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Morneau Shepell Inc. ("Morneau Shepell" or the "Company") was incorporated pursuant to the laws of the Province of Ontario on October 19, 2010, and as of January 1, 2011, is the successor to Morneau Sobeco Income Fund (the "Fund").

This Management's Discussion and Analysis ("MD&A") covers the year ended December 31, 2013 and should be read in conjunction with the accompanying consolidated financial statements of Morneau Shepell and notes thereto for the years ended December 31, 2013 and 2012.

All financial information is presented in Canadian dollars and in accordance with International Financial Reporting Standards, unless otherwise noted. Certain totals, subtotals and percentages may not reconcile due to rounding.

This MD&A contains "forward-looking statements" within the meaning of applicable securities laws, such as statements concerning anticipated future events, results, circumstances, performance or expectations that are not historical facts. They are based on certain factors and assumptions, including expected growth, results of operations, business prospects and opportunities. Use of words such as "may", "will", "expect", "believe", or other words of similar effect may indicate a "forward-looking" statement. These statements are not guarantees of future performance and are subject to numerous risks and uncertainties, including those described in our publicly filed documents (available on SEDAR at www.sedar.com) and in this MD&A under the heading "Risks and Uncertainties". Those risks and uncertainties include the ability to maintain profitability and manage growth, ability to pay dividends, reliance on information systems and technology, reputational risk, dependence on key clients, reliance on key professionals and general economic conditions. Many of these risks and uncertainties can affect our actual results and could cause our actual results to differ materially from those expressed or implied in any forward-looking statement made by us or on our behalf. Given these risks and uncertainties, investors should not place undue reliance on forward-looking statements as a prediction of actual results. All forward-looking statements in this MD&A are qualified by these cautionary statements. These statements are made as of the date of this MD&A and, except as required by applicable law, we undertake no obligation to publicly update or revise any forward-looking statement, whether as a result of new information, future events or otherwise. Additionally, we undertake no obligation to comment on analyses, expectations or statements made by third parties in respect of us, our financial or operating results or our securities.

To assist investors in assessing our financial performance, this discussion also makes reference to certain non-IFRS measures such as EBITDA, adjusted EBITDA, EBITDA margin, adjusted EBITDA margin, Free Cash Flow, Normalized Free Cash Flow, Normalized Payout Ratio and twelve-month rolling Normalized Payout Ratio. EBITDA and adjusted EBITDA are intended to represent an indication of Morneau Shepell's capacity to generate profit from operations before taking into account management's financing decisions and costs of consuming tangible and intangible capital assets, which vary according to their vintage, technological currency, and management's estimate of their useful life. Accordingly, EBITDA comprises profit before finance costs, income tax expenses, depreciation and amortization, while Adjusted EBITDA represents EBITDA before taking into account certain unusual expenditures. We believe both EBITDA and Adjusted EBITDA are useful measures in evaluating our performance. We utilize them to monitor compliance with debt covenants and to make decisions related to dividends to shareholders rather than profit due to the significant amount of amortization expense related to our intangible assets acquired from acquisitions. We also believe that Free Cash Flow, Normalized Free Cash Flow and Normalized Payout Ratio are useful supplemental measures of Morneau Shepell's ability to generate cash after deducting capital expenditures required to maintain or expand the business. These ratios, however, are non-IFRS measures and therefore, should not be seen as a substitute for cash flow from operating activities. Free Cash Flow is defined as cash provided by operating activities adjusted for capital expenditures. Normalized Free Cash Flow is defined as cash provided by operating activities, adjusted for changes in non-cash operating working capital, capital expenditures, current income taxes (net of income taxes paid) and certain unusual expenditures.

Non-IFRS measures do not have any standard meaning prescribed by IFRS and therefore may not be comparable to similar measures presented by other issuers.

OUTSTANDING SHARE DATA

The Company is authorized to issue an unlimited number of common shares and 10 million preferred shares. Each common share entitles the holder to one vote at all meetings of shareholders and represents an interest in dividends declared by the Company and an undivided interest in the net assets of the Company. As at March 5, 2014, Morneau Shepell had 47,962,793 common shares, nil preferred shares and $75,000 aggregate principal amount of 5.75% convertible debentures outstanding. In the event all of the outstanding 5.75% convertible debentures are converted into common shares of the Company by the holders prior to their maturity date, the total number of common shares issuable will be approximately 5,000,000.

BUSINESS OVERVIEW

Morneau Shepell is the largest Canadian firm providing health and productivity, administrative and retirement solutions. We deliver solutions to assist employers in managing the financial security, health and productivity of their employees. With approximately 3,200 employees in offices across North America, we offer services to over 9,000 organizations in Canada, the United States and around the globe directly and through our distribution channel partners.

We derive our revenue primarily from fees charged to clients for consulting engagements, outsourcing engagements, employee and family assistance programs and organizational health solution services.

Fees from consulting engagements are charged based on billable hours or on a fee-for-service basis. In some cases, consulting engagements may be billed on a fixed-fee basis, although these engagements are typically much smaller and the services are delivered over a shorter period of time. For some benefits consulting assignments which involve the purchase of an insurance policy underwritten by an insurance company, we may be paid commissions (in lieu of fees) by the client's insurance company, which is a common practice in the industry. These commissions are based on a percentage of the premiums paid by the client to the insurance company and our policy is to disclose them to our client. We assume no underwriting risk as the insurance policy is underwritten by the insurance company. In addition, we earn interest income from our cash balances which is included in other revenue.

Our Administrative Solutions practice is characterized by fixed contracts, which typically have three-year to five-year terms. Most outsourcing contracts contain an upfront implementation fee and an ongoing monthly service fee. Implementations usually take three to twelve months and involve transferring the administration of a client's pension and/or benefits plans onto our systems, tailoring our systems and training our employees. Additional services provided that are outside the scope of the outsourcing contract are usually paid on a fee-for-service basis.

In the billing for Employee Support Solutions ("ESS") services, a portion of the ESS client agreements require payment of a minimum retainer and incremental usage-based fees. The remainder of the ESS agreements are billed based on an actual usage or fixed fees. Most ESS agreements may be terminated by the client upon 30 to 60 days' notice to us, however, it is typical for ESS agreements to continue for multiple years and many automatically renew on an annual basis.

Fees from Organizational Health Solutions ("OHS") services, such as attendance support and disability management are generally based on negotiated fees or a formula tied to the nature of the service being provided. Like most ESS agreements, most workplace health and productivity agreements may be terminated by the client upon 30 to 60 days' notice to us; however, it is typical for these agreements to continue for multiple years and many automatically renew on an annual basis.

Our largest operating expense is compensation and related costs. This includes salaries, annual performance-based bonuses, benefits, payroll taxes, independent service providers and temporary staffing services.

The remaining operating expenses include rent and occupancy costs, technology costs (including equipment leases, telecommunications, and software licenses and maintenance), non-recoverable client service costs (such as printing and travel), training, marketing, office costs, professional services and insurance.

2013 SUMMARY AND OUTLOOK

In thousands of dollars	**Three months ended December 31, 2013**	**Three months ended December 31, 2012**	**Year ended December 31, 2013**	**Year ended December 31, 2012**
Revenue	$118,570	$107,258	$471,154	$419,346
Adjusted EBITDA	$20,217	$18,843	$86,528	$78,135
Adjusted EBITDA margin	17.1%	17.6%	18.4%	18.6%
Normalized Free Cash Flow	$15,939	$13,061	$53,979	$53,314
Profit	$(11,279)	$4,234	$10,445	$21,034

Fourth quarter:

We continued to experience strong revenue and adjusted EBITDA growth in the fourth quarter of 2013 versus the comparative quarter in 2012. Revenue increased by 10.5% and Adjusted EBITDA continued to improve, increasing to $20.2 million versus $18.8 million in the comparative period.

During the fourth quarter we completed a renewal of our credit agreement ("amended agreement") under similar terms of the previous facility. The amended agreement matures on November 29, 2017 and provides for a revolving facility of $250.0 million (including a swing line of $7.0 million). The completion of this re-financing one year in advance of maturity provides us the flexibility to pursue acquisition opportunities as they arise.

Our annual impairment test resulted in an impairment charge to the OHS cash generating unit ("CGU") of $16.7 million. The impairment loss is primarily related to the Health Clinics sub-service line within OHS, and is due to reduced expectations for increasing the operating profit. The Company's long-term strategy for OHS is to focus on its Absence Management sub-service line. Absence Management is growing organically and via acquisitions and has operating margins in-line with the Company's long-term strategic plan. The Company's investment in Shepell.fgi (which for clarity includes ESS and OHS CGUs) continues to yield a positive return for the Company. The recoverable amount of the Company's ESS CGU is well in excess of its carrying amount.

Highlights of 2013 and subsequent events include:

- Revenue growth in all of our business practices during 2013, contributing to an overall revenue increase in 2013 of 12.4% versus the comparative year. Excluding acquisitions, organic growth was 6.4%.

- Adjusted EBITDA increased by $8.4 million to $86.5 million.

- Subsequent to year end, in continuing to strengthen our workers' compensation practice in the Absence Management Services sub-service line within the OHS CGU, we completed the acquisition of Groupe AST (1993) Inc. ("Groupe AST") from ADP Canada Co. This acquisition complements our existing service offering and expands our market leadership position as the largest Canadian provider of workers' compensation services and integrated absence management solutions. Through this acquisition, the Company gains approximately 150 employees, 12,000 clients and 18 prevention mutual groups which represents an estimated $20.0 million in additional annual revenue to the Company. The assets of Groupe AST were acquired for cash consideration of $27.0 million and $5.0 million in vendor take-back notes.

- We continue to execute on our growth strategy of expanding organically and via acquisitions. During the year we completed two small acquisitions – Dion, Durrell + Associates Inc. workers' compensation practice ("Dion Durrell Workers' Compensation") and Collage Pediatric Therapy Centre Inc. ("Collage Pediatric Therapy"). With the Dion Durrell Workers' Compensation acquisition, we are expanding our national workers' compensation practice (a component of our Absence Management sub-service line) and our market presence where we see a growing demand for workers' compensation services. The Collage Pediatric Therapy acquisition complements our existing Children's Support Solutions portfolio, and expands our market presence in Ontario and Quebec.

- The integration of Mercer Canada's Pension and Benefits Outsourcing ("Mercer Canada Outsourcing") operations with our existing Administrative Solutions practice is going well and continues on schedule.

- Going forward, we expect our future growth to be in-line with our longer term historical performance. We also expect that our continued investment in our business, our new acquisitions, capital structure, established business relationships and prospective client base will continue to yield positive results for the Company.

Results of Operations	**Three Months Ended December 31**		**Year Ended December 31**	
Selected Consolidated Financial Information	**2013**	**2012**	**2013**	**2012**
(In thousands of dollars except per share amounts)				
Revenue	$118,570	$107,258	$471,154	$419,346
Deduct:				
Salary, benefits and contractor expenses	83,573	76,620	320,525	287,485
Other operating expenses	20,799	17,896	74,346	64,757
Finance costs	3,566	3,474	14,098	14,036
Depreciation, amortization and impairment losses	24,207	6,379	44,385	24,689
Income tax expenses	(2,296)	2,155	7,355	10,845
Bargain purchase gain on business acquisition	–	(3,500)	–	(3,500)
Profit (loss) for the period	**(11,279)**	**4,234**	**10,445**	**21,034**
Add:				
Finance costs	3,566	3,474	14,098	14,036
Depreciation and amortization	7,507	6,379	27,685	24,689
Income tax expenses	(2,296)	2,155	7,355	10,845
EBITDA[1]	$(2,502)	$16,242	$59,583	$70,604
Adjustments:				
Reorganization and operational effectiveness initiatives	1,894	4,663	2,950	6,497
Sublease loss provision	2,000	–	2,000	–
Impairment charges related to OHS	16,700	–	16,700	–
Business acquisitions: bargain purchase gain and costs	–	(3,101)	–	(3,101)
Provision for E-commerce refundable tax credit	–	–	–	2,155
Enterprise software replacement – expenses	–	490	–	1,431
Mercer Canada Outsourcing conversion costs	2,125	549	5,295	549
Adjusted EBITDA	**$ 20,217**	**$18,843**	**$86,528**	**$78,135**
EBITDA margin	(2.1%)	15.1%	12.6%	16.8%
Adjusted EBITDA margin	17.1%	17.6%	18.4%	18.6%
Cash provided by operating activities	$15,549	$14,876	$39,478	$36,789
Deduct: Capital expenditures [2]	(5,961)	(4,381)	(21,779)	(14,472)
Free Cash Flow [3]	**9,588**	**10,495**	**17,699**	**22,317**
Add (deduct):				
Changes in non-cash operating working capital	(585)	(3,744)	23,920	21,554
Enterprise software replacement – capital	–	457	–	2,149
Mercer Canada Outsourcing conversion – capital	995	–	3,858	–
Current income taxes, net of income taxes paid	1,922	(248)	257	(3,737)
Adjustments to EBITDA, per above [6]	4,019	6,101	8,245	11,031
Normalized Free Cash Flow [4]	**$15,939**	**$13,061**	**$53,979**	**$53,314**
Earnings per Share (basic)	$(0.23)	$0.09	$0.21	$0.43
Earnings per Share (diluted)	$(0.23)	$0.09	$0.21	$0.43
EBITDA per Share (basic)	$(0.05)	$0.33	$1.22	$1.46
Adjusted EBITDA per Share (basic)	$0.41	$0.39	$1.78	$1.61
Normalized Payout Ratio [5]	58.7%	71.6%	69.3%	70.1%
Twelve-month rolling Normalized Payout Ratio	69.3%	70.1%	69.3%	70.1%

Footnotes:

(1) "EBITDA" is defined as profit before finance costs, income tax expenses, depreciation and amortization.

(2) "Capital Expenditures" includes capital assets and intangible assets but excludes additions to intangible assets acquired through business acquisitions, and is presented net of disposals.

(3) "Free Cash Flow" is defined as cash provided by operating activities adjusted for capital expenditures.

(4) "Normalized Free Cash Flow" is defined as cash provided by operating activities, adjusted for changes in non-cash operating working capital, capital expenditures, current income taxes (net of income taxes paid) and certain unusual expenditures.

(5) "Normalized Payout Ratio" is defined as dividends declared divided by Normalized Free Cash Flow.

(6) Adjustments to EBITDA do not include the sublease loss provision, impairment charges related to OHS and the bargain purchase gain on business acquisition (2012 comparative). These amounts have been excluded as they have already been added back in cash from operating activities before the change in non- cash operating working capital.

ANALYSIS OF FOURTH QUARTER 2013 AND 2012 RESULTS

Revenue

Revenue for the three months ended December 31, 2013 increased by $11.3 million, or 10.5%, to $118.6 million compared to $107.3 million for the same period in 2012. The Mercer Canada Outsourcing acquisition contributed to an increase in revenue of 2.0% over the comparative quarter in 2012. The other incremental revenue of 8.5% represents year over year growth which came from all four lines of business with the Administrative Solutions, and Employee Support Solutions lines of business contributing the largest percentage of the increase. This growth was a result of the commencement of service for outsourcing contracts secured in prior quarters, increased mandates from existing clients and new business wins.

Salary, Benefits and Contractor Expenses

Salary, benefits and contractor expenses for the three months ended December 31, 2013 increased by $7.0 million, or 9.1%, to $83.6 million compared to $76.6 million for the same period in 2012. This increase is attributable to the Mercer Canada Outsourcing acquisition which resulted in an incremental compensation expense, including conversion costs, of $1.7 million. The residual increase of $5.3 million was primarily attributable to general increases to support the Company's continued growth and variable compensation expense adjustments.

Other Operating Expenses

Other operating expenses for the three months ended December 31, 2013 increased by $2.9 million, or 16.2%, to $20.8 million compared to $17.9 million for the same period in 2012. The increase is due to additional expenses resulting from the Mercer Canada Outsourcing acquisition, including conversion costs, of $0.6 million that were not in the comparative period. In addition, the Company recorded a $2.0 million sublease loss provision in the fourth quarter (see Adjusted EBITDA and EBITDA section below). The residual increase of $0.3 million reflects general increases required to support business growth.

Finance Costs

Finance costs for the three months ended December 31, 2013 increased by $0.1 million, or 2.6%, to $3.6 million compared to $3.5 million for the same period in 2012. The increase is primarily due to higher interest on the Company's credit facility due to increased borrowing compared to the same period in 2012.

Depreciation, Amortization and Impairment Losses

Depreciation and amortization for the three months ended December 31, 2013 increased by $1.1 million, or 17.7%, to $7.5 million compared to $6.4 million for the same period in 2012. This increase is attributable to increased depreciation and amortization expense from the Mercer Canada Outsourcing acquisition of $0.4 million and increased depreciation and amortization expense of $0.7 million on capital expenditures required to support business growth.

As discussed in the Summary and Outlook section the Company also recorded impairment losses of $16.7 million during the fourth quarter as part of its annual impairment testing under IAS 36 "Impairment of assets."

Income Tax Expenses (Recovery)

Income tax expenses decreased by $4.4 million, or 206.5%, to an income tax recovery of $2.3 million, compared to a $2.2 million expense for the same period in 2012. The decrease was primarily due to lower profit from operations before income taxes and impairment losses, and a reduction in deferred income tax expense as a result of recording impairment losses of $16.7 million as discussed in the Summary and Outlook section.

Profit (Loss) for the Period

As a result of the changes noted above, the loss for the three months ended December 31, 2013 was $11.3 million compared to a $4.2 million profit for the same period in 2012.

Key Financial Measures: EBITDA, Adjusted EBITDA, Free Cash Flow and Normalized Free Cash Flow

Adjusted EBITDA and EBITDA

Adjusted EBITDA increased by $1.4 million, or 7.3%, to $20.2 million compared to $18.8 million for the same period in 2012. The increase is primarily due to growth in revenue of $11.3 million, partially offset by an increase in salaries and other operating expenses of $9.5 million after EBITDA adjustments. These adjusted EBITDA items do not constitute a part of the Company's on-going operating expenses. Below is a description of the fourth quarter ended December 31, 2013 adjustments:

- Reorganization and operational effectiveness initiatives represent costs incurred as part of a major cost savings project. This project began in 2012 and was completed by the end of 2013.

- The sublease loss provision mainly represents costs to be incurred related to the consolidation of the Vancouver office locations and the consolidation of the downtown Toronto office locations. These are the final two groups of offices that remain to be consolidated from the Shepell.fgi and Mercer acquisitions. Consolidation of these offices will maximize the utilization of our office spaces.

- The impairment charges related to goodwill, intangibles and capital assets occurred due to circumstances explained in the Summary and Outlook section.

- Mercer Canada Outsourcing conversion costs represent systems and service improvements required to support the clients acquired in the acquisition in November, 2012. The process commenced immediately after the acquisition was completed and is expected to take approximately three years.

EBITDA decreased by $18.7 million, or (115.4 %), to $(2.5) million compared to $16.2 million for the same period in 2012.

Free Cash Flow

Free Cash Flow for the three months ended December 31, 2013 decreased by $0.9 million to $9.6 million compared to $10.5 million for the same period in 2012. The decrease is primarily due to higher capital expenditures of $1.6 million (see liquidity and capital resources section below), which were partially offset by higher cash provided by operating activities of $0.7 million.

Normalized Free Cash Flow

Normalized Free Cash Flow for the three months ended December 31, 2013 increased by $2.9 million to $15.9 million compared to $13.1 million for the same period in 2012. The increase is primarily a result of an increase in cash provided by operating activities, before non-cash operating working capital and EBITDA adjustments, of $1.4 million and lower current taxes expense for this quarter of $2.6 million. This is partially offset by higher capital expenditures of $1.0 million, once adjusted for the Mercer Canada Outsourcing and Enterprise Software replacement capital.

ANALYSIS OF YEAR ENDED DECEMBER 31, 2013 AND 2012 RESULTS

Revenue

Revenue for the year ended December 31, 2013 increased by $51.8 million, or 12.4%, to $471.2 million compared to $419.3 million in 2012. The Mercer Canada Outsourcing acquisition contributed to an increase in revenue of 5.6% over 2012. The other incremental revenue of 6.8% represents year over year growth which came from all four lines of business, with the Administrative Solutions and Consulting lines of business being the largest contributors. This growth was a result of the commencement of service for outsourcing contracts secured in prior years, increased mandates from existing clients and new business wins.

Salary, Benefits and Contractor Expenses

Salary, benefits and contractor expenses for the year ended December 31, 2013 increased by $33.0 million, or 11.5%, to $320.5 million compared to $287.5 million in 2012. In 2012, we made a provision of $2.2 million for the Company's e-commerce refundable tax credit for the years 2010 and 2011, making the adjusted salary, benefits and contractor expense increase $35.2 million versus the comparative period. This increase is primarily attributable to the Mercer Canada Outsourcing acquisition which resulted in an incremental expense, including conversion costs, of $17.4 million. The residual increase of $17.8 million was required to support the Company's continued growth.

Other Operating Expenses

Other operating expenses for the year ended December 31, 2013 increased by $9.6 million, or 14.8%, to $74.3 million compared to $64.8 million in 2012. The increase is primarily due to additional expenses resulting from the Mercer Canada Outsourcing acquisition, including conversion costs, of $5.8 million and $2.0 million recognized as a sublease loss provision (see adjusted EBITDA and EBITDA section below). The residual increase of $1.8 million reflects general increases in rent and occupancy costs required to support business growth.

Finance Costs

Finance costs for the year ended December 31, 2013 increased by $0.1 million, or 0.4%, to $14.1 million compared to $14.0 million in 2012. The increase is primarily due to higher interest on the convertible debenture which was issued late in the first quarter of 2012, offset by reduced interest on the Company's credit facility's from a lower applicable margin and a reduction of $1.0 million as a result of the loss on the previous interest-rate swap agreement becoming fully amortized during Q2, 2012.

Depreciation, Amortization and Impairment Losses

Depreciation and amortization for the year ended December 31, 2013 increased by $3.0 million, or 12.1%, to $27.7 million compared to $24.7 million in 2012. This increase is attributable to increased depreciation and amortization from the Mercer Canada Outsourcing acquisition of $1.1 million and increased depreciation and amortization of $1.9 million on capital expenditures required to support business growth.

As discussed in the Summary and Outlook section, the Company also recorded an impairment loss of $16.7 million during the fourth quarter as part of its annual impairment testing under IAS 36.

Income Tax Expenses

Income tax expenses decreased by $3.5 million, or 32.2%, to $7.4 million, compared to $10.8 million in 2012. The decrease was primarily due to lower deferred income taxes expense of $4.5 million. The lower deferred income taxes were primarily a result of a $3.7 million deferred income tax recovery recognized on the impairment loss of $16.7 million for the OHS CGU.

Profit for the Year

As a result of the changes noted above, profit for the year ended December 31, 2013 was $10.4 million compared to $21.0 million for the same period in 2012.

Key Financial Measures: EBITDA, Adjusted EBITDA, Free Cash Flow and Normalized Free Cash Flow

Adjusted EBITDA and EBITDA

Adjusted EBITDA increased by $8.4 million, or 10.7%, to $86.5 million, compared to $78.1 million in 2012. The increase is primarily due to growth in revenue of $51.8 million partially offset by an increase in salaries and other operating expenses of $43.0 million after EBITDA adjustments that included reorganization and operational effectiveness initiatives, sublease loss provision, impairment charges related to OHS and Mercer Canada Outsourcing conversion costs. These adjusted EBITDA items do not constitute a part of the Company's on-going operating expenses. EBITDA decreased by $11.0 million, or 15.6%, to $59.6 million compared to $70.6 million in 2012.

Free Cash Flow

Free Cash Flow for the year ended December 31, 2013 decreased by $4.6 million to $17.7 million compared to $22.3 million for the same period in 2012. This decrease is primarily due to an increase in capital expenditures of $7.3 million offset by an increase in cash provided by operating activities of $2.7 million (see liquidity and capital resources section below).

Normalized Free Cash Flow

Normalized Free Cash Flow for the year ended December 31, 2013 increased by $0.7 million to $54.0 million compared to $53.3 million for the same period in 2012. The increase is primarily a result of an increase in cash provided by operating activities, before non-cash operating working capital and EBITDA adjustments of $8.9 million. This was offset by higher capital expenditures of $5.6 million, once adjusted for the Mercer Canada Outsourcing and Enterprise Software replacement capital, higher finance costs paid of $1.6 million primarily due to two convertible debenture interest payments as compared to one in the previous year and higher current tax expenses of $1.0 million from increased profit before taxes.

LIQUIDITY AND CAPITAL RESOURCES

Cash Flows

The following table provides an overview of the Company's cash flows for the periods indicated:

Cash Flow Information

Selected Consolidated Financial Information:

Cash provided by (used in): *(In thousands of dollars)*	**Year ended December 31, 2013**	**Year ended December 31, 2012**
Operating activities	**$ 39,478**	$ 36,789
Financing activities	**(15,265)**	(20,477)
Investing activities	**(29,274)**	(15,639)
Increase/(decrease) in cash	**$ (5,061)**	$ 673

Cash provided by operating activities for the year ended December 31, 2013 increased by $2.7 million to $39.5 million compared to $36.8 million in 2012. The increase is primarily due to higher cash generated from operating activities of $9.3 million. This was offset by an increase in finance costs paid of $1.6 million, primarily due to two convertible debenture interest payments in 2013 compared to one in 2012, and higher income taxes paid of $5.0 million as a result of lower tax installment payments in 2012 resulting from non- capital loss carry forwards from previous years.

Cash used in financing activities for the year ended December 31, 2013 decreased by $5.2 million to $15.3 million compared to $20.5 million for the same period in 2012. This decrease is the result of an increase in borrowing compared to 2012 primarily to finance in-year acquisitions. The net proceeds from the convertible denture offering of $71.4 million in the comparative period were used to repay to the revolving loans outstanding.

Cash used in investing activities for the year ended December 31, 2013 increased by $13.6 million to $29.3 million compared to $15.6 million in 2012. This increase is primarily attributable to settlement of contingent liabilities resulting from past acquisitions of $2.8 million and a one-time bargain purchase gain in 2012 of $3.5 million. Additionally there was an increase in additions to intangible and capital assets of $7.3 million (see capital expenditures section below).

Dividends to Shareholders

Monthly dividends were declared for shareholders of record on the last business day of each month and were paid approximately on the 15th day of the following month. Monthly dividends were $0.065 per share for the quarter.

We consider the amount of cash generated by the business in determining the amount of dividends to pay to shareholders. In general, we do not take into account quarterly working capital fluctuations as these tend to be temporary in nature. We do not generally consider profit or loss in setting the level of dividends as this is a non-cash metric and is not reflective of the level of cash flow that we generate.

The twelve-month rolling Normalized Payout Ratio at December 31, 2013 was 69.3% compared to 70.1% for 2012. The decrease in the Normalized Payout Ratio is primarily due to higher adjusted EBITDA during the past twelve months.

Capital Expenditures

Our capital expenditures typically include information technology hardware and software (external and internally developed), leasehold improvements, and office furniture. Such amounts are expected to be funded from our operating cash flow. Additional capital expenditure requirements may result from significant business expansion. Capital expenditures for the three months ended December 31, 2013 increased by $1.6 million to $6.0 million compared to $4.4 million for the same period in 2012 and the increase for the year ended December 31, 2013 was $7.3 million to $21.8 million from $14.5 million in the comparative period. The increase in capital expenditures for the three months and year ended December 31, 2013 is primarily due to Mercer Canada Outsourcing conversion capital which was $1.0 million and 3.9 million respectively, which represents hardware, software and systems improvements necessary to support the acquired business, additional hardware and software for the Administrative Solutions practice of $1.3 million, expenditures on leasehold improvements, and a general increase to support business growth and to maintain our leading edge technology. This was partially offset by reduced spending on enterprise software replacement capital.

Contractual Obligations

Commitments

We lease office space and selected equipment under operating lease agreements with terms ranging from one to fifteen years. We also have a term loan, revolving loan and convertible debenture described under the section "Capital Resources".

A summary of contractual obligations, which outlines the year the payments are due is as follows:

(In thousands of dollars)	**Total**	**2014**	**2015**	**2016**	**2017**	**2018**	**2019 and thereafter**
Long-term debt	$ 176,720	$ -	$ -	$ -	$ 176,720	$ -	$ -
Convertible debenture	75,000	-	-	-	75,000	-	-
Operating leases, net	115,333	13,612	12,993	12,114	11,384	10,804	54,426
Total	**$ 367,053**	**$ 13,612**	**$ 12,993**	**$ 12,114**	**$ 263,104**	**$ 10,804**	**$ 54,426**

We are party to various subleases to which we would be liable for the rental payment in the case of a default by the subtenants. The minimum payments and the aggregate sublease income related to these premises have been netted against the operating leases amounts reported above. We consider the risk of default by the subtenants to be low therefore no accrual has been set up.

Contingent Consideration

The purchase price for SBC Systems is contingent on future business results and is payable in three instalments. The first instalment of U.S. $5.0 million was satisfied on closing through cash consideration. The second instalment of U.S. $0.5 million was settled in March 2013. The final instalment of U.S. $0.5 million, is subject to revenue adjustments, and will be settled in March 2014. At December 31, 2013, $0.5 million has been recognized as an acquisition liability on the statement of financial position, representing the U.S. $0.5 million future instalment discounted.

The purchase price for Dion Durrell Workers' Compensation is contingent on future business results and the contingent payments are payable in three instalments. The three instalments of $0.3 million, $0.6 million, and $0.6 million to be paid within 45 days of June 30, 2014, June 30, 2015 and June 30, 2016, respectively, are subject to revenue adjustments. At December 31, 2013, $1.2 million has been recognized as an acquisition liability on the statement of financial position, representing the total contingent future instalments of $1.6 million discounted.

We have no material contractual obligations other than those described in this MD&A and have no off-balance sheet financing arrangements.

Capital Resources

The following table provides an overview of our capital resources:

(In thousands of dollars)	**As at December 31, 2013**	**As at December 31, 2012**
Bank indebtedness	$ 5,195	$ 134
Long- term debt, net of debt issuance costs	175,647	153,073
Convertible debenture, net of issuance costs	72,021	71,104
Shareholders' equity	325,247	346,618

As at December 31, 2013, our working capital increased by $21.5 million from $45.6 million as at December 31, 2012 to $67.1 million as at December 31, 2013. The increase is primarily attributable to an increase in trade receivables and unbilled fees because of growth in the business, in year acquisitions and timing of billings.

The Company has a credit facility agreement for a term of four years, maturing on November 29, 2017. The credit facility provides for a senior secured revolving term facility of $250,000, which includes a swing line of $7.0 million. As at December 31, 2013, the Company has $68.8 million of available unused revolving term facility.

The interest rates for the facility are floating, based on a margin over certain referenced rates of interest. The applicable margin may vary up and down depending on the ratio of our consolidated debt to Adjusted EBITDA as calculated in the credit agreement. EBITDA is defined in the credit agreement as profit before finance costs, taxes, depreciation, amortization, non-controlling interest and non-recurring expenditures. Adjusted EBITDA is defined in the credit agreement as EBITDA plus the pro-forma EBITDA from permitted acquisitions' entities.

The credit facility is secured by a general assignment of all our assets. The credit agreement also requires us to maintain the following financial covenants on a consolidated basis:

(i) Ratio of debt to Adjusted EBITDA not greater than 3.0:1.0
(ii) Ratio of EBITDA to interest expense of not less than 3.0:1.0

We are in compliance with all the required financial covenants, and the ratios as at December 31, 2013 were 2.1:1.0 and 6.2:1.0 respectively.

The Company entered into an interest-rate swap agreement to hedge against the variable interest rate component of the term loan outstanding under the Original Credit Facility Agreement. The notional amount of the swap is $130,000, for the period from February 1, 2011 up to and ending January 5, 2015. This swap is used to fix the variable component of the interest rate at 2.48%, before the applicable margin, for the duration of the term and has been designated as a cash flow hedge. Upon entering into the Amended Credit Facility Agreement, the interest-rate swap is used to hedge against the variable interest rate component of $130,000 of the Credit Facilities up to and ending January 5, 2015.

On March 27, 2012, the Company issued $75.0 million principal amount of 5.75% Convertible Unsecured Subordinated Debentures ("Debentures") for net proceeds of $71.4 million allocated between debt and equity. The Debentures pay interest semi-annually on March 31 and September 30, commencing with the initial interest payment on September 30, 2012 and have a maturity date of March 31, 2017.

The debentures are convertible at the option of the holder to common shares at a conversion price of $15.00 per common share. The Company has the option to redeem the debentures on and after March 31, 2015 and at any time prior to March 31, 2016 at a redemption price equal to 100% of their principal amount plus accrued and unpaid interest provided that the weighted average trading price for the 20 consecutive trading days ending five days preceding the date on which the notice of redemption is given is at least 125% of the conversion price of $15.00. On and after March 31, 2016, but prior to the maturity date, the debentures will be redeemable at a redemption price equal to 100% of their principal amount plus accrued and unpaid interest. On redemption or maturity the Company may elect to repay the principal and satisfy its interest obligations by issuing the Company's common shares.

SELECTED STATEMENT OF FINANCIAL POSITION DATA

The following table provides an overview of our selected statement of financial position data:

(in thousands of dollars)	**As at December 31, 2013**	**As at December 31, 2012**
Current assets	$148,290	$ 119,762
Non-current assets	551,826	566,595
Current liabilities	81,143	74,198
Non-current liabilities	293,726	265,541

Current Assets

Current assets as at December 31, 2013 increased by $28.5 million to $148.3 million from $119.8 million as at December 31, 2012. The increase is primarily due to an increase in trade receivables and unbilled fees of $24.0 million as a result of growth in revenue and the timing of revenue billing and collections in accordance with contract terms, an increase in deferred implementation costs of $1.5 million, an increase in prepaid expenses and other of $1.2 million due to the timing of vendor payments, and an increase in cash and investments held in trust for insurance premiums of $1.8 million.

Non-current Assets

Non-current assets as at December 31, 2013 decreased by $14.8 million to $551.8 million from $566.6 million at December 31, 2012. The decrease was primarily due to the amortization of capital and intangible assets of $27.7 million, and impairment losses recorded of $16.7 million as detailed in the Summary and Outlook section. The decrease was partially offset by capital expenditures of $21.8 million to support continued business growth and capital assets, intangibles and goodwill acquired of $6.4 million as a result of the acquisitions of Dion Durrell Workers' Compensation and Collage Pediatric Therapy.

Current Liabilities

Current liabilities as at December 31, 2013 increased by $6.9 million to $81.1 million from $74.2 million as at December 31, 2012. The increase is the result of an increase in bank indebtedness of $5.1 million, an increase in trade and other payables of $3.0 million primarily due to higher accrued salaries and compensation, and an increase in insurance premium liabilities of $1.8 million. This was partially offset by lower income taxes payable of $0.3 million, a decrease in deferred revenue of $0.7 million, and a decrease in the current portion of the future consideration related to acquisitions of $2.0 million primarily due to the payment of the final contingent consideration due to Jacques Lamarre & Associates and Parcours d'enfant during the year.

Non-current Liabilities

Non-current liabilities as at December 31, 2013 increased by $28.2 million to $293.7 million from $265.5 million at December 31, 2012. The increase in non-current liabilities is the result of an increase in long-term debt of $22.6 million required to support overall business growth, an increase in the convertible debenture payable of $0.9 million from accretion and amortization, an increase in future consideration related to acquisitions of $0.4 million from the acquisition of Dion Durrell Workers' Compensation, an increase in other liabilities of $1.4, an increase in the deferred tax liability of $2.3 million due to tax timing differences, and an increase in provisions of $1.9 million primarily due to the accrual for the sublease loss. This was offset by a decrease in the fair value of the interest-rate swap of $1.3 million.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

The preparation of financial statements requires us to make estimates and assumptions that affect the reported values of assets and liabilities as well as disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period.

These estimates are reviewed periodically and, as adjustments become necessary, they are reported in profit or loss in the periods in which they become known. Accordingly, actual results could differ from these estimates. The Company's significant accounting policies are presented in Note 3 of the audited consolidated financial statements and notes thereto for the years ended December 31, 2013 and 2012. The accounting policies and estimates that are critical to our business relate to the following items:

Revenue Recognition

Revenues include fees generated from consulting engagements, outsourcing engagements, ESS and OHS services.

Generally, revenue from the rendering of services is recognized when the following criteria are met:

- The amount of revenue can be reliably measured;
- The stage of completion can be reliably measured;
- The receipt of economic benefits is probable; and
- Costs incurred and to be incurred can be reliably measured.

Concurrently with the above general principles, Morneau Shepell applies the following specific revenue recognition policies:

Fees for consulting engagements are billed either on a time-and-material basis or on a fixed-fee basis. On time-and-material engagements, revenue is recognized as services are rendered and expenditures are incurred. On fixed-fee engagements, revenue is recognized in the period in which the services are rendered.

ESS revenue is recognized through a combination of the minimum contracted amount and incremental usage above the minimum thresholds. The minimum contracted amount is recognized on a basis consistent with the provision of ESS services. Incremental usage is recognized when the minimum usage threshold is exceeded.

OHS revenue is recognized on a fixed-fee or time-and-material basis. On fixed-fee basis arrangements, where the provision of service is characterized by an indeterminate number of acts, revenue is recognized on a straight-line basis over the term of the contract. On time-and-material basis arrangements, revenue is recognized as services are rendered and expenditures are incurred.

Outsourcing engagements typically involve both an implementation and administration component. Where a singular contract requires the delivery of multiple components, revenue recognition criteria are applied to determine whether each component of the outsourcing contract qualifies for treatment as a separate unit of accounting. Multiple deliverable arrangements are determined to exist if all of the following criteria are met:

- The delivered item has value to the customer on a stand-alone basis; and
- The fair value of the undelivered item can be reliably measured.

If these criteria are not met, deliverables (components) included in an arrangement are accounted for as a single unit of accounting and revenue is deferred and recognized on a basis consistent with elements of the service contract.

Unbilled fees represent fees earned for services rendered but not yet invoiced as at the reporting date; upon billing, this balance will be transferred to trade receivables. Unbilled fees are recorded at the lower of unbilled hours worked at normal billing rates and the amount which is estimated to be recoverable upon invoicing. Morneau Shepell maintains a provision for amounts expected to be unrecoverable based on the terms of the agreement.

Commissions are recognized when earned, which is at the later of the billing or the effective date of the policy, net of a provision for returned commissions due to policy cancellations or change of brokers. Other income includes investment income earned in the course of normal business operations, and are recorded on the accrual basis.

Intangible Assets and Goodwill

Intangible assets consist of customer relationships, customer contracts, proprietary software, clawback agreements and trade names acquired through acquisitions or business combinations, internally-developed software and purchased software.

Intangible assets acquired through acquisitions or business combinations are initially recognized at fair value based on an allocation of the purchase price.

Internally-developed software is recognized at the cost of all eligible development costs, when all the following criteria are met:

- It is technically feasible to complete the software so that it will be available for use;
- Management intends to complete the software and use or sell it;
- Morneau Shepell is able to use or sell the software;
- Future benefits associated with the software can be demonstrated;
- Adequate technical, financial, and other resources to complete the development and to use or sell the software are available; and
- The expenditures attributable to the software during its development can be reliably measured.

Eligible expenditures capitalized as part of internally-developed software include external direct costs of materials and services consumed in development, and payroll and payroll-related costs for employees who are directly associated with and who devote time to the internal-use computer software project (to the extent that their time was spent directly on the project). All costs incurred in the preliminary research stage of the projects are expensed as incurred. Purchased software is recognized at initial costs.

Intangible assets with a finite life are amortized on a straight-line basis over their estimated useful lives. Intangible assets with an indefinite life are not amortized, but are tested for impairment annually or whenever impairment indicators are identified. Intangible assets are measured at cost less accumulated amortization and accumulated impairment losses.

Goodwill represents the excess of the cost of business acquisitions over the fair value of our share of the net identifiable assets of the acquired subsidiary at the date of acquisition. Goodwill is carried at cost less accumulated impairment charges and is subject to impairment test annually or whenever impairment indicators are identified.

Impairment of Non-financial Assets

The Company's identifiable tangible and intangible assets with finite useful lives are reviewed for indications of impairment at each statement of financial position date and when events or changes in circumstances indicate that they may be impaired. Impairments are recorded when the recoverable amount of assets are less than their carrying amounts. The recoverable amount is the higher of an asset's fair value less cost to sell or its value in use. Impairment losses, other than those relating to goodwill, are evaluated for potential reversals when events or changes in circumstances warrant such consideration.

Similarly, intangible assets with indefinite useful lives and goodwill are tested for impairment annually or whenever impairment indicators are identified, by estimating their recoverable amounts and comparing it to their carrying amounts. Where individual assets cannot be tested individually, they are grouped together into cash-generating units ("CGU"), the smallest group of assets that are capable of generating cash inflow from continuing use largely independent of other groups of assets, and tested on this basis. Goodwill acquired through business combinations is allocated to each CGU or groups of CGU's but not larger than an operating segment that is expected to benefit from the synergies of the combination.

An impairment loss is recognized if the carrying amount of the CGU exceeds its estimated recoverable amount. Impairment losses are recognized in profit or loss, and those impairment losses recognized in respect of CGUs are allocated first to reduce the carrying amount of any goodwill allocated to the unit, and then to reduce the carrying amount of the other assets in the unit on a pro rata basis.

Impairment losses in respect of goodwill are not reversed. In respect of other assets, impairment losses recognized in prior periods are assessed at each reporting date for any indications that the loss has decreased or no longer exists. An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount, and only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortization had no impairment charge been recorded.

Goodwill and intangible assets impairment review involves significant estimates and assumptions regarding cash flow projections, growth projections, economic risk, and weighted cost of capital. If future events or results differ adversely from these estimates and assumptions, the Company could incur impairment charges in future periods.

Allowance for Doubtful Accounts

We are required to assess whether accounts receivables are collectible from customers. Accordingly, management establishes an allowance for estimated losses arising from non-payment and delinquent accounts, taking into consideration customer creditworthiness, current economic trends, and past experience. If future collections differ from estimates, future earnings could be adversely affected.

Litigation and Claims

We are involved in litigation and other claims arising in the normal course of business. We must use judgment to determine whether or not a claim has any merit, the amount of the claim and whether to record a provision, which is dependent upon the potential success of the claim. We believe that none of the current claims will have a material adverse impact on our financial position.

Convertible Debentures

Compound financial instruments issued by the Company comprise convertible debentures that can be converted to share capital at the option of the holder, and the number of shares to be issued upon conversion does not vary with changes in their fair value.

The liability component of a compound financial instrument is recognized initially at the fair value of a similar liability that does not have an equity conversion option. The equity component is recognized initially at the difference between the fair value of the compound financial instrument as a whole and the fair value of the liability component. Any directly attributable transaction costs are allocated to the liability and equity components in proportion to their initial carrying amounts.

Subsequent to initial recognition, the liability component of a compound financial instrument is measured at amortized cost using the effective interest rate method. The equity component of a compound financial instrument is not re-measured subsequent to initial recognition.

Interest, losses and gains relating to the financial liability are recognized in profit or loss.

Changes in Accounting Policies

IAS 1 Amendment, Presentation of Items of Other Comprehensive Income ("IAS 1")

The Company has adopted the amendments to IAS 1 effective January 1, 2013. These amendments required the Company to group other comprehensive income items by those that will be reclassified subsequently to profit or loss and those that will not be reclassified. The Company has reclassified comprehensive items of the comparative period. These changes did not result in any adjustments to other comprehensive income or comprehensive income.

IFRS 10, Consolidated Financial Statements ("IFRS 10")

IFRS 10 replaces International Accounting Standard ("IAS") 27, Consolidated and Separate Financial Statements, and SIC-12, Consolidation - Special Purpose Entities. This new standard contains a single consolidation model that identifies control as the basis for consolidation for all types of entities, sets forth factors to consider in assessing control, and requires control to be assessed on a continuous basis. The Company has assessed its consolidation conclusions on January 1, 2013 and determined that the adoption of IFRS 10 did not result in any change in the consolidation status of any of its subsidiaries and investees.

IAS 19, Employee Benefits (IAS 19")

IAS 19 (amended in 2011), amends certain accounting requirements for defined benefit plans.

IAS 19 (revised 2011) requires the net defined benefit liability (asset) to be recognized on the balance sheet without any deferral of actuarial gains and losses and past service costs as previously allowed. Past service costs are recognized in net income when incurred. Expected returns on plan assets are no longer included in post- employment benefits' expense. Instead, post-employment benefits' expense includes market yields on high quality bonds on the net defined benefit liability. Actuarial gains and losses and any change in the asset ceiling are recognized in other comprehensive income.

The Company adopted these amendments retrospectively and accordingly adjusted its accumulated other comprehensive income as at January 1, 2012 to recognize previously unrecognized actuarial losses for post-employment plans. Please refer to note 3 of the consolidated financial statements for the year ended December 31, 2013 for a summary of the impact of the adoption of this revised standard.

IFRS 13, Fair Value Measurement ("IFRS 13")

IFRS 13 provides a single framework for measuring fair value. The measurement of the fair value of an asset or liability is based on assumptions that market participants would use when pricing the asset or liability under current market conditions, including assumptions about risk. The Company adopted IFRS 13 on January 1, 2013 on a prospective basis. The adoption of IFRS 13 did not require any adjustments to the valuation techniques used by the Company to measure fair value and did not result in any measurement adjustments as at January 1, 2013.

Future Accounting Changes

IFRS 9, Financial Instruments ("IFRS 9")

IFRS 9 introduces new requirements for classifying and measuring financial assets and may affect the Company's accounting for its financial assets. Specifically, IFRS 9 requires financial assets to be classified into two measurement categories, those measured at fair value and those measured at amortized cost. There is no mandatory effective date for IFRS 9, although it may be adopted immediately. The Company has not early adopted IFRS 9 for the year ended December 31, 2013, and the extent of its impact has not been determined.

IAS 39, Financial Instruments (“IAS 39”)

An amendment to IAS 39 makes it clear that there is no need to discontinue hedge accounting where a derivative hedging instrument has been novated to effect clearing with a central counterparty as a result of laws or regulation, provided specific conditions are met. Novation refers to where parties to a contract agree to replace their original counterparty with a new one. This amendment to IAS 39 is effective for fiscal years beginning on or after January 1, 2014. The Company does not expect this amendment to have a material impact on its consolidated financial statements.

IAS 36, Impairment of Assets (“IAS 36”)

Amendments to IAS 36 cover recoverable amount disclosures for non-financial assets, including circumstances in which the recoverable amount of assets or CGU’s are required to be disclosed, clarification of the disclosures required, and introducing an explicit requirement to disclose the discount rate used in determining impairment or impairment reversals where recoverable amount is determined using a present value technique. The amendments are effective for fiscal years beginning or after January 1, 2014. The Company does not expect this amendment to have a material impact on its consolidated financial statements.

RISKS AND UNCERTAINTIES

The results of operations, business prospects and financial considerations of Morneau Shepell remains subject to a number of risks and uncertainties and are affected by a number of factors outside of our control.

Ability to Maintain Profitability and Manage Growth

There can be no assurance that Morneau Shepell will be able to sustain profitability in future periods. Morneau Shepell's future operating results will depend on a number of factors, including its ability to continue to successfully execute its strategic initiatives.

There can be no assurance that Morneau Shepell will be successful in achieving its strategic plan or that its strategic plan will enable the firm to maintain its historical revenue growth rates or to sustain profitability. Failure to successfully execute any material part of Morneau Shepell’s strategic plan could have a material adverse effect on its business, financial condition and operating results, and the ability of Morneau Shepell to pay dividends.

There can be no assurance that Morneau Shepell will be able to effectively manage its growth, and any failure to do so could have a material adverse effect on the firm’s business, financial condition and operating results, and on the ability of Morneau Shepell to pay dividends.

Cash Dividends Are Not Guaranteed and Will Fluctuate With the Business Performance

As a corporation, Morneau Shepell's dividend policy is at the discretion of its Board of Directors. The ability of Morneau Shepell to make dividend payments, and the actual amount paid is entirely dependent on the operations and assets of its subsidiaries and is subject to various factors applicable to Morneau Shepell and its subsidiaries including financial performance, obligations under credit facilities, fluctuations in working capital, the sustainability of margin and capital expenditure requirements and applicable laws and regulations.

Reliance on Information Systems and Technology

Information systems are an integral part of Morneau Shepell's business and the products and services offered to its clients. Morneau Shepell relies on systems to maintain accurate records and to carry out required administrative functions in accordance with the terms of its contractual obligations to its clients. In order to maintain the level of security, service and reliability that clients require, Morneau Shepell may be required to make significant investments in the online means of delivering services. The adoption of additional laws or regulations with respect to the internet may impede the efficiency of the internet as a medium of exchange of information and decrease the demand for Morneau Shepell's services.

Any disruptions in Morneau Shepell's systems, the failure of the systems to operate as expected, or the firm's ability to use the internet effectively to deliver services could, depending on the magnitude of the problem, result in a loss of current or future business and/or potential claims against Morneau Shepell, all of which could have a material adverse effect on Morneau Shepell's business, financial condition and operating results, and on the ability of Morneau Shepell to pay dividends.

Reputational Risk

Morneau Shepell depends to a large extent upon its relationships with its clients and its reputation for high-quality services. As a result, the impact of client dissatisfaction with Morneau Shepell's services or products may be more damaging in Morneau Shepell's business than in other businesses. Moreover, if the firm fails to meet its contractual or regulatory obligations, Morneau Shepell could be subject to legal liability and a loss of client relationships.

Risk of Future Legal Proceedings

Morneau Shepell may be threatened with, or may be named as a defendant in, or may become subject to, various legal proceedings in the ordinary course of conducting its business, including lawsuits based upon professional errors and omissions.

Consulting services involves assumptions and estimates concerning future events, the actual outcome of which cannot be known with certainty in advance. In addition, computational, software programming or data management errors could occur. For example, possible legal proceedings could result from a client's assertion that actuarial assumptions used in a pension plan were unreasonable, leading to plan underfunding; a claim that inaccurate data was used, which could lead to an underestimation of plan liabilities; or a claim that employee benefits plan documents were misinterpreted or plan amendments were misstated in plan documents, which could lead to overpayments to beneficiaries. The employee health and productivity services involve confidential counseling, occupational health activities and disability case management. Each of these activities could potentially put Morneau Shepell in conflict with its customers, their employees, or both. Possible legal proceedings could also result from matters such as an employee claiming for breach of confidence, failure to provide adequate counsel, or denial of benefits or employment as a result of Morneau Shepell's actions.

Defending lawsuits of this nature could require much management attention, which could divert its focus from operations. Such claims could produce negative publicity that could harm Morneau Shepell's reputation and business. A significant judgment against Morneau Shepell, or the imposition of a significant fine or penalty as a result of a finding that Morneau Shepell failed to comply with laws or regulations, could have a material adverse effect on Morneau Shepell's business, financial condition and operating results, and on the ability of Morneau Shepell to pay dividends.

Confidentiality of Client Information

Morneau Shepell depends to a large extent on its relationships with its customers and its ability to properly maintain confidential client information. Morneau Shepell maintains rigorous controls to protect confidential information from unauthorized use or disclosure, however the failure of Morneau Shepell to maintain client confidentiality could, depending on the magnitude of the problem, result in a loss of future business and/or potential claims against Morneau Shepell. This could have a material adverse effect on Morneau Shepell's business, financial condition and operating results, and on the ability of Morneau Shepell to pay dividends.

Dependence on Key Clients

As clients may terminate engagements with minimum notice, there can be no assurance that Morneau Shepell will be able to retain relationships with its largest clients. Moreover, there can be no assurance that such clients will continue to use Morneau Shepell's services in the future. Any negative change involving any of Morneau Shepell's largest clients, including but not limited to a client's financial condition or desire to continue using the firm's services, could result in a significant reduction in revenue which could have a material adverse effect on Morneau Shepell's business, financial condition and operating results, and on the ability of Morneau Shepell to pay dividends. No one Morneau Shepell client makes up more than 10% of Morneau Shepell's total revenue for the years December 31, 2013 and 2012.

Reliance on Key Professionals

Morneau Shepell's operations are dependent upon the abilities, experience and efforts of its professionals, many of whom have excellent reputations and a significant number of contacts in the industry in which Morneau Shepell operates. Morneau Shepell's business depends, in part, on its professionals' abilities to develop and maintain client relationships and alliances with businesses such as financial services companies, healthcare organizations, insurance companies, business process outsourcing organizations and other companies, in order to develop, market and deliver its services. Profitability could be negatively impacted if Morneau Shepell's client relationships or business alliances are discontinued due to the loss of professional staff or if the firm has difficulty developing new alliances.

Should any member of its professional staff be unable or unwilling to continue his or her relationship with Morneau Shepell, this change could have a material adverse effect on Morneau Shepell's business, financial condition and operating results, and on the ability of Morneau Shepell to pay dividends.

Economic Conditions

An economic slowdown could cause a decline in demand for Morneau Shepell's services. Growth in its clients' businesses may be affected by economic slowdowns and could therefore potentially have an impact on Morneau Shepell's operating results. During an economic downturn, Morneau Shepell clients and potential clients may reduce or delay services or projects, or defer contracts currently underway. This situation could also lead to greater delays and defaults in payments or debt collection, resulting in lower operating results. Because of lower revenue during an economic slowdown, competition may increase and prices may be reduced by certain competitors to maintain or expand their market share. Pricing and profitability could be adversely affected as a result.

Competition

Morneau Shepell operates in a highly competitive North American market. As a result, Morneau Shepell competes with many domestic and international firms. Some of its competitors have achieved substantially more market penetration in certain of the areas in which Morneau Shepell competes. In addition, some of Morneau Shepell's competitors have substantially more financial resources and/or financial flexibility than Morneau Shepell. Further, Morneau Shepell's business relies, in part, upon its ability to develop and implement technology solutions, in a cost effective manner that anticipate and keep pace with rapid and continuing changes in technology, industry standards and client preferences.

Morneau Shepell's competitors may offer new technologies more efficiently or cost effectively than Morneau Shepell. Competitive forces could result in reduced market share and thus have a material adverse effect on Morneau Shepell's business, financial condition and operating results, and on the ability of Morneau Shepell to pay dividends.

Satisfactory Performance of Obligations

In its contracts with clients, Morneau Shepell is sometimes committed to meeting identified service levels and/or timelines. If the service levels/timelines are not met, Morneau Shepell may experience reduced revenues, incur significant additional costs or be held responsible for the costs incurred by the client for failure to meet the service level/timeline. Morneau Shepell's success depends in large part upon whether it fulfills these and other contractual obligations with clients and maintains client satisfaction. If Morneau Shepell fails to satisfactorily perform its contractual obligations, its clients could terminate contracts and/or take legal action against Morneau Shepell. Such occurrences could result in a loss of its professional reputation and in extra costs needed to defend or rectify the situation and thus have a material adverse effect on Morneau Shepell's business, financial condition and operating results, and on the ability of Morneau Shepell to pay dividends.

Protection of Intellectual Property

Morneau Shepell continually develops and improves its proprietary technology solutions for the delivery of its services. No assurance can be given that Morneau Shepell's competitors will not develop substantially similar technology.

Morneau Shepell relies on one or more of the following to protect its proprietary rights: trademarks, copyrights, trade secrets, confidentiality procedures and contractual provisions. Despite Morneau Shepell's efforts to protect its proprietary rights, unauthorized parties may attempt to obtain and use information that Morneau Shepell regards as proprietary. Stopping unauthorized use of Morneau Shepell's intellectual property may be difficult, time-consuming and costly. There can be no assurance that Morneau Shepell will be successful in protecting its proprietary rights and, if it is not, this could have a material adverse effect on Morneau Shepell’s business, financial condition and operating results, and on the ability of Morneau Shepell to pay dividends.

Relationship with Channel Partners

Morneau Shepell markets its services directly to end-user employers as well as through certain channel partners, primarily insurance companies (many of which compete amongst themselves directly). There can be no assurance that Morneau Shepell will be able to maintain its existing relationships with all these channel partners, which could have a material adverse effect on Morneau Shepell’s business, financial condition and operating results, and on the ability of Morneau Shepell to pay dividends.

Potential Undisclosed Liabilities Associated with Acquisition/Limited Indemnification

In connection with acquisitions completed by Morneau Shepell, there may be liabilities and contingencies that Morneau Shepell failed to discover or were unable to quantify in its due diligence which it conducted prior to the execution of an acquisition, and Morneau Shepell may not be indemnified for some or all of these liabilities and contingencies. The existence of any material liabilities or contingencies could have a material adverse effect on Morneau Shepell’s business, financial condition, liquidity and results of operations.

Implications of Fixed-Price Contracts

A portion of Morneau Shepell’s revenue comes from fixed-price contracts. A fixed-price contract requires Morneau Shepell to perform either all or a specified portion of work under the contract for a fixed price.

Fixed-price contracts expose Morneau Shepell to a number of risks, including underestimation of costs, ambiguities in specifications, unforeseen costs or difficulties, problems with new technologies, delays beyond the control of Morneau Shepell, failures of subcontractors to perform, and economic or other changes that may occur during the contract period. Losses under fixed-price contracts could have a material adverse effect on Morneau Shepell's business, financial condition and operating results, and on the ability of Morneau Shepell to pay dividends.

Insurance

Morneau Shepell believes that its professional errors and omissions insurance, director and officer liability insurance, and commercial general liability insurance coverage address all material insurable risks, provides coverage that is similar to that which would be maintained by a prudent operator of a similar business and is subject to deductibles, limits and exclusions which are customary or reasonable given the cost of procuring insurance and current operating conditions.

However, there can be no assurance that such insurance will continue to be offered on economically feasible terms, that all events that could give rise to a loss or liability are insurable, or that the amounts of insurance will at all times be sufficient to cover each and every loss or claim that may occur involving Morneau Shepell's assets or operations.

Indebtedness and Interest Rates

The ability of Morneau Shepell to pay dividends or make other payments or advances will be subject to applicable laws and contractual restrictions contained in the instruments governing any indebtedness of those entities.

The degree to which Morneau Shepell is leveraged could have important consequences including: Morneau Shepell's ability to obtain additional financing for working capital, capital expenditures or acquisitions in the future may be limited; a significant portion of Morneau Shepell's cash flow from operations may be dedicated to the payment of the principal of and interest on its indebtedness, thereby reducing funds available for future operations; certain borrowings will be at variable rates of interest, which exposes Morneau Shepell to the risk of increased interest rates; and Morneau Shepell may be more vulnerable to economic downturns and be limited in its ability to withstand competitive pressures.

These factors may increase the sensitivity of free cash flow to interest rate variations. Interest rate swap agreements are used as part of Morneau Shepell's program to manage the fixed and floating interest rate of Morneau Shepell's credit facility related overall cost of borrowing.

The advance of the credit facility and the issuance of the convertible debenture have significantly increased the amount of Morneau Shepell's debt compared to historical levels. The credit facility contains numerous restrictive covenants that limit the discretion of management with respect to certain business matters. These covenants place significant restrictions on, among other things, the ability of Morneau Shepell to create liens or other encumbrances, to pay dividends or make certain other payments, investments, loans and guarantees and to sell or otherwise dispose of assets and merge or consolidate with another entity.

In addition, the credit facility contains a number of financial covenants that require Morneau Shepell to meet certain financial ratios and financial condition tests. A failure to comply with the obligations in the credit facility could result in a default which, if not cured or waived, could result in a reduction or termination of dividends by Morneau Shepell and permit acceleration of the relevant indebtedness. If the indebtedness under the credit facility was to be accelerated, there can be no assurance that the assets of Morneau Shepell would be sufficient to repay in full that indebtedness. In addition, the credit facility matures on November 29, 2017. There can be no assurance that future borrowings or equity financing will be available to Morneau Shepell or available on acceptable terms, in an amount sufficient to fund Morneau Shepell's needs.

The convertible debentures are convertible into the Company's common shares at the option of the holder of the debenture. If the debenture converts this may have a dilutive impact on the Company's earnings per share. Additionally, a conversion will increase the cash required to maintain dividend payments at current levels.

Foreign Exchange Risk

A portion of Morneau Shepell's sales are in U.S. dollars and thus Morneau Shepell is exposed to fluctuations in the value of the U.S. dollar relative to the Canadian dollar.

The net revenue exposure denominated in U.S. dollars was $4.8 million and $16.7 million respectively, for the three months and year ended December 31, 2013. An increase in foreign revenues would expose Morneau Shepell to fluctuations in exchange rates which may have a material adverse effect on Morneau Shepell's business, financial condition, and operating results, and on the ability of Morneau Shepell to pay dividends.

Market Price of Common Shares

The market price of the Common Shares may be subject to wide fluctuations in response to many factors, including variations in operating results of Morneau Shepell, divergence in financial results from expectations, changes in business prospects for Morneau Shepell, general economic conditions, legislative changes, and other events and factors outside Morneau Shepell's control.

Sales of a substantial number of Common Shares by a significant shareholder in the public market or otherwise could adversely affect the prevailing market prices of the Common Shares and could impair the Corporation's ability to raise additional capital through an offering of Common Shares. The possible perception among the public that these sales will occur could also produce the same effect.

Dilution of Common Shares

Pursuant to its articles of incorporation, Morneau Shepell is authorized to issue an unlimited number of Common Shares and 10 million preferred shares for the consideration and on such terms as are established by the Board of Directors without the approval of any shareholders. Any further issuance of Common shares may dilute the interests of existing shareholders. Furthermore, Morneau Shepell may make future acquisitions or enter into financings or other transactions involving the issuance of securities of Morneau Shepell which may be dilutive.

SELECTED ANNUAL INFORMATION

(In thousands of dollars except per share amounts)	**Year ended December 31, 2013**	**Year ended December 31, 2012**	**Year ended December 31, 2011**
Revenue	$471,154	$419,346	$364,988
Profit	10,445	21,034	24,903
Earnings per share (basic)	0.21	0.43	0.52
Earnings per share (diluted)	0.21	0.43	0.51
Dividends declared per share [(1)]	0.78	0.78	0.78
Total Assets	700,116	686,357	668,089
Total long-term debt	247,668	224,177	207,121

SUPPLEMENTARY SUMMARY OF QUARTERLY RESULTS

Selected Unaudited Consolidated Financial information (in thousands of dollars except per share amounts)

Quarter ended	December 31, 2013	September 30, 2013	June 30, 2013	March 31, 2013	December 31, 2012	September 30, 2012	June 30, 2012	March 31, 2012
Revenue	118,570	118,526	118,328	115,730	107,258	101,331	106,791	103,966
Profit	(11,279)	6,937	7,835	6,951	4,234	6,105	6,274	4,421
EBITDA	(2,502)	20,484	21,412	20,188	16,242	18,269	19,920	16,173
Adjusted EBITDA	20,217	21,909	22,847	21,554	18,843	19,278	20,763	19,251
EBITDA margin	(2.1%)	17.3%	18.1%	17.4%	15.1%	18.0%	18.7%	15.6%
Adjusted EBITDA margin	17.1%	18.5%	19.3%	18.6%	17.6%	19.0%	19.4%	18.5%
Earnings per share (basic)	(0.23)	0.14	0.16	0.14	0.09	0.13	0.13	0.09
Earnings per share (diluted)	(0.23)	0.14	0.16	0.14	0.09	0.12	0.13	0.09
Twelve-month rolling normalized payout ratio	69.3%	73.2%	72.7%	72.4%	70.1%	77.1%	77.5%	86.3%
Total assets	700,116	708,412	699,259	695,388	686,357	677,864	688,298	682,998
Total long-term debt [1]	247,668	245,324	245,062	233,593	224,177	227,790	233,003	212,858

(1) Includes convertible debentures issued on March 27, 2012.

Disclosure Controls and Procedures

Our disclosure controls and procedures have been designed to provide reasonable assurance that all relevant information is identified to our Disclosure Committee to ensure appropriate and timely decisions are made regarding public disclosure.

The Chief Executive Officer and the Chief Financial Officer have concluded that the disclosure controls and procedures are appropriately designed as at December 31, 2013.

Internal Control Over Financial Reporting

Management is responsible for designing internal controls over financial reporting, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with IFRS. In designing these controls, Management used the *Internal Control – Integrated Framework* (COSO 1992 Framework) published by The Committee of Sponsoring Organizations of the Treadway Commission.

The Chief Executive Officer and the Chief Financial Officer have concluded that the internal controls over financial reporting are appropriately designed and operating effectively to provide this assurance based on the evaluation of these controls conducted as at December 31, 2013. No changes were made in our internal controls over financial reporting during the fourth quarter ended December 31, 2013, that have materially affected, or are reasonably likely to materially affect, our internal controls over financial reporting.

Additional Information

Morneau Shepell's shares currently trade on the Toronto Stock Exchange under the symbol MSI. Additional information relating to us, including all public filings, is available on the SEDAR Web site (www.sedar.com) and on our own Web site at www.morneaushepell.com.

The content of this MD&A reflects information known as of March 5, 2014.