.

## FOURTH QUARTER 2005

| Three months ended December 31 ($ thousands, except share amounts) | 2005 (2) | 2004 | % change |
|---|---|---|---|
| **Revenues** | $ 475,488 | $ 403,260 | 18% |
| Cost of goods sold | 365,829 | 314,597 | 16% |
| Gross profit | 109,659 | 88,663 | 24% |
| Selling and administrative expenses | 59,818 | 46,104 | 30% |
| Asset impairment charge | 17,800 | – | n/m |
| **Operating income** | 32,041 | 42,559 | (25%) |
| Interest expense | 4,030 | 3,032 | 33% |
| Interest and investment income | (1,443) | (735) | 96% |
| Income before income taxes | 29,454 | 40,262 | (27%) |
| Income taxes | 2,158 | 13,770 | (84%) |
| **Earnings from continuing operations** | 27,296 | 26,492 | 3% |
| Earnings from discontinued operations (1) | – | 262 | n/m |
| **Net earnings** | $ 27,296 | $ 26,754 | 2% |
| **Earnings per share – basic** | $ 0.43 | $ 0.42 | 2% |

(1) The assets of Ontario Sterling were sold for $18.9 million effective August 31, 2005, and an after tax gain of $745,000 (one cent per share) was included in third quarter results. The results summarized have been restated to reflect Ontario Sterling as a discontinued operation. This discussion and analysis has been prepared on a continuing operations basis.

(2) The Company changed its revenue recognition policy in the fourth quarter of 2005. Financial results for the first three quarters of 2005 have been restated to reflect this change. Periods prior to January 1, 2005 have not been restated.

Both the Equipment and the Compression Groups reported strong operating results in the fourth quarter, with revenue growth of 17% and 19% respectively. Three items, previously discussed, were recorded in the period which reduced reported earnings in the quarter by a net $300,000.

Compression Group package revenues were higher on increased natural gas and coal-bed methane compression activity. Equipment Group revenues were higher on increased new and used machine sales and brisk rental activity. Product support continued to improve, with double-digit increases in both Groups. The strengthening of the Canadian dollar relative to the U.S. currency, adversely impacted reported revenues by an estimated $26 million for the quarter versus the fourth quarter of 2004.

Gross profit increased 24% in the quarter over last year on higher sales volumes and improved margins. Gross profit margin increased 1.1 percentage points to 23.1% in the fourth quarter compared to the same quarter of the prior year on improved margins in the Equipment Group.

Selling and administrative expenses increased $13.7 million or 30% for the quarter versus the comparable period of the prior year, principally due to compensation increases initiated at the beginning of the year and higher sales activity. Salaries and benefits were up $2.5 million in the quarter, reflecting aforementioned compensation adjustments and increased headcount. Profit sharing was also higher by $1.1 million in the quarter as a result of the improved earnings. Additional expenses at companies acquired in late 2004 amounted to $0.6 million in the quarter. Sales related expenses were up $2.0 million in the quarter on higher volumes.

## CONTRACTUAL OBLIGATIONS

Contractual obligations are set out in the following table. Management believes that these obligations will be met comfortably through cash generated from operations and existing short and long-term financing facilities.

| | Payments due by Period | | | | |
|---|---|---|---|---|---|
| ($ thousands) | Total | Less than 1 year | 1 to 3 years | 4 to 5 years | After 5 years |
| Long-Term Debt | $ 254,093 | $ 12,828 | $ 74,605 | $ 22,608 | $ 144,052 |
| Operating Leases | 13,594 | 4,764 | 5,528 | 2,083 | 1,219 |
| Total | $ 267,687 | $ 17,592 | $ 80,133 | $ 24,691 | $ 145,271 |

## SELECTED ANNUAL INFORMATION

| ($ thousands, except per share amounts) | 2005 | 2004 | 2003 |
|---|---|---|---|
| Revenues | $ 1,599,792 | $ 1,434,756 | $ 1,299,389 |
| Net earnings – continuing operations | 78,392 | 70,140 | 58,391 |
| Net earnings | 78,962 | 70,518 | 58,693 |
| Earnings per share – continuing operations | | | |
| Basic | $ 1.24 | $ 1.10 | $ 0.93 |
| Diluted | $ 1.22 | $ 1.08 | $ 0.91 |
| Earnings per share | | | |
| Basic | $ 1.25 | $ 1.11 | $ 0.93 |
| Diluted | $ 1.23 | $ 1.09 | $ 0.91 |
| Dividends per share | $ 0.32 | $ 0.26 | $ 0.21 |
| Total assets | 1,143,972 | 962,437 | 856,176 |
| Total long-term liabilities | 254,093 | 187,047 | 176,990 |

Revenue growth has been strong with year-over-year increases of 21%, 15% and 12% in 2003, 2004 and 2005 respectively. Strong organic growth was achieved in both operating segments on increases in machine and package sales, rental revenues and product support activities. Revenue growth has also been complemented by acquisitions. Toromont Energy Systems, which was acquired effective January 1, 2003, contributed approximately $106 million to revenue in 2003.

Growth in net earnings, on a continuing operations basis, has also been strong, with year-over-year increases of 45%, 17% and 12% in 2003, 2004 and 2005 respectively. Earnings per share have grown in line with earnings growth. Improvements have been the result of higher sales volumes and margins in both operating segments, lower levels of selling and administrative expenses relative to revenues and lower effective income tax rates.

Dividends have been paid consistently over the three-year period noted above with the rate of dividends increasing in line with growth in trailing earnings.

Total assets have increased over the three-year period noted above through acquisitions and investments in capital assets in target markets.

Long-term debt has increased in 2005 and represents 53% of total shareholders' equity. In 2003, long-term debt represented 47% of shareholders' equity. Debt net of cash to shareholders' equity has improved since 2003, and is 42% at December 31, 2005 compared to 47% in 2003.

Shareholders' equity has increased as a result of consistently strong earnings which more than offset dividends and common share repurchases.

## QUARTERLY RESULTS

| ($ thousands, except per share amounts) | Q1 | Q2 | Q3 | Q4 | Year |
|---|---|---|---|---|---|
| **2005** | | | | | |
| Revenues | $ 306,289 | $ 390,127 | $ 427,888 | $ 475,488 | $ 1,599,792 |
| Net earnings – continuing operations | 8,250 | 18,903 | 23,943 | 27,296 | 78,392 |
| Net earnings | 8,177 | 18,804 | 24,685 | 27,296 | 78,962 |
| Earnings per share – continuing operations | | | | | |
| Basic | 0.13 | 0.30 | 0.38 | 0.43 | 1.24 |
| Diluted | 0.13 | 0.29 | 0.37 | 0.43 | 1.22 |
| Earnings per share | | | | | |
| Basic | 0.13 | 0.30 | 0.39 | 0.43 | 1.25 |
| Diluted | 0.13 | 0.29 | 0.38 | 0.43 | 1.23 |
| Dividends per share | 0.080 | 0.080 | 0.080 | 0.080 | 0.320 |
| **2004** | | | | | |
| Revenues | $ 265,187 | $ 398,206 | $ 368,103 | $ 403,260 | $ 1,434,756 |
| Net earnings – continuing operations | 6,528 | 18,573 | 18,547 | 26,492 | 70,140 |
| Net earnings | 6,502 | 18,679 | 18,583 | 26,754 | 70,518 |
| Earnings per share – continuing operations | | | | | |
| Basic | 0.10 | 0.30 | 0.29 | 0.41 | 1.10 |
| Diluted | 0.10 | 0.29 | 0.29 | 0.40 | 1.08 |
| Earnings per share | | | | | |
| Basic | 0.10 | 0.30 | 0.29 | 0.42 | 1.11 |
| Diluted | 0.10 | 0.29 | 0.29 | 0.41 | 1.09 |
| Dividends per share | 0.065 | 0.065 | 0.065 | 0.065 | 0.260 |

Interim period revenues and earnings historically reflect some seasonality in both the Compression and Equipment Groups. The first quarter is typically the weakest due to winter shutdowns in the construction industry. The fourth quarter has consistently been the strongest quarter due to a number of factors. The Equipment Group benefits from higher conversions at the Caterpillar dealership of equipment on rent with a purchase option. Prior to the recent change in the revenue recognition policy, the fourth quarter was also positively affected by the timing of project completions in the Compression Group. The second and third quarter impacts of seasonality are relatively neutral.

## RISKS AND RISK MANAGEMENT

In the normal course of business, Toromont is exposed to operating and financial risks that may potentially impact its operating results in either or both of its business segments. The Company and each operating segment employ risk management strategies with a view to mitigating these risks on a cost effective basis.

### Business Cycle

Expenditures on capital goods have historically been cyclical, reflecting a variety of factors including interest rates, consumer and business confidence, commodity prices, corporate profits, credit conditions and the availability of equity capital. Toromont's customers are typically affected, to varying degrees, by trends in the general business cycle within their respective markets. As a result, financial performance is affected by the impact of such business cycles on our customer base.

Sales are also indirectly affected by fluctuations in commodity prices. Commodity price movements in the forestry, metals and petroleum sectors can have an impact on customers' demands for equipment and customer service.

Toromont's business is diversified across a wide range of industry market segments and geographic territories, serving to temper the effects of business cycles on consolidated results. Continued diversification through expansion of the customer base, broadening of the product offering and geographic diversification will further moderate business cycle impacts. Across both operating segments, the Company has focused on the sale of specialized equipment and ongoing support through parts distribution and skilled service. Product support growth has been, and will continue to be, fundamental to mitigation of downturns in the business cycle. The product support business contributes significantly higher profit margins and is subject to less volatility than equipment supply activities.

### Product and Supply

The Equipment Group purchases most of its equipment inventories and parts from Caterpillar under a dealership agreement that dates back to 1993. As is customary in distribution arrangements of this type, the agreement with Caterpillar can be terminated by either party upon 90 days notice. In the event Caterpillar terminates, it must repurchase substantially all inventories of new equipment and parts at cost. Toromont has maintained an excellent relationship with Caterpillar for over a decade and management expects this will continue going forward. In 2005, Toromont improved on its standing amongst North American Caterpillar dealerships, moving into Gold status, which is awarded to the top ten dealers.

Toromont is dependent on the continued market acceptance of Caterpillar's products. It is believed that Caterpillar has a solid reputation as a high quality manufacturer, with excellent brand recognition and customer support and high market shares in many of the markets it serves.

Toromont is also dependent on Caterpillar for timely supply of equipment and parts. From time to time, during periods of intense demand, Caterpillar may find it necessary to allocate its supply of particular products among its dealers. Such allocations of supply have not in the past proven to be a significant impediment in the conduct of business. However, there can be no assurance that Caterpillar will continue to supply its products in the quantities and timeframes required by our customers. Further, product supply could also be disrupted by potential labour disputes or strike action at Caterpillar.

### Competition

Both the Equipment and Compression Groups compete with a large number of international, national, regional and local suppliers. Although price competition can be strong, there are a number of factors that have enhanced the Company's ability to compete throughout its market areas including: the range and quality of products and services; ability to meet sophisticated customer requirements; distribution capabilities including number and proximity of locations; financial services offered by Caterpillar Finance; e-commerce solutions; reputation and financial strength.

### Credit Risk

The Company has a large diversified customer base and is not dependent on any single customer or group of customers. Toromont also has credit exposure arising from foreign exchange and interest rate derivative contracts. This risk is minimized by ensuring there is no excessive concentration of credit risk with any single counterparty and by dealing only with highly rated financial institutions.

### Warranties and Maintenance Contracts

Toromont provides warranties for most of the equipment it sells, typically for a one-year period following sale. The warranty claim risk is generally shared jointly with the equipment manufacturer. Accordingly, liability is generally limited to the service component of the warranty claim, while the manufacturer is responsible for providing the required parts.

The Company also enters into long-term maintenance and repair contracts, whereby it is obligated to maintain equipment for its customers. The length of these contracts varies generally from two to five years. The contracts are typically fixed price with provisions for inflationary adjustments. Due to the long-term nature of these contracts, there is a risk that maintenance costs may exceed estimate, thereby resulting in a loss on the contract. These contracts are closely monitored for early warning signs of cost overruns. In addition, the manufacturer may, in certain circumstances, share in the cost overruns if profitability falls below a certain threshold.

### Foreign Exchange

The Equipment Group sources the majority of its products from the United States. Consequently, reported costs of inventory and the transaction prices charged to customers for equipment and parts are affected by the relative strength of the Canadian dollar. The Company mitigates exchange rate risk by entering into foreign currency contracts to fix the cost of imported inventory where appropriate. In addition, pricing to customers is generally adjusted to reflect changes in the Canadian dollar landed cost of imported goods.

The Compression Group purchases components from suppliers in the United States and sells packages in foreign currencies, primarily U.S. dollar and Euro. Entering into foreign currency contracts, where appropriate, reduces these exchange rate risks.

Fluctuations in the value of the Canadian dollar relative to other currencies also has some impact on Toromont's consolidated financial reporting, with the financial results of subsidiaries in the United States and other countries being translated into Canadian dollars upon consolidation. However, such exchange rate fluctuations have historically not been material relative to the overall earnings or financial position.

### Interest Rate

Interest rate risk arises from potential changes in interest rates and the impact on the cost of borrowing. Floating rate debt exposes the Company to fluctuations in short-term interest rates, while fixed rate debt exposes it to future interest rate movements upon the debt's maturity. Balancing the portfolio of credit facilities at floating rates and term debt at fixed rates has reduced interest rate risk. In addition, the Company will from time to time enter into interest rate swap agreements to manage its current and anticipated exposure to interest rates. Market conditions and the impact of interest rate fluctuations on its fixed/floating interest rate exposure are monitored closely.

## CRITICAL ACCOUNTING POLICIES AND ESTIMATES

Toromont's significant accounting policies are described in Note 1 to the consolidated financial statements. The most critical of these policies are those related to revenue recognition, and property, plant and equipment. Each policy involves a number of estimates and assumptions made by management. Different accounting policies, or changes to estimates or assumptions could potentially have a material impact, positive or negative, on Toromont's financial position and results of operations. These critical accounting policies and estimates are described below.

### Revenue Recognition

In 2005, the Company changed its accounting policy to reflect revenues generated from the assembly and manufacture of projects using the percentage-of-completion approach of accounting for performance of production-type contracts. This is discussed in more detail in this MD&A under the heading "Change in Accounting Policy."

This approach to revenue recognition requires management to make a number of estimates and assumptions surrounding the expected profitability of the contract, the estimated degree of completion based on cost progression and other detailed factors. Although these factors are routinely reviewed as part of the project management process, changes in these estimates or assumptions could lead to changes in the revenues recognized in a given period. However, there are many of these projects in process at any given point, the majority of which are in actual construction for a period of three months or less. Therefore, management believes that a material difference would require systemic changes in the approach to these assumptions and estimates.

### Valuation of Capital Assets

Valuations of capital assets are reviewed on a regular basis or whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. In cases where the undiscounted expected future cash flows are less than the carrying amount, an impairment loss is recognized. Impairment losses on long-lived assets are measured as the amount by which the carrying value of an asset or asset group exceeds its fair value, as determined by the discounted future cash flows of the asset or asset group.

In 2005, this measurement process led to the recording of a $17.8 million asset impairment charge taken against these assets. After reflecting this charge, the total net book value of the power generation assets held by Toromont is reduced to $14.9 million. Assumptions that significantly impact the expected future cash flows of these assets, including future prices of electricity, the cost of natural gas and operating hours over the estimated life of the plants require significant judgment. Actual results could differ significantly from management estimates.

A significant amount of the Company's assets include property, plant and equipment and rental equipment. These assets are depreciated over their estimated useful lives, determined based on current circumstances and past experience. The rates and methodologies used are reviewed on an ongoing basis to ensure they continue to be appropriate.

## FUTURE ACCOUNTING STANDARDS

As at the date of the MD&A, there were no anticipated accounting changes that would materially impact the financial reporting of future periods.

# MANAGEMENT'S REPORT

The preparation and presentation of the Company's consolidated financial statements is the responsibility of management. The financial statements have been prepared in accordance with generally accepted accounting principles and necessarily include estimates, which are based on management's best judgments. Information contained elsewhere in the Annual Report is consistent, where applicable, with that contained in the financial statements.

Management maintains appropriate systems of internal control. Policies and procedures are designed to give reasonable assurance that transactions are appropriately authorized, assets are safeguarded from loss or unauthorized use and financial records are properly maintained to provide reliable information for preparation of financial statements.

Ernst & Young LLP, an independent firm of Chartered Accountants, were appointed by the shareholders as external auditors to examine the consolidated financial statements in accordance with generally accepted auditing standards in Canada and provide an independent professional opinion. Their report is presented with the consolidated financial statements.

The Board of Directors, acting through an Audit Committee comprised solely of independent directors, is responsible for determining that management fulfills its responsibilities in the preparation of the consolidated financial statements and the financial control of operations. The Audit Committee recommends the independent auditors for appointment by the shareholders. It meets regularly with financial management and the independent auditors to discuss internal controls, auditing matters and financial reporting issues. The independent auditors have unrestricted access to the Audit Committee. The consolidated financial statements and Management's Discussion and Analysis have been approved by the Board of Directors for inclusion in this Annual Report, based on the review and recommendation of the Audit Committee.

Hugo T. Sørensen
President and
Chief Executive Officer

Paul R. Jewer
Vice President Finance and
Chief Financial Officer

*Toronto, Ontario*
*February 2, 2006*

# AUDITORS' REPORT

To the Shareholders of Toromont Industries Ltd.:

We have audited the consolidated balance sheets of Toromont Industries Ltd. as at December 31, 2005 and 2004 and the consolidated statements of earnings, retained earnings and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2005 and 2004 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

Ernst & Young LLP

Ernst & Young LLP
Chartered Accountants

*Toronto, Ontario*
*February 2, 2006*

# CONSOLIDATED BALANCE SHEETS

| as at December 31 ($ thousands) | 2005 | 2004 |
|---|---|---|
| **Assets** | | |
| Current assets | | |
| Cash and cash equivalents | $ 50,716 | $ – |
| Accounts receivable | 337,381 | 257,459 |
| Inventories (note 5) | 379,819 | 324,461 |
| Future income taxes (note 16) | 18,501 | 12,716 |
| Other current assets | 7,742 | 4,890 |
| Total current assets | 794,159 | 599,526 |
| Property, plant and equipment (note 6) | 168,253 | 186,811 |
| Rental equipment (note 8) | 115,154 | 110,834 |
| Goodwill | 34,800 | 34,800 |
| Future income taxes (note 16) | 1,126 | – |
| Other assets (note 9) | 30,480 | 30,466 |
| Total assets | $ 1,143,972 | $ 962,437 |
| **Liabilities** | | |
| Current liabilities | | |
| Accounts payable and accrued liabilities (note 19) | $ 357,714 | $ 302,440 |
| Current portion of long-term debt (note 10) | 12,828 | 20,539 |
| Income taxes payable | 12,627 | 13,253 |
| Total current liabilities | 383,169 | 336,232 |
| Deferred revenues | 31,709 | 29,543 |
| Long-term debt (note 10) | 241,265 | 166,508 |
| Accrued pension liability (note 15) | 6,017 | 5,860 |
| Future income taxes (note 16) | – | 8,439 |
| **Shareholders' equity** | | |
| Share capital (note 11) | 107,348 | 102,719 |
| Contributed surplus (note 12) | 6,692 | 4,484 |
| Retained earnings | 373,993 | 313,615 |
| Cumulative translation adjustment | (6,221) | (4,963) |
| Total shareholders' equity | 481,812 | 415,855 |
| Total liabilities and shareholders' equity | $ 1,143,972 | $ 962,437 |

See accompanying notes

On behalf of the Board:

Robert M. Ogilvie
Director

John S. McCallum
Director

# CONSOLIDATED STATEMENTS OF EARNINGS

| Years ended December 31 ($ thousands, except share amounts) | 2005 | 2004 |
|---|---|---|
| **Revenues** | $ 1,599,792 | $ 1,434,756 |
| Cost of goods sold | 1,250,714 | 1,130,516 |
| Gross profit | 349,078 | 304,240 |
| Selling and administrative expenses | 211,899 | 184,883 |
| Asset impairment charge (note 7) | 17,800 | – |
| **Operating income** | 119,379 | 119,357 |
| Interest expense (note 10) | 12,977 | 12,138 |
| Interest and investment income | (2,785) | (1,936) |
| Income before income taxes | 109,187 | 109,155 |
| Income taxes (note 16) | 30,795 | 39,015 |
| **Earnings from continuing operations** | 78,392 | 70,140 |
| Gain on disposal of discontinued operations (note 3) | 745 | – |
| (Loss) earnings from discontinued operations (note 3) | (175) | 378 |
| **Net earnings** | $ 78,962 | $ 70,518 |
| **Basic earnings per share** (note 17) | | |
| Continuing operations | $ 1.24 | $ 1.10 |
| Discontinued operations | 0.01 | 0.01 |
| | $ 1.25 | $ 1.11 |
| **Diluted earnings per share** (note 17) | | |
| Continuing operations | $ 1.22 | $ 1.08 |
| Discontinued operations | 0.01 | 0.01 |
| | $ 1.23 | $ 1.09 |
| **Weighted average number of shares outstanding – Basic** | 63,310,574 | 63,462,156 |
| **Weighted average number of shares outstanding – Diluted** | 64,420,633 | 64,655,599 |

See accompanying notes

# CONSOLIDATED STATEMENTS OF RETAINED EARNINGS

| Years ended December 31 ($ thousands) | 2005 | 2004 |
|---|---|---|
| Retained earnings, beginning of year, as reported | $ 313,615 | $ 277,361 |
| Change in accounting policy (note 2) | 1,696 | – |
| Retained earnings, beginning of year, as restated | 315,311 | 277,361 |
| Net earnings | 78,962 | 70,518 |
| Dividends | (20,280) | (16,486) |
| Shares purchased for cancellation | – | (17,778) |
| Retained earnings, end of year | $ 373,993 | $ 313,615 |

See accompanying notes

# CONSOLIDATED STATEMENTS OF CASH FLOWS

| Years ended December 31 ($ thousands) | 2005 | 2004 |
|---|---|---|
| **Operating activities** | | |
| Net earnings | $ 78,962 | $ 70,518 |
| Items not requiring cash and cash equivalents | | |
| Depreciation | 46,594 | 42,756 |
| Asset impairment charge | 17,800 | – |
| Stock-based compensation | 2,378 | 2,128 |
| Accrued pension liability | 157 | 853 |
| Future income taxes | (12,792) | (486) |
| Gain on sale of rental equipment and property, plant and equipment | (8,258) | (7,682) |
| Gain on disposal of discontinued operations (note 3) | (745) | – |
| | 124,096 | 108,087 |
| Change in non-cash working capital and other | | |
| Accounts receivable | (68,670) | (32,043) |
| Inventories | (82,487) | (22,581) |
| Accounts payable and accrued liabilities | 59,363 | 9,103 |
| Other | (7,688) | (2,257) |
| Cash provided by operating activities | 24,614 | 60,309 |
| **Investing activities** | | |
| Additions to rental equipment | (52,268) | (39,133) |
| Additions to property, plant and equipment | (20,545) | (26,475) |
| Sale of rental equipment | 27,103 | 27,452 |
| Sale of property, plant and equipment | 435 | 4,797 |
| Disposal of discontinued operations (note 3) | 18,933 | – |
| Decrease in other assets | 1,219 | 1,258 |
| Business acquisitions (note 4) | – | (6,836) |
| Cash used in investing activities | (25,123) | (38,937) |
| **Financing activities** | | |
| (Decrease) increase in term credit facility debt | (40,101) | 19,590 |
| Issue of other long-term debt | 138,121 | 8,925 |
| Repayment of other long-term debt | (30,974) | (18,458) |
| Dividends | (20,280) | (16,486) |
| Shares issued on exercise of options | 4,459 | 4,525 |
| Shares purchased for cancellation | – | (19,468) |
| Cash provided by (used in) financing activities | 51,225 | (21,372) |
| Increase in cash and cash equivalents | 50,716 | – |
| Cash and cash equivalents at beginning of year | – | – |
| Cash and cash equivalents at end of year | $ 50,716 | $ – |
| **Supplemental cash flow information** | | |
| Interest paid | $ 12,298 | $ 12,215 |
| Income taxes paid | $ 50,422 | $ 41,685 |
| Capital asset additions included in accounts payable and accrued liabilities | $ 2,532 | $ 5,733 |

See accompanying notes

# NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2005 ($ thousands except where otherwise indicated)

## 1 SIGNIFICANT ACCOUNTING POLICIES

The consolidated financial statements of Toromont Industries Ltd. and its subsidiaries (the "Company") have been prepared by management in accordance with Canadian generally accepted accounting principles ("GAAP").

### Basis of Consolidation

The consolidated financial statements include the accounts of the Company and its wholly owned subsidiaries. All significant inter-company accounts and transactions have been eliminated.

### Use of Estimates

The preparation of the consolidated financial statements in conformity with Canadian GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the year. Actual results could differ from those estimates. Estimates are used in accounting for items and matters such as long-term contracts, allowance for uncollectible accounts receivable, inventory obsolescence, product warranty, depreciation, asset valuations, employee benefits and taxes.

### Revenue Recognition

Revenue is recognized when persuasive evidence of an arrangement exists, the price is fixed or determinable, performance requirements are achieved and ultimate collection is reasonably assured. In addition to this general policy, the following describes the specific revenue recognition policies for each major category of revenue.

(a) Revenues from the sale of equipment are recorded when goods are shipped to the customer, at which time title to the equipment and significant risks of ownership have passed.

(b) Revenues from the supply of equipment systems involving design, manufacture, installation and start-up are recorded based on the percentage-of-completion method, determined based on total costs incurred to expected total costs of the project. Revenues and costs begin to be recognized when progress reaches a stage of completion sufficient to reasonably determine the probable results. Any foreseeable losses on such projects are charged to operations when determined.

(c) Revenues from equipment rentals are recognized in accordance with the terms of the relevant agreement with the customer, generally on a straight-line basis over the term of the agreement.

(d) Product support services include sales of parts and servicing of equipment. For the sale of parts, revenues are recognized when the part is shipped to the customer. For servicing of equipment, revenues are recognized as the service work is completed and billed.

(e) Revenues on extended warranty and long-term maintenance contracts are recognized on a percentage-of-completion basis proportionate to the service work that has been performed based on the parts and labour service provided. At the completion of the contract, any remaining profit on the contract is recognized as revenue. Any losses estimated during the term of the contract are recognized when identified.

### Translation of Foreign Currencies

Transactions denominated in foreign currencies are translated into Canadian dollars at the rate of exchange in effect at the time of the transaction, unless the transaction is hedged. Monetary assets and liabilities are translated into Canadian dollars at the year-end exchange rate. Non-monetary items are translated at historical rates. All exchange gains and losses are included in earnings.

Foreign subsidiaries are financially and operationally self-sustaining. Accordingly, their assets and liabilities are translated into Canadian funds at the year-end exchange rate. Revenue and expense items are translated at the average exchange rate for the year. The foreign exchange impact of these translations is included in the cumulative translation adjustment account in shareholders' equity.

### Derivative Financial Instruments

Derivative financial agreements are used to manage exposure to fluctuations in exchange rates and interest rates. The Company does not enter into derivative financial agreements for speculative purposes.

All derivative financial instruments designated as hedges are formally documented, including the risk management objective and strategy. On an ongoing basis, an assessment is made as to whether the designated derivative financial instruments continue to be effective in offsetting changes in fair values or cash flows of the hedged transactions.

Foreign exchange forward contracts and options are identified as a hedge of commitments with realized gains and losses being included in the cost of the underlying hedged item. Unrealized gains and losses on currency forwards are not recognized.

The interest rate swap is identified as a hedge against interest rate fluctuations because it offsets the interest rate exposure on the underlying hedged item. The exchange of interest payments on the interest rate swap is recognized on an accrual basis over the life of the contract as an adjustment to interest expense. Unrealized gains and losses are not recognized.

**Income Taxes**

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

**Stock-Based Compensation**

The fair value method of accounting for stock options is used. The fair value of option grants is calculated using the Black-Scholes option pricing model and is recognized as compensation expense over the vesting period of those grants. A corresponding adjustment is recorded through contributed surplus. On the exercise of stock options, the consideration paid by the employee and the related amounts in contributed surplus are credited to common share capital.

**Employee Future Benefits**

For defined contribution plans, which cover the majority of employees, the pension expense recorded in earnings is the amount of the contributions the Company is required to pay in accordance with the terms of the plan.

For defined benefit plans, which cover approximately 7% of employees, the Company accrues its obligations and the related costs, net of plan assets. The Company has adopted the following policy for its defined benefit plans:

- The cost of pensions earned by employees is actuarially determined using the projected unit credit method pro-rated on length of service and management's best estimate assumptions to value its pensions using a measurement date of December 31;
- For the purpose of calculating the expected return on plan assets, those assets are valued at fair value;
- Past service costs from plan amendments are amortized on a straight-line basis over the average remaining service period of employees active at the date of amendments;
- The excess of the net actuarial gain (loss) over 10% of the greater of the benefit obligation and the fair value of plan assets is amortized on a straight-line basis over the average remaining service period of the active employees.

**Earnings per Share ("EPS")**

Basic EPS is calculated by dividing the net earnings available to common shareholders by the weighted average number of common shares outstanding during the year. Diluted EPS is calculated using the treasury stock method, which assumes that all outstanding stock option grants are exercised, if dilutive, and the assumed proceeds are used to purchase the Company's common shares at the average market price during the year.

**Cash and Cash Equivalents**

Cash and cash equivalents, including cash on account, demand deposits and short-term investments with original maturities of three months or less, are recorded at cost, which approximates market value.

**Inventories**

Equipment inventories, repair and distribution parts, and work-in-process are recorded at the lower of cost and net realizable value. Cost for serialized inventory is determined on a specific item basis. Cost for non-serialized inventory is determined based on weighted average actual cost. Direct materials are recorded at the lower of cost and replacement cost.

**Rental Equipment**

Rental equipment is recorded at cost. Rental equipment is depreciated over its estimated useful life on a straight-line basis. Estimated useful lives range from 1 to 10 years.

**Property, Plant and Equipment**

Property, plant and equipment are recorded at cost. Depreciation is recognized principally on a straight-line basis to depreciate the cost of these assets over their estimated useful lives. Estimated useful lives range from 20 to 30 years for buildings, 3 to 10 years for equipment and 20 years for power generation assets.

### Impairment of Long-lived Assets

Long-lived assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. In cases where the undiscounted expected future cash flows are less than the carrying amount, an impairment loss is recognized. Impairment losses on long-lived assets are measured as the amount by which the carrying value of an asset group exceeds its fair value, as determined by the discounted future cash flows of the asset group.

### Goodwill

Goodwill represents the cost of acquired businesses in excess of the fair value of net identifiable assets acquired. Goodwill is tested for impairment annually, or more frequently if events or changes in circumstances indicate a potential impairment.

### Comparative Amounts

Certain comparative figures have been restated to conform with the current year's presentation.

## 2 CHANGE IN ACCOUNTING POLICY

In the fourth quarter of 2005, the percentage-of-completion approach of accounting for performance of production-type contracts was adopted. In the past, the completed contract method was used. Results for each of the first three quarters of the year ended December 31, 2005 have been restated to reflect the percentage-of-completion method of revenue recognition. Periods prior to January 1, 2005 have not been restated.

Under the new method, revenues and cost of goods sold are recognized in income based on the total costs incurred to period end as a percentage of expected total costs of the project. Revenues and costs begin to be recognized when progress reaches a stage of completion sufficient to reasonably determine the probable results. Any foreseeable losses on projects are charged to income at the time they become evident. This method of revenue recognition matches revenues and cost of goods sold to the period in which the projects occurred and promotes a clearer understanding of underlying activities.

As a result of the adoption of this policy, the Company has adjusted retained earnings as at January 1, 2005 to reflect the percentage of completion of work in progress at December 31, 2004. Prior periods have not been restated. The components of this adjustment are summarized in the following table. The adjustment is attributable to the Compression Group; there is no impact on reported results for the Equipment Group.

| | |
|---|---|
| Revenues | $ 22,493 |
| Cost of goods sold | 19,860 |
| Income taxes | 937 |
| Increase to retained earnings at January 1, 2005 | $ 1,696 |

Had this change in accounting policy not occurred, revenue recognized in the year would have been reduced by $34.3 million, cost of goods sold would have been reduced by $26.7 million and income taxes would have been reduced by $2.7 million, resulting in a decrease in net income of $4.9 million.

## 3 DISCONTINUED OPERATIONS

Effective August 31, 2005, the assets of the Ontario Sterling Division, previously included in the Equipment Group, were sold. Ontario Sterling was a Sterling Truck franchise in the Greater Toronto Area selling and servicing medium and heavy duty Class 5 to Class 8 trucks. It was determined that this business was not core to the growth of the Company, and that it was not generating returns commensurate with the Company's expectations. Total proceeds on the sale were $18,933 consisting of $17,707 for working capital and $1,226 for other, including capital assets. The after-tax gain on the sale of these operations was $745.

Earnings from discontinued operations include the following:

| | 2005 | 2004 |
|---|---|---|
| Revenues | $ 32,238 | $ 52,582 |
| (Loss) income before income taxes | $ (283) | $ 610 |

## 4 BUSINESS ACQUISITIONS

Effective December 1, 2004, the Company purchased (a) Access Rentals and Supply Limited, a privately owned rental operator based in Sudbury, Ontario, and (b) Engineered Refrigeration Systems, Inc., a privately owned industrial refrigeration company based in Mobile, Alabama. There were no business acquisitions in 2005.

The acquisitions were accounted for using the purchase method, which allocates the purchase price of a business to the assets acquired and the liabilities assumed based on their fair value at date of acquisition, with any excess recognized as goodwill. The results of the companies acquired are included in the consolidated financial statements from date of acquisition.

Details of the business acquisition purchase equations, including cash consideration paid and the net assets acquired at their fair values, are as follows:

| | 2004 |
|---|---|
| Cash | $ 542 |
| Non-cash working capital | 1,463 |
| Property, plant and equipment | 444 |
| Rental equipment | 4,183 |
| Goodwill | 450 |
| Future income taxes | 296 |
| Total investment | $ 7,378 |
| Less: assumed debt | (3,424) |
| Purchase price | $ 3,954 |

Goodwill does not include any amounts that are deductible for tax purposes.

## 5 INVENTORIES

| | 2005 | 2004 |
|---|---|---|
| Equipment | $ 229,054 | $ 196,325 |
| Repair and distribution parts | 72,786 | 60,642 |
| Direct materials | 33,291 | 14,287 |
| Work-in-process | 44,688 | 53,207 |
| | $ 379,819 | $ 324,461 |

## 6 PROPERTY, PLANT AND EQUIPMENT

| | | | 2005 | | | 2004 |
|---|---|---|---|---|---|---|
| | Cost | Accumulated Depreciation | Net Book Value | Cost | Accumulated Depreciation | Net Book Value |
| Land | $ 37,134 | $ – | $ 37,134 | $ 35,745 | $ – | $ 35,745 |
| Buildings | 109,008 | 33,409 | 75,599 | 104,076 | 27,877 | 76,199 |
| Equipment | 125,840 | 85,205 | 40,635 | 114,489 | 74,501 | 39,988 |
| Power generation | 44,565 | 29,680 | 14,885 | 44,565 | 9,686 | 34,879 |
| | $ 316,547 | $ 148,294 | $ 168,253 | $ 298,875 | $ 112,064 | $ 186,811 |

Depreciation expense for the year ended December 31, 2005 was $22,705 (2004 – $20,919).

## 7 IMPAIRMENT OF LONG-LIVED ASSETS

Toromont recently signed a Letter of Intent for a five-year agreement with the Ontario Power Authority. Based on the terms of this agreement, the Company has concluded that the revenues generated will not be sufficient to cover the fixed operating costs and depreciation of the assets. The Company has recorded a pre-tax loss of $17,800 to reflect impairment of these long-lived assets, $11,600 on an after-tax basis. After recording this charge, the net book value of power generation assets was $14,885.

## 8 RENTAL EQUIPMENT

| | 2005 | 2004 |
|---|---|---|
| Cost | $ 191,123 | $ 182,557 |
| Less: Accumulated depreciation | 75,969 | 71,723 |
| | $ 115,154 | $ 110,834 |

Depreciation expense for the year ended December 31, 2005 was $23,889 (2004 – $21,837). Operating income from rental operations for the year ended December 31, 2005 was $19.5 million (2004 – $18.9 million).

## 9 OTHER ASSETS

Other assets include $29,855 (2004 – $28,623), representing equipment sold directly to customers or to third-party lessors for which the Company has provided a guarantee to repurchase, at a predetermined residual value and date. In accordance with GAAP, such transactions that involve a repurchase undertaking by the Company, or other contingent obligation similar to the guarantee of lease residuals, are accounted for as operating leases, wherein revenue is recognized over the period extending to the date of residual value guarantee.

## 10 LONG-TERM DEBT

| | 2005 | 2004 |
|---|---|---|
| Drawn on bank term facility (a) | $ 30,000 | $ 70,101 |
| Senior debentures (b) | 206,174 | 97,175 |
| Notes payable (c) | 17,919 | 19,771 |
| Total long-term debt | 254,093 | 187,047 |
| Less current portion | 12,828 | 20,539 |
| | $ 241,265 | $ 166,508 |

All debt is unsecured.

(a) The Company maintains $231,000 (2004 – $181,000) in bank credit, provided through committed credit facilities, maturing in 2008. Bank borrowings bear interest at rates ranging from prime to bankers acceptance rates. Standby letters of credit issued in lieu of holdbacks utilized an additional $9,800 of the credit lines at December 31, 2005 (2004 – $13,300).

(b) Terms of the senior debentures are:
- $21,174, 8.17% senior debentures due September 18, 2008, blended principal and interest payments semi-annually from September 18, 2004 through to maturity;
- $45,000, 6.80% senior debentures due March 29, 2011, interest payable semi-annually through March 29, 2007; thereafter, blended principal and interest payments through to maturity;
- $125,000, 4.92% senior debentures due October 13, 2015, interest payable semi-annually, principal due on maturity;
- $15,000, 7.06% senior debentures due March 29, 2019, interest payable semi-annually through September 29, 2009; thereafter, blended principal and interest payments through to maturity.

(c) Notes payable mature from 2006 to 2008 and bear interest at rates ranging from 1.36% to 7.75%.

The above credit arrangements include covenants, restrictions and events of default usual in credit facilities of this nature, including requirements to meet certain financial tests periodically and restrictions on additional indebtedness and encumbrances.

Scheduled principal repayments of long-term debt are as follows:

| | |
|---|---|
| 2006 | $ 12,828 |
| 2007 | 21,970 |
| 2008 | 52,635 |
| 2009 | 10,661 |
| 2010 | 11,947 |
| 2011 to 2019 | 144,052 |
| | $ 254,093 |

Interest expense includes interest on debt initially incurred for a term greater than one year of $12,461 (2004 – $11,837).

## 11 SHARE CAPITAL

The Company is authorized to issue an unlimited number of common shares and preferred shares. No preferred shares have been issued.

The changes in the common shares issued and outstanding during the year were as follows:

| | | 2005 | | 2004 |
|---|---|---|---|---|
| | Number of Common Shares | Common Share Capital | Number of Common Shares | Common Share Capital |
| Balance, beginning of year | 63,082,586 | $ 102,719 | 63,563,246 | $ 99,785 |
| Exercise of stock options | 542,350 | 4,629 | 573,640 | 4,624 |
| Purchase of shares for cancellation | – | – | (1,054,300) | (1,690) |
| Balance, end of year | 63,624,936 | $ 107,348 | 63,082,586 | $ 102,719 |

On April 14, 2004, the Company effected a two-for-one stock split by way of a stock dividend. All share amounts disclosed in the consolidated financial statements have been retroactively adjusted to give effect to the stock dividend.

## 12 CONTRIBUTED SURPLUS

Changes in contributed surplus were as follows:

| | 2005 | 2004 |
|---|---|---|
| Contributed surplus, beginning of year | $ 4,484 | $ 2,455 |
| Stock-based compensation | 2,378 | 2,128 |
| Value of compensation cost associated with exercised options | (170) | (99) |
| Contributed surplus, end of year | $ 6,692 | $ 4,484 |

## 13 FINANCIAL INSTRUMENTS

Hedging activities are contracted with Canadian Schedule A chartered banks as counterparties. There is no significant concentration of credit risk with counterparties.

Transactions are limited to the following:

### Foreign Exchange Contracts

In the normal course of business, foreign exchange contracts and options are entered into with financial institutions to hedge foreign currency denominated obligations related to purchases of inventory and sales of products. Gains and losses arising from these contracts offset the foreign exchange losses and gains from the underlying hedged transactions. Forward exchange contracts in Euros and U.S. dollars at December 31, 2005 are as follows:

| | | Notional Amount | Average Exchange Rate |
|---|---|---|---|
| Purchase contracts | USD | 127,570 | $ 1.1770 |
| Sales contracts | USD | 17,296 | $ 1.1815 |
| | EUR | 1,369 | $ 1.3833 |

### Interest Rate Swap Contract

An interest rate swap is held which converts $30,000 (2004 – $30,000) of floating rate debt into fixed rate debt at 5.88%. This transaction is with a Canadian chartered bank and matures September 1, 2008. This swap partially offsets exposure to Canadian floating interest rates.

### Fair Value of Financial Instruments

The following methods and assumptions have been used to estimate the fair value of financial instruments:

- Cash and cash equivalents, accounts receivable and accounts payable and accrued liabilities and borrowings under the bank term facility are valued at their carrying amounts on the balance sheet, which represent an appropriate estimate of their fair values due to their near-term maturities;
- Senior debentures and notes payable are valued based on discounted cash flows using current interest rates for debt with similar terms and remaining maturities. The Company has no plans to prepay these instruments prior to maturity;
- The interest rate swap reflects the present value of the potential loss if settlement were to take place at the balance sheet date; and
- Foreign exchange contracts are represented by the estimated amounts that the Company would receive or pay to settle the contracts at the balance sheet date.

The fair value and the carrying amount of financial instruments as at December 31 are as follows:

| | 2005 | | 2004 | |
|---|---|---|---|---|
| | Fair Value | Carrying Amount | Fair Value | Carrying Amount |
| Senior debentures | $ 212,714 | $ 206,174 | $ 104,797 | $ 97,175 |
| Notes payable | $ 17,650 | $ 17,919 | $ 19,251 | $ 19,771 |
| Foreign exchange contracts | $ (1,464) | $ – | $ (5,538) | $ – |
| Interest rate swap contract | $ (1,394) | $ – | $ (2,450) | $ – |

## 14 STOCK-BASED COMPENSATION PLAN

The Company maintains an Executive Stock Option Plan for certain employees. Under the plan, options may be granted for up to 6,096,000 common shares. Stock options have a seven-year term, vest 20% cumulatively on each anniversary date of the grant and are exercisable at the designated common share price, which is fixed at prevailing market prices of the common shares at the date the option is granted. Each stock option is exercisable into one common share of the Company at the price specified in the terms of the option.

A reconciliation of the outstanding options is as follows:

| | 2005 | | 2004 | |
|---|---|---|---|---|
| | Number of Options | Weighted Average Exercise Price | Number of Options | Weighted Average Exercise Price |
| Options outstanding, beginning of year | 2,849,170 | $ 10.47 | 2,895,820 | $ 8.76 |
| Granted | 411,375 | 21.97 | 565,340 | 16.59 |
| Exercised | (542,350) | 7.75 | (573,640) | 7.70 |
| Forfeited | (28,400) | 15.10 | (38,350) | 12.86 |
| Options outstanding, end of year | 2,689,795 | $ 12.72 | 2,849,170 | $ 10.47 |
| Options exercisable at year-end | 1,211,876 | $ 9.54 | 1,234,124 | $ 8.26 |

The following table summarizes stock options outstanding and exercisable at December 31, 2005:

| | Options Outstanding | | | Options Exercisable | |
|---|---|---|---|---|---|
| Range of Exercise Prices | Number Outstanding | Weighted Average Remaining Life (years) | Weighted Average Exercise Price | Number Outstanding | Weighted Average Exercise Price |
| $7.09 – $8.04 | 749,600 | 1.6 | $ 7.72 | 651,720 | $ 7.67 |
| $10.27 – $10.71 | 1,003,950 | 3.6 | 10.66 | 459,358 | 10.66 |
| $16.59 – $22.78 | 936,245 | 5.6 | 18.94 | 100,798 | 16.59 |
| Total | 2,689,795 | 3.7 | $ 12.72 | 1,211,876 | $ 9.54 |

The fair value of each stock option granted is estimated on the date of grant. The weighted average fair value price of options granted during the year was $6.98 (2004 – $5.22). The fair value of the stock options was determined using the Black-Scholes option pricing model with the following assumptions:

| | 2005 | 2004 |
|---|---|---|
| Expected life of options (years) | 5.75 | 5.60 |
| Expected stock price volatility | 25.0% | 25.0% |
| Expected dividend yield | 1.5% | 1.6% |
| Risk-free interest rate | 3.5% | 3.6% |

## 15 EMPLOYEE FUTURE BENEFITS

The Company sponsors pension arrangements for substantially all of its employees, primarily through defined contribution plans in Canada and a 401(k) matched savings plan in the United States. Certain unionized employees do not participate in Company-sponsored plans, and contributions are made to these union-sponsored plans in accordance with respective collective bargaining agreements. In the case of the defined contribution plans, regular contributions are made to the employees' individual accounts, which are administered by a plan trustee, in accordance with the plan document.

Approximately 7% of participating employees are included in defined benefit plans.

a) Powell Plan – Consists of personnel of Powell Equipment (acquired by Toromont in 2001). The plan is a contributory plan which provides pension benefits based on length of service and career average earnings. The most recent actuarial valuation of the plan was completed as at December 31, 2003. The next valuation is scheduled as at December 31, 2006.

b) Executive Plan – This is a non-contributory pension arrangement for certain senior executives which provides for a supplementary retirement payout in excess of amounts provided for under the registered plan. The most recent actuarial valuation of the plan was completed as at January 1, 2005. The next valuation is scheduled as at January 1, 2008.

c) Other Plan assets and obligations – This provides for certain retirees and terminated vested employees of businesses previously acquired by the Company as well as for retired participants of the defined contribution plan that, in accordance with the plan provisions, have elected to receive a pension directly from the plan. The most recent actuarial valuation of the plan was completed as at January 1, 2003. The next valuation is scheduled as at January 1, 2006.

The changes in the fair value of assets and the pension obligations and the funded status of the defined benefit plans were as follows:

| | 2005 | 2004 |
|---|---|---|
| **Accrued benefit obligations:** | | |
| Balance, beginning of year | $ 66,723 | $ 57,236 |
| Service cost | 2,186 | 2,432 |
| Interest cost | 3,787 | 3,814 |
| Actuarial loss | 3,992 | 7,330 |
| Benefits paid | (6,185) | (4,089) |
| Balance, end of year | $ 70,503 | $ 66,723 |
| **Plan assets:** | | |
| Fair value, beginning of year | $ 53,132 | $ 50,028 |
| Actual return on plan assets | 5,368 | 4,590 |
| Company contributions | 2,260 | 2,051 |
| Participant contributions | 525 | 552 |
| Benefits paid | (6,185) | (4,089) |
| Fair value, end of year | $ 55,100 | $ 53,132 |
| **Funded status of the plans:** | $ (15,403) | $ (13,591) |
| Unrecognized actuarial loss | 11,455 | 10,096 |
| Unrecognized past service benefit | (2,069) | (2,365) |
| **Accrued pension liability** | $ (6,017) | $ (5,860) |

The accrued net pension liability of $6,017 includes a $6,364 prepaid pension asset related to the Powell Plan and Other Plan assets and obligations. It also includes a $12,381 liability related to the defined benefit arrangement for senior executives, specifically, the supplementary portion of the liability that exists outside of the registered plan. The Company expenses the costs of these plans with cash funding limited to the maximum amount according to pension regulations.

The significant annual actuarial assumptions adopted in measuring the accrued benefit obligations were as follows:

| | 2005 | 2004 |
|---|---|---|
| Discount rate | 5.00% | 5.75% |
| Expected long-term rate of return on plan assets | 7.00% | 7.00% |
| Rate of compensation increase | 4.00% | 4.25% |

There were no Toromont common shares held in the plan as at December 31, 2005. As at December 31, 2004, plan assets included Toromont common shares with a market value of $708.

The allocation of plan assets was as follows:

| | 2005 | 2004 |
|---|---|---|
| Equity securities | 45.4% | 43.7% |
| Debt securities | 39.3% | 41.7% |
| Real estate | 13.6% | 11.8% |
| Cash and cash equivalents | 1.7% | 2.8% |

The net pension expense for the years ended December 31 included the following components:

| | 2005 | 2004 |
|---|---|---|
| **Defined Benefit Plans** | | |
| Service cost | $ 1,661 | $ 1,880 |
| Interest cost | 3,787 | 3,814 |
| Actual return on plan assets | (5,368) | (4,590) |
| Prior service cost | – | (2,660) |
| Actuarial loss | 3,992 | 7,330 |
| Difference between actual and expected return on assets | 1,765 | 1,125 |
| Difference between actual and recognized actuarial loss | (3,124) | (6,360) |
| Difference between actual and recognized past service benefits | (296) | 2,365 |
| | 2,417 | 2,904 |
| **Defined Contribution Plans** | 6,217 | 4,879 |
| **401(k) matched savings plan** | 426 | 350 |
| **Net pension expense** | $ 9,060 | $ 8,133 |

The total cash amount paid or payable for employee future benefits in 2005 was $9,356 (2004 – $7,398).

## 16 INCOME TAXES

Significant components of the provision for income tax expense were as follows:

| | 2005 | 2004 |
|---|---|---|
| Current income tax expense | $ 43,587 | $ 39,501 |
| Future income tax recovery | (12,792) | (486) |
| Total income tax expense | $ 30,795 | $ 39,015 |

A reconciliation of income taxes at Canadian statutory rates with the reported income taxes was as follows:

| | 2005 | 2004 |
|---|---|---|
| Statutory Canadian federal and provincial income tax rates | 36.12% | 36.12% |
| Expected taxes on income | $ 39,438 | $ 39,427 |
| Increase (decrease) in income taxes resulting from: | | |
| Impact of adjustment to tax reserves | (8,700) | – |
| Higher effective tax rates at foreign subsidiaries | 96 | 20 |
| Manufacturing and processing rate reduction | (134) | (231) |
| Large corporation tax | 60 | 203 |
| Non-taxable gains | (119) | (123) |
| Other | 154 | (281) |
| Provision for income taxes | $ 30,795 | $ 39,015 |
| Effective income tax rate | 28.2% | 35.7% |

In 2005, Toromont recognized an $8,700 reduction of tax reserves following a comprehensive review of current items. This review was triggered by the successful closure of several outstanding matters including the completion by federal, provincial and state taxing authorities of their review of filings for the three successive tax years up to and including the period ended December 31, 2002.

The income tax effects of temporary differences that gave rise to significant portions of the future income tax assets and future income tax liabilities were as follows:

| | 2005 | 2004 |
|---|---|---|
| **Current future income tax assets** | | |
| Accrued liabilities | $ 10,844 | $ 9,652 |
| Deferred revenue | 2,467 | 3,258 |
| Accounts receivable | 2,228 | 2,075 |
| Inventories | 2,962 | (2,269) |
| | $ 18,501 | $ 12,716 |
| **Non-current future income tax assets** | | |
| Capital assets | $ (5,467) | $ – |
| Other | 6,593 | – |
| | $ 1,126 | $ – |
| **Non-current future income tax liabilities** | | |
| Capital assets | $ – | $ 11,952 |
| Other | – | (3,513) |
| | $ – | $ 8,439 |

## 17 EARNINGS PER SHARE

The following table sets forth the computation of basic and diluted earnings per share.

| | 2005 | 2004 |
|---|---|---|
| Earnings from continuing operations | $ 78,392 | $ 70,140 |
| Earnings from discontinued operations | 570 | 378 |
| Net earnings available to common shareholders | $ 78,962 | $ 70,518 |
| Weighted average common shares outstanding | 63,310,574 | 63,462,156 |
| Dilutive effect of stock option conversion | 1,110,059 | 1,193,443 |
| Diluted weighted average common shares outstanding | 64,420,633 | 64,655,599 |
| **Basic earnings per share** | | |
| Continuing operations | $ 1.24 | $ 1.10 |
| Discontinued operations | 0.01 | 0.01 |
| | $ 1.25 | $ 1.11 |
| **Diluted earnings per share** | | |
| Continuing operations | $ 1.22 | $ 1.08 |
| Discontinued operations | 0.01 | 0.01 |
| | $ 1.23 | $ 1.09 |

## 18 COMMITMENTS

Certain land, buildings and equipment are leased under several non-cancellable operating leases that require minimum annual payments as follows:

| | |
|---|---|
| 2006 | $ 4,764 |
| 2007 | 3,199 |
| 2008 | 2,329 |
| 2009 | 1,494 |
| 2010 | 589 |
| 2011 and thereafter | 1,219 |
| | $ 13,594 |

## 19 ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

Accounts payable and accrued liabilities included $74.1 million in deferred revenue (2004 – $31.0 million).

## 20 SEGMENTED INFORMATION

The Company has two reportable operating segments, each supported by the corporate office. The business segments are strategic business units that offer different products and services, and each is managed separately. The corporate office provides finance, treasury, legal, human resources and other administrative support to the business segments. Corporate overheads are allocated to the business segments based on operating income.

The Equipment Group includes one of the world's largest Caterpillar dealerships by revenue and geographic territory in addition to industry leading rental operations. The Compression Group is a North American leader specializing in the design, engineering, fabrication and installation of compression systems for natural gas, coal-bed methane, fuel gas and carbon dioxide in addition to process systems and industrial and recreational refrigeration systems. Both Groups offer comprehensive product support capabilities.

The accounting policies of the reportable operating segments are the same as those described in the summary of significant accounting policies. Each reportable operating segment's performance is measured based on operating income. No reportable operating segment is reliant on any single external customer.

| | Equipment Group | | Compression Group | | Consolidated | |
|---|---|---|---|---|---|---|
| | 2005 | 2004 | 2005 | 2004 | 2005 | 2004 |
| Revenues | $ 913,945 | $ 821,039 | $ 685,847 | $ 613,717 | $ 1,599,792 | $ 1,434,756 |
| Operating income before impairment charges | $ 80,596 | $ 65,842 | $ 56,583 | $ 53,515 | $ 137,179 | $ 119,357 |
| Asset impairment charges | $ 17,800 | $ – | $ – | $ – | $ 17,800 | $ – |
| Operating Income | $ 62,796 | $ 65,842 | $ 56,583 | $ 53,515 | $ 119,379 | $ 119,357 |
| Interest expense | | | | | 12,977 | 12,138 |
| Interest and investment income | | | | | (2,785) | (1,936) |
| Income taxes | | | | | 30,795 | 39,015 |
| Net earnings from continuing operations | | | | | $ 78,392 | $ 70,140 |

### Selected Balance Sheet Information

| | Equipment Group | | Compression Group | | Consolidated | |
|---|---|---|---|---|---|---|
| | 2005 | 2004 | 2005 | 2004 | 2005 | 2004 |
| Identifiable assets | $ 660,028 | $ 641,820 | $ 418,192 | $ 311,414 | $ 1,078,220 | $ 953,234 |
| Corporate assets | | | | | 65,752 | $ 9,203 |
| Total assets | | | | | $ 1,143,972 | $ 962,437 |
| Capital expenditures | $ 65,312 | $ 52,349 | $ 7,501 | $ 13,259 | $ 72,813 | $ 65,608 |
| Depreciation | $ 37,837 | $ 33,738 | $ 8,757 | $ 9,018 | $ 46,594 | $ 42,756 |

Operations are based primarily in Canada and the United States. The following summarizes the final destination of revenues to customers and the assets held in each geographic segment.

| | 2005 | 2004 |
|---|---|---|
| Revenues | | |
| Canada | $ 1,381,629 | $ 1,236,616 |
| United States | 148,124 | 119,173 |
| International | 70,039 | 78,967 |
| | $ 1,599,792 | $ 1,434,756 |
| Capital Assets and Goodwill | | |
| Canada | $ 305,431 | $ 323,081 |
| United States | 12,469 | 9,364 |
| International | 307 | – |
| | $ 318,207 | $ 332,445 |

## 21 ECONOMIC RELATIONSHIP

The Company, through its Equipment Group, sells and services heavy equipment and related parts. Distribution agreements are maintained with several equipment manufacturers, of which the most significant are with subsidiaries of Caterpillar Inc. The distribution and servicing of Caterpillar products account for the major portion of the Equipment Group's operations. Toromont has had a strong relationship with Caterpillar since 1993.

# TEN-YEAR FINANCIAL REVIEW

| For the years ended December 31 ($ thousands except where otherwise indicated) | 2005 | 2004 (1) | 2003 (2) |
|---|---|---|---|
| **Operating Results** | | | |
| Revenues | 1,599,792 | 1,434,756 | 1,299,389 |
| Net earnings before unusual items | 78,962 | 70,518 | 58,693 |
| Unusual items | – | – | – |
| Net earnings | 78,962 | 70,518 | 58,693 |
| Net interest (income) expense | 10,192 | 10,202 | 10,608 |
| Capital expenditures | 72,813 | 65,608 | 72,922 |
| Dividends declared | 20,280 | 16,486 | 13,319 |
| **Financial Position** | | | |
| Working capital | 410,990 | 263,294 | 203,577 |
| Capital assets | 283,407 | 297,645 | 293,211 |
| Total assets | 1,143,972 | 962,437 | 856,176 |
| Long-term debt | 241,265 | 166,508 | 159,694 |
| Shareholders' equity | 481,812 | 415,855 | 376,837 |
| **Financial Ratios** | | | |
| Working capital | 2.1:1 | 1.8:1 | 1.7:1 |
| Return on opening shareholders' equity (%) | 18.9 | 18.7 | 17.5 |
| Total debt net of cash to shareholders' equity | .4:1 | .4:1 | .5:1 |
| **Per Share Data ($)** | | | |
| Net earnings before unusual items | 1.25 | 1.11 | 0.93 |
| Unusual items | – | – | – |
| Net earnings | 1.25 | 1.11 | 0.93 |
| Dividends declared | 0.32 | 0.26 | 0.21 |
| Book value | 7.57 | 6.59 | 5.93 |
| Shares outstanding at year end | 63,624,936 | 63,082,586 | 63,563,246 |
| Price range | | | |
| High | 25.68 | 20.85 | 16.73 |
| Low | 20.05 | 15.88 | 9.88 |
| Close | 25.40 | 20.72 | 16.53 |

Notes

(1) Results prior to 2004 have not been restated to conform with the current year's presentation.

(2) Includes the results of Energy Industries from January 1, 2003.

(3) Includes the results of Powell Equipment Limited from July 1, 2001.

(4) Includes the results of Newfoundland and Labrador Caterpillar Dealership from November 1, 1996.

| 2002 | 2001 (3) | 2000 | 1999 | 1998 | 1997 | 1996 (4) |
|---|---|---|---|---|---|---|
| 1,076,930 | 911,005 | 800,464 | 723,937 | 683,482 | 684,716 | 542,477 |
| 40,457 | 43,700 | 32,345 | 32,057 | 28,242 | 25,674 | 21,905 |
| – | – | – | – | 9,946 | 35,159 | – |
| 40,457 | 43,700 | 32,345 | 32,057 | 38,188 | 60,833 | 21,905 |
| 7,136 | (6,913) | 3,797 | (1,774) | 1,910 | 2,424 | 5,213 |
| 53,042 | 77,394 | 57,968 | 52,146 | 36,307 | 29,627 | 20,632 |
| 11,541 | 10,646 | 9,257 | 8,213 | 7,650 | 5,859 | 4,382 |
| 213,222 | 218,132 | 165,098 | 183,922 | 144,109 | 138,458 | 96,294 |
| 258,764 | 252,104 | 206,526 | 138,499 | 106,628 | 84,831 | 68,132 |
| 771,902 | 720,702 | 613,787 | 531,201 | 442,972 | 434,341 | 318,287 |
| 156,479 | 171,970 | 157,187 | 120,000 | 60,000 | 60,000 | 60,806 |
| 335,316 | 314,248 | 218,213 | 203,062 | 183,596 | 155,821 | 100,305 |
| 1.8:1 | 2.0:1 | 1.7:1 | 1.9:1 | 1.8:1 | 1.7:1 | 1.6:1 |
| 12.9 | 17.1 | 15.9 | 17.5 | 24.5 | 60.6 | 27.5 |
| .4:1 | .5:1 | .7:1 | .6:1 | .3:1 | .4:1 | .6:1 |
| 0.63 | 0.71 | 0.56 | 0.55 | 0.48 | 0.44 | 0.38 |
| – | – | – | – | 0.17 | 0.60 | – |
| 0.63 | 0.71 | 0.56 | 0.55 | 0.65 | 1.04 | 0.38 |
| 0.18 | 0.17 | 0.16 | 0.14 | 0.13 | 0.10 | 0.08 |
| 5.28 | 4.90 | 3.77 | 3.47 | 3.12 | 2.65 | 1.72 |
| 63,455,146 | 64,194,946 | 57,951,396 | 58,576,196 | 58,916,420 | 58,797,736 | 58,536,536 |
| 13.25 | 13.10 | 10.38 | 9.95 | 11.50 | 9.20 | 6.82 |
| 9.25 | 7.63 | 6.90 | 6.88 | 7.13 | 6.34 | 3.57 |
| 10.33 | 10.24 | 8.75 | 8.13 | 7.88 | 8.25 | 6.69 |

# CORPORATE GOVERNANCE OVERVIEW

A strong and effective corporate governance program continues to be a principal priority for Toromont. The Nominating and Corporate Governance Committee, on behalf of the Board, establishes and monitors the governance program and its effectiveness. The Company's corporate governance structure and procedures are founded on our Code of Business Conduct that applies to all directors, officers and employees. Our governance program includes the activities of the Board of Directors, who are elected by and are accountable to the shareholders, and the activities of management who are appointed by the Board and are charged with the day-to-day management of the Company.

Toromont regularly reviews and enhances its governance practices, monitoring and, where appropriate, responding to regulatory developments and other applicable legislation.

The Company's corporate governance program is in compliance with National Policy 58 -201 – *Corporate Governance Guidelines* and Multilateral Instrument 52-110 – *Audit Committees*.

## BOARD OF DIRECTORS

The role of the Board of Directors, its activities and responsibilities are documented and are regularly, and at least annually, assessed, as are the terms of reference for each of the committees of the Board, for the Lead Director, for the Chairman and for the President and Chief Executive Officer, inclusive of scope and limits of authority of management. The Board acts in a supervisory role and any responsibilities not delegated to management remain with the Board. The Board's supervisory role includes such matters as strategic planning, identification and management of risks, succession planning, communication policy, internal controls and governance.

The Lead Director is an independent director appointed annually by the independent directors of the Board to facilitate the Board's functioning autonomously from management. The Lead Director serves as a non-partisan contact for other directors on matters not deemed appropriate to be discussed initially with the Chairman or in situations where the Chairman is not available. The Lead Director is available to counsel the Chairman on matters appropriate for review in advance of discussion with the full Board of Directors. The Lead Director chairs a session at each Board meeting during which only independent directors are present. The Chairman, Mr. Ogilvie, retired as an officer of Toromont on May 31, 2005. This will further increase the independence of the Board.

## COMMITTEE STRUCTURE AND MANDATES

Committees of the Board are an integral part of the Company's governance structure. Three committees have been established with a view to allocating expertise and resources to particular areas, and to enhance the quality of discussion at Board meetings. The committees facilitate Board decision-making by providing recommendations to the Board on matters within their respective responsibilities.

All committees are comprised solely of directors who are independent of management. A summary of the responsibilities and the membership of the committees follow.

The Nominating and Corporate Governance Committee: Principal responsibilities are reviewing and making recommendations as to all matters relating to effective corporate governance. The committee is responsible for assessing effectiveness of the Board, its size and composition, its committees, director compensation, the Board's relationship to management and individual performance and contribution of its directors. The committee is responsible for identification and recruitment of new directors and new director orientation.

The Audit Committee: Principal duties include oversight responsibility for financial statements and related disclosures, reports to shareholders and other related communications, establishment of appropriate financial policies, the integrity of accounting systems and internal controls, legal compliance on ethics programs established by management, the approval of all audit and non-audit services provided by the independent auditors and consultation with the auditors independent of management and overseeing the work of the auditors.

The Human Resources and Compensation Committee: Principal responsibilities are compensation of executive officers and other senior management, short- and long-term incentive programs, pension and other benefit plans, executive officer appointments, evaluation of performance of the President and Chief Executive Officer, succession planning and executive development. The committee also oversees compliance with the Company's Code of Business Conduct and the health, safety and environment program.

# CORPORATE INFORMATION

## EQUIPMENT GROUP

**Toromont CAT**
3131 Highway 7 West
P.O. Box 5511
Concord, Ontario L4K 1B7
T: 416 667 5511
F: 416 667 5555
*S.J. Medhurst*
*President*

**Battlefield – The CAT Rental Store**
880 South Service Road
Stoney Creek, Ontario L8H 7S8
T: 905 577 7777
F: 905 643 6008
*R.B. Casson*
*President*

## COMPRESSION GROUP

**Toromont Energy Systems Inc.**
10121 Barlow Trail Northeast
Calgary, Alberta T3J 3C6
T: 403 291 3438
F: 403 291 3443
*D.F. Duncan*
*President*

**Toromont Energy Systems Inc.**
10815 Telge Road
Houston, Texas 77095
T: 281 345 9300
F: 281 345 7434
*D.F. Duncan*
*President*

**CIMCO Refrigeration**
65 Villiers Street
Toronto, Ontario M5A 3S1
T: 416 465 7581
F: 416 465 8815
*S.D. McLeod*
*President*

**CIMCO Refrigeration Inc.**
2502 Commercial Park Drive
Mobile, Alabama 36606
T: 251 471 2426
F: 251 476 7337
*S.D. McLeod*
*President*

**Aero Tech Manufacturing Inc.**
395 West 1100 North
North Salt Lake, Utah 84054
T: 801 292 0493
F: 801 292 9908
*T.J. Riley*
*President*

## ANNUAL AND SPECIAL MEETING

The Annual and Special Meeting of the Shareholders of Toromont Industries Ltd. will be held at 10:00 a.m. on Thursday, April 20, 2006 in the Auditorium, Toronto Stock Exchange Centre, The Exchange Tower, 130 King Street West, Toronto, Ontario.

# BOARD OF DIRECTORS AND OFFICERS

**Robert M. Franklin ● ▲**
Chairman, Human Resources and Compensation Committee
Director since 1994
Mr. Franklin was Chairman of the Board and a director of Placer Dome Inc. (an international gold mining company). He currently serves on the Board of Directors of Barrick Gold Corporation, Royster-Clark Ltd. and Great Lakes Carbon Corporation.

**Ronald G. Gage**, FCA ■ ●
Chairman, Nominating and Corporate Governance Committee
Director since 2000
Mr. Gage, a Fellow of The Institute of Chartered Accountants of Ontario, was Chairman and Chief Executive officer of Ernst & Young LLP, Canada from 1993 to 1999. He is a director of AIM Canada Fund Inc., AIM Global Fund Inc. and easyhome Ltd. Mr. Gage is also a member of the Canadian Public Accountability Board.

**David A. Galloway ■ ▲**
Director since 2002
Mr. Galloway was President and Chief Executive Officer of Torstar Corporation from 1988 until his retirement in May 2002. He is Chairman of the Board and a director of Bank of Montreal. He also serves on the Board of Directors of Bankmont Financial Corp., E.W. Scripps Company and Hudson's Bay Company.

**Wayne S. Hill**
Director since 1988
Mr. Hill is Executive Vice President of the Company. Mr. Hill joined Toromont in 1985 as Vice President, Finance and Chief Financial Officer and became Executive Vice President in February 2002.

**H. Stanley Marshall ▲**
Director since 1998
Mr. Marshall is President and Chief Executive Officer and a director of Fortis Inc. and all of its subsidiaries (an international electric utility holding company).

**John S. McCallum ■ ●**
Lead Director and Chairman, Audit Committee
Director since 1985
Mr. McCallum is a Professor of Finance in the Faculty of Management at the University of Manitoba. He is also a director of IGM Financial Inc., Wawanesa Mutual Insurance Company, Wawanesa General Insurance Company, Wawanesa Life Insurance Company and Fortis Inc.

**Robert M. Ogilvie**
Director since 1986
Mr. Ogilvie is Chairman of the Board. Mr. Ogilvie joined Toromont as President in 1985 and was Chairman, President and Chief Executive Officer of the Company from 1987 to 1997. He was Chairman and Chief Executive Officer of the Company from 1997 to 2002, at which time he became Executive Chairman of the Board.

**Hugo T. Sørensen**
Director since 1998
Mr. Sørensen is President and Chief Executive Officer of the Company. Mr. Sørensen joined Toromont as President in 1997 and was President and Chief Operating Officer from 1998 to 2002, at which time he was appointed President and Chief Executive Officer.

## OFFICERS

Hugo T. Sørensen
President and Chief Executive Officer

Wayne S. Hill
Executive Vice President

Paul R. Jewer
Vice President, Finance and Chief Financial Officer

Michael P. Cuddy
Vice President and Chief Information Officer

David C. Wetherald
Vice President, General Counsel & Secretary

Eric C. Breitkreutz
Vice President, Human Resources

■ Member of Nominating and Corporate Governance Committee
● Member of Audit Committee
▲ Member of Human Resources and Compensation Committee

back row **John McCallum, Stanley Marshall, Robert Franklin, Ronald Gage, David Galloway**
front row **Hugo Sørensen, Wayne Hill, Robert Ogilvie**

TOROMONT

**How to get in touch with us**
Tel: 416 667 5511
Fax: 416 667 5555
E-mail: investorrelations@toromont.com
www.toromont.com

**How to reach our transfer agent and registrar**
Investors are encouraged to contact CIBC Mellon Trust for information regarding their security holdings.

**CIBC Mellon Trust**
P.O. Box 7010
Adelaide Street Postal Station
Toronto ON M5C 2W9
Answer Line: 416 643 5550 or
Toll-Free North America: 1 800 387 0825
E-mail: inquiries@cibcmellon.com
www.cibcmellon.com

**Common Shares**
Listed on the Toronto Stock Exchange
Stock Symbol – TIH

**Toromont Industries Ltd.**
Corporate Office
3131 Highway 7 West
P.O. Box 5511
Concord ON L4K 1B7