

**CHESSWOOD GROUP LIMITED**

**CONDENSED CONSOLIDATED INTERIM  
FINANCIAL STATEMENTS**

**FOR THE THREE AND NINE MONTHS ENDED**

**SEPTEMBER 30, 2013**



## **CHESSWOOD GROUP LIMITED**

### **NOTICE TO READERS**

Accompanying this notice are the unaudited condensed consolidated interim financial statements of Chesswood Group Limited for the three and nine months ended September 30, 2013. These statements have been prepared by, and are the responsibility of, the Company's management.

Following consultation with management and with the Company's independent auditors, the Company's board of directors concluded that the auditors would not be engaged to perform a review of these financial statements. Under applicable securities legislation, there is no requirement that auditors be engaged to review these statements, but the Company must advise you if (as noted above) no review engagement is made.

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## **TO OUR SHAREHOLDERS**

We continued the trend of our first half of the year, in the third quarter, by posting strong gains over the same quarter of the prior year while generating nine months of excellent earnings that are well ahead of our nine-month earnings of 2012. We earned \$9.2 million thru three quarters this year, compared to \$5.8 million last year, for an increase of 59%.

Each one of our operating businesses improved their results in the quarter, over the third quarter of last year, lead again by our largest business, Pawnee Leasing Corporation.

We are proud to have launched a new business in late September, as our entrant into the growing working capital loan industry in the United States. Windset Capital Corporation will make working capital loans to small businesses throughout America, and will leverage the expert administration and collection infrastructures already in place at Pawnee, to reach out to the many brokers and others that now offer this product as a regular financing tool for small business.

Windset's loans are expected to average approximately \$30,000 each, while generating risk-adjusted returns consistent with the returns we generate in our other finance businesses. This newer industry has been generating large annual origination volumes and our initial experience to date has been very favorable.



Barry Shafran  
President & CEO

## **COMPANY PROFILE**

Chesswood Group Limited ("Chesswood" or the "Company"), is an Ontario corporation and is the successor to Chesswood Income Fund (the "Fund") following the "conversion" of the Fund under a plan of arrangement which became effective on January 1, 2011.

Through its interest in Pawnee Leasing Corporation ("Pawnee"), Chesswood is involved in the business of micro and small-ticket equipment finance to small businesses in the start-up and "B" credit market in the lower 48 states of the United States. Through its interest in Sherway LP, Chesswood is involved in selling, servicing and leasing Acura automobiles in the Province of Ontario. Through its interest in Case Funding Inc. ("Case Funding"), Chesswood is involved in the business of providing financing to plaintiffs and attorneys and the purchase of medical liens that form part of litigation throughout the United States. Through its interest in Windset Capital Corporation ("Windset"), Chesswood is becoming involved with the business of providing working capital loans to small businesses in United States. Through its interest in Lease-Win Limited ("Lease-Win"), Chesswood owns cars4U.com.

The Company's annual report and annual information form for the year-ended December 31, 2012 are available on SEDAR at [www.sedar.com](http://www.sedar.com), and provide additional information on the Company and its operating companies.

The Company's common shares are listed on the Toronto Stock Exchange under the symbol CHW.

## **PAWNEE**

Pawnee is an equipment finance company that provides financing on micro and small-ticket business equipment. Pawnee focuses on small businesses (with a particular focus in the start-up and "B" credit segment of the U.S. equipment finance market), servicing the lower 48 states through a network of approximately 550 independent brokers. As of September 30, 2013, Pawnee administered 9,753 leases and loans in its portfolio, with remaining scheduled payments of approximately U.S.\$175.2 million over the next five years.

Pawnee finances equipment where generally:

- (i) the equipment is fundamental to the core operations of the lessee/borrower's business;

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- (ii) the cost of the equipment usually does not exceed U.S.\$75,000;
- (iii) a personal guarantee of at least the major shareholder/owner is obtained; and
- (iv) all scheduled payments are required to be paid by direct debit out of the lessee's/borrower's account.

Pawnee's business does not involve financing of consumer goods. Pawnee funds only commercial equipment.

A key aspect of Pawnee's business is managing potential risks in order to limit defaults to the greatest extent possible. Pawnee has developed a number of risk management tools and processes which it continually monitors and improves to address changes in its market and in the equipment finance industry.

Management believes that Pawnee is the leading micro and small-ticket funding source available to equipment financing brokers in the start-up equipment finance market in the U.S. and is a well-recognized player in the "B" credit market. Pawnee's success in these higher risk niche markets is due to Pawnee's ability to select creditworthy businesses through its proprietary credit analysis matrix and process, to price for higher risk, and its efficient servicing and collection processes.

Pawnee has traditionally provided funding to two very similar micro and small-ticket commercial financing markets – the start-up market and the "B" credit market. The creditworthiness of start-up businesses does not fall into traditional credit categories because of their lack of business credit history. Pawnee defines "start-up" businesses to be those businesses with less than two years of operating history. "B" credit businesses are those that have two or more years of operating history and have some unique aspect to their overall credit profile such that they are not afforded an "A" rated credit score or that the business owner(s) do not have an "A" rated personal credit history.

The start-up and "B" credit segments of the micro and small-ticket equipment finance market have historically been, and continue to be, more sensitive to monthly lease/loan payment amounts than to the effective rates of interest charged.

Pawnee added a new product offering to a limited number of its broker network in late 2008. This additional "B" market product, now offered to all of Pawnee's brokers, referred to as "B+" complements Pawnee's long standing core "B" product, by offering funding to lessees that have stronger credit profiles than Pawnee had considered in the past.

Assessed as lower risk business than Pawnee's traditional "B" business, "B+" borrowers receive funding based on rates that typically range from 14-30%. At September 30, 2013, approximately 65% of Pawnee's lease and loan receivables consisted of the "B+" product.

Pawnee's business model is different from certain other leasing, equipment finance, consumer, sub-prime mortgage and finance companies in a number of important respects, including the following:

- Pawnee does not sell its leases and loans, but rather retains its leases and loans for their full term,
- Pawnee's revenues are derived directly from its leases and loans, and are not derived from (and therefore, and more importantly, Pawnee's revenues are not dependent upon) fees from the sale of its portfolio of leases and loans, and
- not only is there significant geographic diversification (within the United States) within Pawnee's portfolio of leases and loans, there is also significant diversification in terms of the equipment funded and the industries in which Pawnee's lessees and borrowers operate. At September 30, 2013:
  - no state represented more than 11.1% of the number of Pawnee's total active leases and loans, with the exception of California which represented 12.5%;
  - Pawnee financed over 70 equipment categories, with its five largest categories by volume, being restaurant, auto repair, titled trucks and trailers, medical and computer equipment, which combined accounted for 52.7% of the number of active leases and loans;
  - its lessees and borrowers operated in over 85 different industry segments, with no industry concentration accounting for more than 15.9% of its number of active leases and loans;
  - no lessee/borrower accounted for more than 0.01% of its total lease and loan portfolio; and
  - its largest source of originations accounted for 7.1% of its gross lease and loan receivable, and its ten largest origination sources accounted for 31.4% of its gross lease and loan receivable.

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Pawnee's revenues and fundings are not dependent upon continuously finding third party buyers for its lease and loan portfolio (where demand is driven by factors such as prevailing interest rates and the quality of other available portfolios and other available investments). Rather, Pawnee has a continuing lending facility.

As of September 30, 2013, Pawnee employed approximately 40 full-time equivalent employees, over one-third of whom are dedicated to collection and default remediation.

### **CASE FUNDING**

On June 10, 2011, Chesswood acquired the shares of Case Funding Inc. ("Case Funding"), a newly incorporated and organized corporation which acquired the tangible and intangible assets required to carry on the going forward business of Quick Cash Inc. ("Quick Cash"), a provider of legal financing to plaintiffs and attorneys throughout the United States.

The entire team of Quick Cash joined Case Funding, combining their legal finance experience with Chesswood's specialty finance expertise and financial resources to build a growth-oriented legal finance business.

#### *The Legal Funding Market - Overview*

The legal finance market is a large underserved market that has been growing rapidly over the last decade. Case Funding provides litigators with loans based on a percentage of the value of their contingent fees (as determined by Case Funding) and provides legal funding for plaintiffs based on Case Funding's views of the strength of their lawsuits. Quick Cash has been in the legal finance business since 2003. Case Funding did not acquire Quick Cash's existing portfolio of advances.

Management believes that Case Funding provides Chesswood with the ability to expand its specialty finance business by generating superior risk adjusted returns, through an existing infrastructure with market position, and in so doing provides opportunities for significant long-term growth.

Legal funding provides an alternative source of funding in situations where a person has a strong legal claim and where that person, or the person's law firm, is in need of financial resources to pursue the claim. Conventional lenders such as banks and commercial lenders generally avoid this market due to its relative complexity and lack of robust balance sheets (in the case of law firms), leaving both plaintiffs and law firms without the required funds to pursue potentially high probability, high dollar value cases.

In the United States, legal funding improves fairness in the legal process by permitting a person lacking the required funds to continue pursuing a claim against a defendant. Legal funding provides an alternative funding option for plaintiffs who are in financial need (due to inability to work, medical issues or otherwise), while their case is being litigated.

Many plaintiffs are unable to afford fee-based attorneys and are forced to seek out contingency attorneys who are willing to represent them on a percentage-of-win basis. Contingency based attorneys typically only pursue cases they feel have merit and can generate significant fees. Because of the delays in the litigation process, however, plaintiffs and their law firms still have a strong need for funds to see them through until the full settlement of their cases.

Before legal funding, plaintiffs suffered a distinct disadvantage as they often had to wait years for their cases to be resolved. This delay caused many plaintiffs to prematurely settle potentially valuable claims at a substantial discount to their true value. The industry does not generally provide funding, unless an action has already commenced.

While legal funding markets in the U.K. and Australia are reasonably mature, legal funding is a young industry in the U.S., and is highly fragmented.

There are significant variations amongst funders in the structure of loans and advances, especially to law firms, and in the fees and rates that are charged to plaintiffs and law firms. The attorney/law firm funding business is growing in the United States, as numerous but poorly capitalized legal funding companies have emerged. In the United States, it is estimated that 10,000 to 20,000 plaintiff funding applications per month are presented to leading legal funding companies.

Internationally there are several firms engaged exclusively in legal financing that are publicly listed in foreign markets. These listed firms are primarily centered on corporate litigation with a focus on insolvency or commercial litigation.

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In most states throughout the United States, it is illegal for lawyers to share contingency fees with non-lawyers, thereby prohibiting non-lawyers from becoming equity investors in law firms. To add to the difficulties presented to lawyers when financing their practices, banks in the United States do not generally lend to professional service businesses that do not have significant balance sheets. This situation leads to a fragmented, capital-hungry industry where no one law firm owns a significant percentage of the market for any type of tort claim in their primary state of practice.

Lawyers in the United States are limited in the way they can leverage their businesses. Larger, fee-based law firms doing corporate and defense work have long been able to obtain bank financing by pledging their receivables. However, subrogation and other contingency fee-based law firms have limited ability to access working capital financing from traditional banks. These firms are often forced to refer their cases out to larger trial firms and accept relatively small referral fees for their origination services because of their limited capital.

#### *Attorney Loans*

Like all specialty finance businesses, Case Funding's attorney loans are structured and administered with a focus on risk management.

In order to mitigate the potential for loss, an attorney loan made by Case Funding will always be in an amount significantly less than the contingency fees that Case Funding expects, after its own independent evaluation, the attorney is likely to earn from the basket of existing cases against which the advance is made. Case Funding's advance rate is a maximum of 20% of the expected total fees. Only cases already in progress are eligible for inclusion in a basket.

Repayment of Case Funding's attorney loans is required by contract to be made on a priority basis, meaning that a significant portion of attorney fees resulting from settlements of cases from the basket are usually required to be used first to repay the loan, further reducing the potential for loan losses. In cases where Case Funding deems the law firm to be creditworthy, revolving arrangements can be negotiated where such law firms pay on each recovery from an identified case and Case Funding re-advances funds against new cases in an amount that fits within its risk and "loan-to-value" guidelines. This generates additional income opportunities from known clients.

In the case of attorney advances, such terms generally include; guarantees of the law firm, guarantees of the partners (often joint and several), registered liens against all of the firm's cases, a direction that requires the trust accounts to repay Case Funding upon receipt of proceeds and that all proceeds are to be held in escrow when received; generous effective annual rates of interest (18% - 40%) of which a portion is paid monthly, and the balance is paid upon payout or partial payout; underwriting and origination fees; requirement to report on an ongoing basis the status of cases in the basket; provision of the firm's monthly bank statements; and notice provisions for all settled cases including copies of all remittance cheques.

Case Funding primarily uses in-house lawyers to evaluate new applications for loans and advances. Case Funding's lawyers review the case files of cases being offered by the attorneys, and arrive at their own assessment of expected fees for the entire basket. These lawyers also assist in our ongoing administration as it relates to the assessment of changes to any significant cases in each basket, including a formal review three times a year.

Case Funding's staff visits the office of all attorneys requesting a loan in excess of \$100,000 as a key part of the due diligence, in assessing an application. While the visit includes the examination of case files, it also includes an assessment of the firm itself, including confirming that information regarding the firm matches up with an onsite visit, such as staffing, number of partners, etc. The standing and license of each partner is verified with the state's bar association.

Because these loans often function as lines of credit for the attorneys, where amounts are repaid and then advanced again, against additional (and collateralized) cases, cash flow with respect to principal repayment is "lumpy" and the term is generally longer.

#### *Plaintiff Advances*

Plaintiff advances are made on the probability of success and potential claim size, not the plaintiff's credit score. The standard for this industry is that advances are made on a non-recourse, at-risk basis where the funder forfeits its entire advance and any related fees if the plaintiff is not successful in the lawsuit. Inherent to the underwriting process is the approval for funding of cases that have a high probability of success, to be achieved either in pre-trial settlement or as a result of a judgment by a court.

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Commercial banks in the United States have traditionally been unwilling to advance funding to plaintiffs or lawyers based on a contingent recovery, and lawyers are generally prohibited under state law from providing financial assistance to their clients. While the United States landscape is open to the use of plaintiff legal funding, the key issues of acceptability include rights of access to justice, lending and usury laws, legal ethics, champerty and maintenance restrictions, public policy and perception issues.

Plaintiff advances are made in smaller amounts and can therefore provide Case Funding with “smoother” cash flow and a diversification of risk. In addition, it is not unusual to make plaintiff advances, subject to Case Funding’s normal underwriting policies, in response to the requests of attorneys that are often clients of Case Funding.

*Medical Liens*

Case Funding has started funding medical liens, as they are very similar to plaintiff advances. There is tremendous demand for financing medical procedures and/or purchasing medical liens relating to plaintiff cases where the plaintiff has little or no insurance, but has a valid case that Case Funding would otherwise be willing to advance against (after undergoing the same underwriting process as performed on a plaintiff advance).

In addition, the medical lien business enables Case Funding to capitalize on the void within the closely wound networks of attorneys and medical providers trying to service their plaintiffs/patients but lacking funds to do so.

Medical liens are recourse debt obligations of the patient.

As of September 30, 2013, Case Funding employed 12 full-time equivalent employees.

**WINDSET CAPITAL CORPORATION**

Chesswood launched Windset, its new working capital loan business, in late September 2013. Windset provides working capital loans up to \$250,000 to tenured small businesses throughout the United States.

More than ever before, small business owners in the United States find that banks either will not consider them for working capital loans or the process of applying for a bank loan may take too long and the outcome is less than certain. Many U.S. banks can no longer afford to consider loans under \$250,000 due to their high internal administration and regulatory costs. While the working capital loan market that Windset joins is a newer market that sprung from the financial crisis, the significant demand for this product has been clearly demonstrated, as billions of dollars of loans have been originated since 2008. Payments are processed automatically and deducted every business day from the borrowers' bank account. The terms of these loans can range from 3 months to 18 months but are typically 9-10 months on average, and extensions are common for those borrowers that have been in good standing during the initial term of the loan.

Windset will leverage off of the equipment finance business expertise of Pawnee, and use its experience, processes and broker channel to offer this new product to small businesses throughout the U.S. Windset will rely on Pawnee's documentation, collection and administrative departments to provide "back-office" support to Windset, under the terms of a managed services agreement.

Capital for Windset's initial portfolio growth will be provided by making use of a modest portion of Pawnee's unused credit facility, allocated to Windset by agreement with Pawnee's lenders that is expected to be finalized early in the fourth quarter. Notwithstanding the \$250,000 limit on Windset loans, initial expectations are for loans that average \$30,000 to \$40,000.

Management believes that Windset provides Chesswood with the ability to expand its specialty finance business by generating superior risk adjusted returns, utilizing some of Pawnee's existing infrastructure and providing equipment leasing brokers with a working capital funder that understands their unique marketplace and needs.

At September 30, 2013, Windset had approximately \$75,000 in loans outstanding.

**SHERWAY LP AND CARS4U.COM**

Sherway LP, through its Acura Sherway dealership, sells new Acura brand vehicles and related automobile services and products, and also sells used vehicles of various brands. Lease-Win, whose portfolio of leases has been fully wound down, continues to operate cars4U.com, an edealer that offers new cars to consumers on a lease, finance or purchase basis.

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Chesswood's automotive business follows a seasonal pattern, with revenue and net earnings traditionally being significantly lower in the first quarter than in other quarterly periods.

### **MANAGEMENT'S DISCUSSION AND ANALYSIS**

The following management's discussion and analysis ("MD&A") is a review of the financial condition and financial performance of Chesswood Group Limited ("Chesswood" or the "Company") for the three and nine months ended September 30, 2013. This discussion should be read in conjunction with the audited consolidated financial statements and accompanying notes of the Company for the year ended December 31, 2012 set forth in the Company's 2012 Annual Report. The fiscal year of the Company ends on December 31. The date of this MD&A is November 1, 2013. All dollar amounts in this MD&A are Canadian dollars, unless otherwise indicated.

Through its interest in Pawnee Leasing Corporation ("Pawnee"), Chesswood is involved in the business of micro and small-ticket equipment finance to small businesses in the start-up and "B" credit market in the lower 48 states of the United States. Through its interest in Sherway LP, Chesswood is involved in selling, servicing and leasing Acura automobiles in the Province of Ontario. Through its interest in Case Funding Inc. ("Case Funding"), Chesswood is involved in the business of legal financing to plaintiffs and attorneys and the purchase of medical liens that form part of litigation throughout the United States. Through its interest in Windset Capital Corporation ("Windset"), Chesswood is becoming involved with the business of providing working capital loans to small businesses in the United States. Through its interest in Lease-Win Limited ("Lease-Win"), Chesswood owns and operates cars4U.com.

The Company prepares its financial statements in accordance with Canadian Generally Accepted Accounting Principles ("GAAP") as set out in The Handbook of the Canadian Institute of Chartered Accountants ("CICA Handbook"). In 2010, the CICA Handbook was revised to incorporate International Financial Reporting Standards ("IFRS"), and require publicly accountable enterprises to apply such standards effective for years beginning on or after January 1, 2011. Accordingly, the Company adopted IFRS as its basis of financial reporting commencing with the interim financial statements for the three-months ended March 31, 2011 using January 1, 2010 as the transition date (the "Transition Date").

This discussion contains forward-looking statements. Please see "Forward-Looking Statements" for a discussion of the risks, uncertainties and assumptions relating to these statements. This discussion makes reference to certain non-GAAP measures to assist in assessing the Company's financial performance. Non-GAAP measures do not have any standard meaning prescribed by GAAP and are therefore unlikely to be comparable to similar measures presented by other issuers. See "Non-GAAP Measures" for the definition of and reconciliation to GAAP measures of EBITDA and Adjusted EBITDA.

Our annual information form in respect of the fiscal year ended December 31, 2012 is available on SEDAR at [www.sedar.com](http://www.sedar.com), and provides additional information and should be read in conjunction with this report, management's discussion and analysis, consolidated financial statements and notes thereto.

On January 1, 2011, Chesswood Income Fund (the "Fund"), which until that date had been a publicly listed income fund, was converted into the Company, an Ontario corporation, through a plan of arrangement under the Business Corporations Act (Ontario). In connection with the conversion to a corporation, unitholders of the Fund exchanged their trust units of the Fund ("Fund Units") for common shares of the Company ("Common Shares") on a one-for-one basis.

Accordingly, the Company is considered a continuation of the Fund and the consolidated financial statements are prepared using the continuity of interests method. Under this method, the assets, liabilities and equity of the Fund transferred to the Company on the conclusion of the conversion transaction are recognized at their net carrying amount (after the effect of the adoption of IFRS). Due to the application of the continuity of interests method, some expressions, such as "Company" and "Fund", "unitholder" and "shareholder", "Fund Units" and "Common Shares", or "dividend" and "distribution", may be used to describe the activities throughout these consolidated financial statements, depending on whether the transaction occurred before or after the conversion.

### **FORWARD-LOOKING STATEMENTS**

In this report, management makes statements that are considered forward-looking statements. Forward-looking information consists of disclosure regarding possible events, conditions or results that is based on assumptions about future economic conditions and courses of action. Wherever used, the words "may", "could", "should", "will", "anticipate", "intend", "expect", "plan", "predict", "believe", and similar expressions identify forward-looking statements. These statements reflect



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management's current beliefs and are based on information currently available to management, but indicate management's expectations of future growth, results of operations, business performance, and business prospects and opportunities.

Forward-looking statements should not be read as guarantees of future performance or results, and will not necessarily be accurate indications of whether, or the times at which, such performance or results will be achieved. Forward-looking statements are based on information available at the time they are made, assumptions made by management, and management's good faith belief with respect to future events, and are subject to risks and uncertainties that could cause actual performance or results to differ materially from those expressed in forward-looking statements, historical results or current expectations. The Company assumes no obligation to publicly update or revise its forward-looking statements even if experience or future changes make it clear that any projected results expressed or implied therein will not be realized.

The Company operates in a dynamic environment that involves various risks and uncertainties, many of which are beyond the Company's control and which could have an effect on the Company's business, revenues, operating results, cash flow and financial condition, including without limitation:

- continuing access to required financing;
- continuing access to products to allow us to hedge our exposure to changes in interest rates;
- risks of increasing default rates on leases, loans and advances;
- our provision for credit losses;
- increasing competition (including without limitation, more aggressive risk pricing by competitors);
- increased governmental regulation of the rates and methods we use in financing and collecting on our equipment leases or loans, on the legal funding business generally and on our working capital loans;
- dependence on key personnel; and
- general economic and business conditions.

Readers should also carefully review the risk factors described under "Risk Factors" below and the risk factors described in the Company's annual information form filed with various Canadian securities regulatory authorities through SEDAR (the System for Electronic Document Analysis and Retrieval) at [www.sedar.com](http://www.sedar.com).

#### **KEY PERFORMANCE INDICATORS – PAWNEE**

Management regularly evaluates and analyzes key performance indicators, including the following, to more effectively operate Pawnee's business:

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**Pawnee Portfolio Statistics** (in U.S.\$ thousands except # of leases/loans and %'s)

	Dec 31 2011	Mar 31 2012	June 30 2012	Sep 30 2012	Dec 31 2012	Mar 31 2013	June 30 2013	Sep 30 2013
Number of leases and loans outstanding (#)	8,258	8,401	8,625	8,701	9,009	9,348	9,670	9,753
Gross lease and loan receivable ("GLR") <sup>(1)</sup>	\$130,601	\$134,613	\$140,605	\$141,971	\$150,125	\$163,311	\$173,092	\$175,208
Residual receivable	\$16,354	\$16,754	\$17,258	\$17,546	\$18,015	\$18,552	\$18,646	\$18,379
Net investment in leases and loans receivable, before allowance <sup>(4)</sup>	\$105,905	\$109,832	\$115,074	\$117,121	\$123,497	\$133,212	\$140,510	\$141,150
Security deposits (nominal value) <sup>(4)</sup>	\$11,233	\$11,478	\$11,854	\$12,074	\$12,378	\$12,669	\$12,770	\$12,635
Allowance for doubtful accounts – IFRS	\$2,198	\$1,990	\$2,259	\$2,629	\$2,950	\$3,098	\$3,128	\$3,522
Over 31 days delinquency (% of GLR) <sup>(2)</sup>	1.90%	1.54%	1.64%	1.98%	2.23%	1.99%	1.99%	2.12%
Net charge-offs for the three-months ended <sup>(3)</sup>	\$1,146	\$1,097	\$945	\$1,017	\$1,295	\$1,287	\$1,079	\$1,553
Provision for credit losses for the three-months ended – previous method	\$659	\$788	\$760	\$924	\$1,448	\$1,472	\$1,602	\$1,703
Provision for credit losses for the three-months ended – IFRS	\$980	\$968	\$1,238	\$1,431	\$1,635	\$1,515	\$1,370	\$1,832

## Notes:

- (1) Excludes residual receivable.
- (2) Over 31-days delinquency includes non-accrual gross lease and loan receivables. Pawnee ceases to accrue interest income on leases and loans after they become 94 days contractually past due unless information indicates that an earlier cessation of income is warranted and charges-off leases and loans when they become 154 days contractually past due, unless information indicates that an earlier charge-off is warranted.
- (3) Excludes the "charge-offs" of interest revenue on finance leases and loans on non-accrual leases recognized under IFRS.
- (4) Excludes adjustment for discounting security deposits and increasing unearned income for interest savings on security deposits.

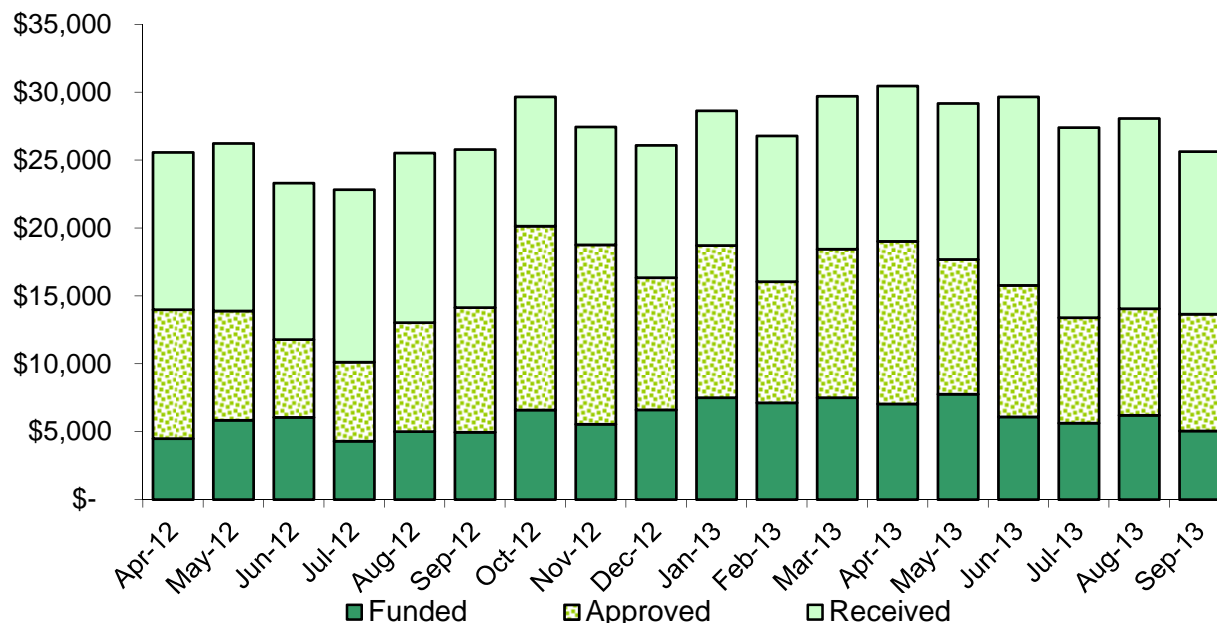
*Lease and Loan Application, Approval and Origination Volume*

Management regularly reviews lease and loan application, approval and origination volumes, for trends that may indicate changes in the economic or competitive landscape and that may necessitate adjustments in Pawnee's approach to doing business in its market segments. Pawnee also uses this data in its forecasting and budgeting process. Management reviews application approval data to analyze and predict shifts in the credit quality of Pawnee's applicants, and looks at individual broker approval rates to determine whether a broker is submitting applications that meet Pawnee's credit criteria. Pawnee refers to total originations as a percentage of leases and loans approved as the "closing ratio". Pawnee tracks and reviews the closing ratio to aid management in determining the efficiency and effectiveness of Pawnee's origination processes. Significant changes in any of these key metrics, as well as other less significant metrics, usually results in a more detailed review, which may include, amongst other things, a review of broker, industry or equipment type, equipment cost, or geographic areas for specific results.

Pawnee's lease originations were down in the quarter compared to the prior three quarters due to increased competition in the industry. Please see the "Outlook" section for a further discussion on this matter.

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**Lease and Loan Application, Approval and Origination Volume** (in thousands U.S.\$)



#### Asset Quality

Pawnee is a niche specialty finance company that is focused on doing business with commercial enterprises that are not usually considered by conventional financing sources and that generally have a higher risk profile. This exposes the firm to a greater risk level; however management has built an operating model that is based on managing this risk. As a result, Pawnee has been able to generate greater margins with lower volume than many typical finance companies.

Risk management begins with carefully selecting which independent brokers Pawnee does business with. Brokers must have personal credit profiles acceptable to Pawnee, industry references and preferably have been active in the equipment finance industry for a minimum of one year. Regional marketing managers are responsible for training and for developing a knowledge base with new and existing brokers regarding Pawnee's underwriting policies and procedures. This training process is very important in ensuring that neither the broker nor Pawnee spend extraordinary time in reviewing and handling applicants that can't meet Pawnee's basic qualifications. The managers are also responsible for monitoring the brokers for credit application review and closing efficiencies, including applications submitted, approved and ultimately funded.

The Pawnee credit process is not the automated scoring procedure typical of high volume equipment finance companies. A credit analyst reviews each application and manually completes a proprietary credit matrix which is used as a guide for reaching a prudent credit decision. The matrix is designed to ensure that all of Pawnee's analysts are consistent in their review of applications. Analysts are available to directly assist brokers submitting applications and communicate credit decisions, including what would make an applicant more likely to be approved. Pawnee applies several basic principles for all credit decisions on new leases and loans, including the requirement that all business owners personally guarantee the lease/loan and must therefore submit their personal credit information for consideration, and all scheduled payments must be paid through direct debit. All leases and loans assigned to Pawnee, must be approved by Pawnee in accordance with the same criteria used in originating its own leases and loans.

Pawnee's credit matrix undergoes continual review by management, in addition to periodic assessment by outside professionals with statistical expertise.

*Operating Efficiency*

Pawnee manages operating performance using, in addition to other tools, a comprehensive budgetary review process. Included in this review are line-item-level comparisons of revenues and expenses to budget and trend data for the period then ended. If management finds there is a significant or unusual variance from budget or expectations, management will review the variance in detail and take corrective action, if necessary. Management focuses its attention on significant changes from projections and takes appropriate action, as necessary.

Pawnee's static pool loss analysis measures lease/loan loss performance by identifying a finite pool of lease/loan originations and segmenting this pool into quarterly or annual vintages according to when the leases and loans were originated. Poorly performing brokers, geographic areas, equipment types and industries are reviewed in more detail to determine if there is a systematic or other identifiable cause on which corrective action can be taken. For example, if management determines that Pawnee has unusually high losses on leases/loans for a particular type of equipment, management may raise the minimum required credit matrix score for those leases/loans to be approved or stop originating leases/loans of that equipment type altogether.

*Collections*

The ability to efficiently service and collect on leases and loans is critical in achieving appropriate profit margins and stable cash flows. Management of Pawnee recognizes the importance of the ability to collect on leases/loans and, as such, a great deal of emphasis is placed on the employment and retention of experienced collection personnel. Over one-third of Pawnee's personnel dedicate their activities to the collections process. Pawnee's collections department is structured to systematically and quickly resolve delinquent leases and loans whenever possible, mitigate losses and collect post-default recovery dollars.

Pawnee's collections activities begin when a lease/loan initially becomes delinquent. An account is recognized as troubled if for any reason the direct debit payment is not successfully received on the required due date – the account is immediately considered delinquent. When the lease/loan becomes 31 days past due, or earlier if the collector recognizes that the problem is something more significant than a past due payment, the lease/loan is referred to the appropriate negotiation, repossession/remarketing, bankruptcy or legal specialist on the Advanced Collection team. Pawnee regularly remediates a high percentage of leases/loans that go initially past due.

The Advanced Collection team's objective is to minimize Pawnee's loss through a combination of collecting payments, writing forbearances, repossessing and selling financed equipment, initiating lawsuits and, most importantly, negotiating settlements. After 154 days of delinquency, or earlier if the Advanced Collection team determines the account is uncollectible, the lease/loan is charged off.

After an account is charged off, it may continue to be handled internally when collection prospects for recovery through a personal guarantor or other remedy are considered good. If not, it is normally assigned to an independent collection agency for additional collection efforts. At this stage in the collections process, the primary sources of recovery are payments on restructured accounts, settlements with guarantors, equipment sales, litigation and bankruptcy court distributions.

Throughout the collections process, Pawnee's repossession/remarketing specialists perform a wide variety of functions, including acting on repossession requests from any collector, managing third-party vendors that perform repossession activities, working with remarketers to establish and approve the selling price on all repossessed equipment, and selling equipment on behalf of Pawnee.

**KEY PERFORMANCE INDICATORS – CASE FUNDING**

As a specialty finance business that began operations without a portfolio, management initially monitored Case Funding's overhead expenses as they compared to budget, on an ongoing basis, as well as tracking and measuring originations by product type, for volume, pricing and in the case of attorney loans, credit quality.

As Case Funding has grown since June 2011, its portfolio, processes and systems are subject to ongoing enhancement and change, in monitoring, measurement and analyses.

All attorney loans are subject to conditional approval of a credit committee after having first been evaluated by Case Funding's credit underwriting. That conditional approval most often reflects the fact that a prospective attorney borrower's basket of cases must still meet Case Funding's legal underwriting criteria. Legal underwriting generally commences after a borrower's credit profile has been determined to meet Case Funding's standards.

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FOR THE THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2013

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Operationally, Case Funding monitors the collection of attorney interest payments (generally made monthly by ACH) and activity in the borrower's trust accounts, as two key steps out of a number of control measures, that provide effective monitoring tools of the borrower's payment history and settlement activity. There are a variety of other controls and processes in place to monitor these loans, including regularly scheduled updates from the borrowers, on the status of their cases.

Plaintiff advances are also subject to regularly scheduled updates from the plaintiff's attorney as to the status of the case and any changes that may have taken place since the last update. The plaintiff portfolio is also periodically examined for the aging of the advances and concentration by case types, amongst other metrics.

#### **KEY PERFORMANCE INDICATORS – SHERWAY LP**

Management monitors and analyzes a number of key indicators of the Acura Sherway dealership's operations, by profit centre/department. One key indicator for each department is the level of gross margins being generated – on a per unit and total volume basis. This measure, along with other metrics that may vary amongst departments, as applicable, is monitored daily, weekly and monthly. The analyses of these various metrics allows management to react quickly to trends, concerns and opportunities in each department, on a daily, weekly and/or monthly basis.

#### **NON-GAAP MEASURES**

The Company provides non-GAAP measures as supplementary information. Management believes EBITDA and Adjusted EBITDA are useful measures in evaluating the performance of the Company and in determining whether to invest in Common Shares. EBITDA and Adjusted EBITDA are not earnings measures recognized by GAAP and do not have standardized meanings prescribed by GAAP. Therefore, EBITDA and Adjusted EBITDA may not be comparable to similarly titled measures presented by other issuers. Investors are cautioned that EBITDA and Adjusted EBITDA should not be construed as an alternative to net income (loss) determined in accordance with GAAP as indicators of performance or to cash flows from operating, investing and financing activities as measures of liquidity and cash flows.

##### *Definitions of EBITDA and Adjusted EBITDA*

“EBITDA” is defined as net income (loss) adjusted to exclude interest, income taxes, depreciation and amortization.

“Adjusted EBITDA” is defined as EBITDA adjusted for (i) interest on leasing and vehicle credit lines, (ii) non-cash gain (loss) on interest rate swaps, (iii) non-cash unrealized gain (loss) on foreign exchange, (iv) non-cash share-based compensation expenses, (v) non-cash fair value adjustments on other liabilities, and (vi) the non-cash loss on sale of property and equipment.

Management refers to operating income in the MD&A which equals income before undernoted items presented on the consolidated statement of income.

## FOR THE THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2013

**Adjusted EBITDA <sup>(1)</sup>**

For the quarter-ended (\$ thousands)	2011	2012				2013		
	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3
Net income	\$2,629	\$1,901	\$2,307	\$1,558	\$3,223	\$2,994	\$3,329	\$2,872
Interest expense	913	901	928	918	906	929	1,046	1,076
Provision for taxes	1,628	1,998	1,863	1,677	2,100	2,146	2,577	2,146
Amortization	187	183	172	164	160	165	89	47
<b>EBITDA <sup>(1)</sup></b>	<b>\$5,357</b>	<b>\$4,983</b>	<b>\$5,270</b>	<b>\$4,317</b>	<b>\$6,389</b>	<b>\$6,234</b>	<b>\$7,041</b>	<b>\$6,141</b>
Interest expense	(913)	(901)	(928)	(918)	(906)	(929)	(1,046)	(1,076)
Share-based compensation expense	373	427	329	334	346	365	416	289
Contingent consideration <sup>(4)</sup>	43	43	47	48	(863)	—	—	—
Foreign exchange loss (gain)	(120)	53	(240)	338	(208)	(204)	166	22
Unrealized loss (gain) – interest rate swaps	(238)	(161)	203	169	(218)	(260)	(730)	(47)
<b>Adjusted EBITDA <sup>(1)</sup></b>	<b>\$4,502</b>	<b>\$4,444</b>	<b>\$4,681</b>	<b>\$4,288</b>	<b>\$4,540</b>	<b>\$5,206</b>	<b>\$5,847</b>	<b>\$5,329</b>

**SELECTED FINANCIAL INFORMATION**

As at and for the quarter-ended (\$ thousands, except per share figures)	2011	2012				2013		
	Q4	Q1	Q2	Q3	Q4(4)	Q1	Q2	Q3
Revenue <sup>(5)</sup>	\$21,767	\$19,174	\$23,142	\$21,474	\$22,806	\$19,778	\$24,354	\$24,935
Gross margin before expenses <sup>(5)</sup>	8,501	8,017	8,633	8,228	8,358	8,980	10,138	9,766
Income before tax, and gain (loss) on interest rate swaps, and fx	3,942	3,834	4,180	3,790	4,034	4,676	5,342	4,993
Income before tax	4,257	3,899	4,170	3,235	5,323	5,140	5,906	5,018
Provision for taxes	1,628	1,998	1,863	1,677	2,100	2,146	2,577	2,146
Net income	\$2,629	\$1,901	\$2,307	\$1,558	\$3,223	\$2,994	\$3,329	\$2,872
Basic earnings per share <sup>(2)(3)</sup>	\$0.24	\$0.17	\$0.20	\$0.14	\$0.29	\$0.26	\$0.30	\$0.25
Diluted earnings per share <sup>(2)(3)</sup>	\$0.23	\$0.16	\$0.20	\$0.13	\$0.28	\$0.25	\$0.28	\$0.23
Total assets	147,366	149,431	163,214	153,742	161,395	174,446	190,371	187,782
Long-term financial liabilities	77,428	77,007	89,302	83,220	86,381	96,170	112,170	107,335
<u>Other Data</u>								
Adjusted EBITDA <sup>(1)(4)</sup>	\$4,502	\$4,444	\$4,681	\$4,288	\$4,540	\$5,206	\$5,847	\$5,329
Dividends declared <sup>(3)</sup>	1,691	1,694	1,809	1,867	1,869	1,983	2,047	2,057
Dividends declared per share <sup>(2)(3)</sup>	\$0.15	\$0.15	\$0.16	\$0.165	\$0.165	\$0.175	\$0.18	\$0.18

(1) Adjusted EBITDA and EBITDA are non-GAAP measures. See “Non-GAAP Measures” for the definition of Adjusted EBITDA and EBITDA.

(2) Based on weighted average shares outstanding during period.

(3) Includes dividends on Exchangeable Securities (non-controlling interest as described below under "Statement of Financial Position").

(4) While Case Funding continues to grow and shows promise, the projected results are less than the original forecasts used as a basis for the contingent consideration. It has been determined that the estimated probability that Chesswood will have to pay the contingent consideration and bonus in June 2014 is extremely low. The \$850,000 accrual at September 30, 2012, relating to the contingent consideration (\$680,000) and bonus (\$170,000) was reversed in Q4 2012. While management believes the \$399,000 deferred tax asset at Case Funding will be realized, given the

**FOR THE THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2013**

uncertainty of forecasting the growth of Case Funding, the timing of the utilization of the tax losses was not certain and thus the deferred tax asset established in Q4 2011 was reversed in Q4 2012. Previously disclosed quarterly Adjusted EBITDA amounts did not consider contingent consideration and bonus, the calculation of quarterly Adjusted EBITDA was updated in Q4 2012.

(5) Canadian automotive business represents approximately 55.3% of the Company's total revenue, however only represents approximately 18.1% of the Company's gross margin before expenses. The Canadian automotive revenue can significantly fluctuate throughout the year and year-to-year based on seasonality, sales volumes and market conditions with little effect to the Company's gross margin before expenses.

**RESULTS OF OPERATIONS FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2013 AND 2012**

Pawnee and Case Funding's U.S. dollar results for the nine months ended September 30, 2013 were converted at approximately 1.0235, which was the average exchange rate for the nine month period. The U.S. dollar results for the nine months ended September 30, 2012 were converted at approximately 1.0023, which was the average exchange rate for the corresponding period.

Please see Note 21 – *Segment Information* in the notes to the Company's consolidated financial statements for a breakdown of operating results and other information by industry segment and/or geographic location.

For the nine months ended September 30, 2013, the Company reported consolidated net income of \$9.2 million compared to \$5.8 million in the same period in the prior year, an increase of \$3.4 million year-over-year.

For the nine months ended September 30, 2013, the Company reported consolidated operating income ("income before undernoted items") of \$15.0 million compared to \$11.8 million in the same period in the prior year, an increase of \$3.2 million year-over-year.

The \$3.2 million increase in operating income for the nine month period year-over-year was the result of:

- An increase in Pawnee's operating income by \$2.1 million in the nine month period compared to the prior year, predominantly from a \$3.6 million increase in finance income due to a larger portfolio offset by a \$1.2 million increase in provision for credit losses and a \$504,000 increase in personnel and other expenses compared to the prior year. In the nine month period, Pawnee's actual net charge-offs increased by U.S.\$860,000 year-over-year, predominantly from the increase in leases outstanding year-over-year. Pawnee's amortization expense decreased \$194,000 year-over-year in the nine month period as the broker network intangible asset was fully depreciated by the end of April 2013, seven years after the acquisition of Pawnee although the broker network remains viable and largely unchanged since acquisition.
- Case Funding's operating income for the nine month period increased by \$886,000 year-over-year and totaled \$572,000 compared to a loss of \$314,000 in the prior year. Case Funding was acquired on June 10, 2011, however Chesswood did not acquire Case Funding's existing loan portfolio. Case Funding has been gradually building its own legal finance receivables portfolio since June 2011. The increase in finance revenue of \$1.2 million in the period year-over-year reflects the growth in the portfolio.
- Automotive operations income increased \$595,000 year-over-year reflecting an increase in income from Sherway of approximately \$350,900, and the absence of \$244,100 in net expenses for Lease-Win. New vehicle sales increased by 43 vehicles in the nine month period, due in part to the introduction of new models. Automotive revenue from Lease-Win was down \$618,000 in the nine month period compared to the prior year, and gross profit from Lease-Win was down \$182,000 which reflects the wind-down and eventual sale of its remaining automotive leases in August 2012.
- Corporate overhead before foreign exchange increased by \$362,000 year-over-year, predominantly from a \$178,000 increase in general and administrative expenses and \$124,000 increase in share-based compensation expense.

The provision for taxes for the nine months ended September 30, 2013 totaled \$6.9 million compared to \$5.5 million in the same period of the prior year. The \$6.9 million provision for taxes for the nine months ended September 30, 2013 is comprised of \$10.0 million in current tax expense, \$439,000 in withholding tax on intercompany dividends and a reduction in future taxes payable of \$3.6 million.

**RESULTS OF OPERATIONS FOR THE THREE MONTHS ENDED SEPTEMBER 30, 2013 AND 2012**

Pawnee and Case Funding's U.S. dollar results for the three months ended September 30, 2013 were converted at approximately 1.0386, which was the average exchange rate for the three month period. The U.S. dollar results for the three months ended September 30, 2012 were converted at approximately 0.9953, which was the average exchange rate for the corresponding period.

Please see Note 21 – *Segment Information* in the notes to the Company's consolidated financial statements for a breakdown of operating results and other information by industry segment and/or geographic location.

For the three months ended September 30, 2013, the Company reported consolidated net income of \$2.9 million compared to \$1.6 million in the same period in the prior year, an increase of \$1.3 million year-over-year.

For the three months ended September 30, 2013, the Company reported consolidated operating income ("income before undernoted items") of \$5.0 million compared to \$3.8 million in the same period in the prior year, an increase of \$1.2 million year-over-year.

The \$1.2 million increase in operating income for the three month period year-over-year was the result of:

- An increase in Pawnee's operating income by \$814,000 in the three month period compared to the prior year, predominantly from a \$1.4 million increase in finance income due to a larger portfolio offset by a \$478,000 increase in provision for credit losses and a \$253,000 increase in personnel and other expenses compared to the prior year. In the three month period, Pawnee's actual net charge-offs increased by U.S.\$536,000 year-over-year consistent with the growth in the portfolio. Pawnee's amortization expense decreased \$120,000 year-over-year in the three month period as its broker network intangible asset was fully depreciated by the end of April 2013, seven years after the acquisition of Pawnee although the broker network remains viable and largely unchanged since acquisition.
- Case Funding's operating income for the three month period increased by \$208,000 year-over-year and totaled \$134,000 compared to a loss of \$74,000 in the prior year. The increase in finance revenue of \$302,000 in the three month period year-over-year reflects the growth in the portfolio year-over-year. The \$160,000 decrease in finance revenue from the previous quarter is the result of adjusting estimates on the timing of the collection of medical liens and outstanding plaintiff advances.
- Automotive operations income increased \$280,000 year-over-year reflecting an increase in income from Sherway of approximately \$172,000, and the absence of approximately \$108,000 in net expenses for Lease-Win. New vehicle sales at Sherway increased by 22 vehicles in Q3 2013 compared to Q3 2012, and higher gross profit per vehicle year-over-year contributed to the increase in Sherway's operating income.
- Corporate overhead before foreign exchange increased by \$99,000 year-over-year, predominantly from an \$110,000 increase in general and administrative expenses and \$41,000 increase in share-based compensation expense offset by a reduction in personnel expenses of \$52,000 due to timing of bonus accruals in the prior year.

The provision for taxes for the three months ended September 30, 2013 totaled \$2.1 million compared to \$1.7 million in the same period of the prior year. The \$2.1 million provision for taxes for the three months ended September 30, 2013 is comprised of \$7.1 million in current tax expense, \$142,200 in withholding tax on intercompany dividends and a reduction in future tax payable of \$5.1 million.

**STATEMENT OF FINANCIAL POSITION**

Total consolidated assets of the Company at September 30, 2013 were \$187.8 million, an increase of \$26.4 million from December 31, 2012. The exchange rate on September 30, 2013 was 1.0285 compared to 0.9949 at December 31, 2012. The change in the foreign exchange rate increased assets by \$4.8 million, thus total assets excluding the foreign exchange impact increased by \$21.6 million from December 31, 2012.



**FOR THE THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2013**

Cash totaled \$5.2 million at September 30, 2013 compared to \$5.6 million at December 31, 2012, a decrease of approximately \$377,000. At September 30, 2013, approximately U.S.\$7.2 million (December 31, 2012 – U.S.\$8.1 million) that could have been sent up to Chesswood was still at Pawnee, being utilized to fund portfolio growth and to lower interest costs. This is one of Chesswood's best avenues for deploying cash resources.

Accounts receivable totaled \$1.5 million at September 30, 2013 compared to \$771,000 at December 31, 2012. The accounts receivable balance principally relates to the Acura Sherway dealership and includes amounts due from the manufacturer for financing contracts in transit, which are typically collected within seven to ten days, and are usually at their highest levels at month end. Vehicle receivable balances fluctuate throughout the year based on seasonality, and sales volumes of the industry.

Inventory totaled \$7.1 million at September 30, 2013 compared to \$7.9 million at December 31, 2012, a decrease of \$0.8 million. Vehicle inventory balances at dealerships fluctuate throughout the year based on seasonality, sales volumes and market conditions.

Prepaid expenses and other assets total \$0.6 million at September 30, 2013, a decrease of \$341,000 from December 31, 2012.

Finance receivables consist of the following:

	<b>September 30, 2013</b>	June 30, 2013	December 31, 2012
		<i>(\$ thousands)</i>	
Net investment in leases	<b>\$ 124,791</b>	\$ 128,739	\$ 111,905
Equipment financing agreements ("EFAs", "loans")	<b>16,756</b>	14,275	6,700
Legal finance receivables	<b>9,068</b>	8,175	5,645
	<b><u>\$ 150,615</u></b>	<u>\$ 151,189</u>	<u>\$ 124,250</u>

The finance receivables in Canadian dollars are down compared to June 30, 2013 primarily due to the drop in the foreign exchange rate which was 1.0512 at June 30, 2013 and 1.0285 at September 30, 2013, which translated to a \$3.3 million decrease. As well, Pawnee's lease originations were down in the quarter compared to the prior three quarters due to increased competition in the industry (please see the "Outlook" section for a further discussion on this matter).

As at September 30, 2013, net investment in leases and EFAs totaled \$141.5 million compared to \$118.6 million at December 31, 2012, an increase of \$22.9 million or 19.3%. The gross receivable of leases and loans under administration as at September 30, 2013 was approximately \$180.2 million (U.S.\$175.2 million), compared to \$149.3 million (U.S.\$150.1 million) at December 31, 2012.

The \$141.5 million in net investment in leases and loans is net of \$3.7 million in allowance for doubtful accounts compared to \$2.9 million in allowance for doubtful accounts at December 31, 2012. Under IFRS, an allowance can only be set up if there is objective evidence that the impairment has already occurred; potential losses expected as a result of future events, no matter how likely based on past historical evidence, are not allowed to be recognized. Pawnee charges-off leases and EFAs when they become 154 days contractually past due, unless information indicates that an earlier charge-off is warranted. A high percentage of the charge-offs are made before the subject leases/EFAs reach 154 days contractually past due. As only a small percentage of the total lease and EFA receivable portfolio have monthly payments that are past due at any one reporting date, the portion of the receivables that shows observable objective evidence of impairment at any one reporting date is quite small, despite long-term historical experience that indicates that future charge-offs with respect to the current lease and loan (EFAs) receivable will typically exceed the level of observable impairment, in a matter of months.

Unlike certain other equipment finance companies, Pawnee does not sell any of its lease or loan (EFA's) receivables. All receivables originated by Pawnee are retained for their full term. Pawnee funds its leases and loans through a floating rate facility offered by a banking syndicate, as discussed below.

Legal finance receivables consist of funds advanced to plaintiffs, attorneys, and for the purchase of medical liens relating to plaintiff cases. At September 30, 2013, there were 501 advances and loans outstanding (December 31, 2012 – 366 advances and loans). The advances and loans are due when the underlying cases are settled; however, attorney borrowers do make partial monthly interest payments that are generally equal to at least half of the interest accruing on the loan. These payments are collected through automatic monthly debits to the borrowers' bank accounts.

**FOR THE THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2013**

Interest income is recognized for accounting purposes by estimating the collection date and thus total funds to be collected, from which income can be determined on an effective interest basis. During the quarter, management adjusted estimates on medical lien loans and plaintiff advances resulting in a decrease in the quarterly finance revenue from legal finance receivables.

# of Days Outstanding (**)	1day -> 90 days	91 days -> 180 days	181 days -> 365 days	366 days ->	Total
# of loans & advances	93	66	168	174	501
\$ thousands	\$1,738	\$1,327	\$3,480	\$2,523	\$9,068

*(\*\*)The advances and loans are due when the underlying cases are settled; the number of days the receivable is outstanding does not necessarily indicate the likelihood of impairment. It is normal for receivables in this industry to be outstanding anywhere from 6 months to 48 months.*

Under IFRS, an allowance for the collectability of the legal finance receivables can only be set up if there is objective evidence that the impairment has already occurred; potential losses expected as a result of future events, no matter how likely based on past historical evidence or known uncertainties with this type of receivable, are not allowed to be recognized.

The collectability of loans and/or advances made by Case Funding depends on litigation outcomes in the form of judgments and/or settlements. Once an advance/loan is made, the timing of the collection cycle is out of Case Funding's control. Therefore, the timing of actual collections will be irregular. At September 30, 2013, Case Funding is not aware of any situation where the collection of a receivable is doubtful and thus there is no observable objective evidence of impairment and therefore no basis for establishing an allowance for doubtful accounts under IFRS; however historical experience and the uncertainties involved would indicate that Case Funding will not collect 100% of the loans and advances. Case Funding's pricing to the markets it serves, reflects this fact.

Additions to property and equipment totaled \$466,500 for the nine months ended September 30, 2013. Approximately \$365,871 was spent on computer hardware and systems, the majority of which was spent at Pawnee and Windset. Approximately \$86,700 of the property and equipment additions in the current year (and \$140,300 in total) relates to architect and other preliminary costs associated with Sherway's re-imaging upgrade of the dealership. While not final, the current estimate of costs for the project is between \$2.0 million and \$2.5 million. Initial funding for the re-imaging upgrade will be funded by Sherway's bank. Once complete, a large portion of the costs will be reimbursed by Acura Canada. The construction is currently expected to start in late 2013 or early 2014. At September 30, 2013, approximately \$140,300 of the renovation costs was not being amortized as it relates to leaseholds improvements being upgraded.

Intangible assets totaled \$6.8 million at September 30, 2013 relatively unchanged from December 31, 2012. The net change in intangible assets is comprised of \$169,300 in amortization of broker relationships and a \$197,000 increase as the result of the change in foreign exchange rates. The significant intangible assets of broker relationships and trade names do not require any outlay of cash to be maintained, as the creation of lease and loan receivables does not require an outlay of cash, other than commissions, which are separately expensed.

Goodwill totaled \$14.3 million at September 30, 2013 compared to \$13.9 million at December 31, 2012. The movement in the foreign exchange rate resulted in an increase of \$383,000 in goodwill during the nine months ended September 30, 2013. Goodwill is typically tested annually for impairment unless certain circumstances arise that would require an assessment prior to an annual review.

Accounts payable and other liabilities totaled \$7.7 million at September 30, 2013 compared to \$8.3 million at December 31, 2012, a decrease of \$0.6 million. Current taxes paid at Pawnee represented the majority of the decrease. See Note 10 for more detail on the balances that comprise accounts payable and other liabilities.

Vehicle inventory is financed through vehicle financing credit facilities, of which \$6.0 million was outstanding at September 30, 2013 compared to \$6.2 million at December 31, 2012, leaving \$1.2 million of inventory that was self-financed as at September 30, 2013 compared to \$1.7 million self-financed at December 31, 2012. Vehicle inventory balances at dealerships fluctuate throughout the year based on seasonality, sales volumes and market conditions.

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 FOR THE THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2013
 

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Pawnee enters into interest rate swap agreements with its principal lender under its banking facility that provides for payment of an annual fixed rate, in exchange for a LIBOR based floating rate amount. Pawnee's bank has the option to terminate the swaps typically one year prior to the maturity date. The interest rate swaps are intended to offset a portion of the variable interest rate risk on the credit facility. At September 30, 2013, the mark-to-market adjustment is a loss of approximately \$1.5 million compared to a loss of approximately \$2.5 million at December 31, 2012 and is shown as a liability on the statement of financial position.

The following interest rate swaps were outstanding at September 30, 2013:

<b>Effective Date</b>	<b>Notional Amount U.S.\$</b>	<b>Annual Fixed Rate</b>	<b>Maturity date</b>
March 2011	\$15 million	3.12%	March 2014
March 2012	\$15 million	4.00%	March 2015
April 2013	\$15 million	0.96%	April 2016
March 2014	\$15 million	1.33%	March 2016
March 2015	\$15 million	1.56%	March 2017

Pawnee's interest rate swaps are not considered trading instruments as it intends to hold them until maturity. Nonetheless, the interest rate swaps do not qualify as a hedge for accounting purposes, and are therefore recorded as a separate derivative financial instrument. Accordingly, the estimated fair value of the interest rate swaps is recorded as a liability on the accompanying consolidated statement of financial position. Payments made and received pursuant to the terms of the interest rate swaps and adjustments to the fair value of the interest rate swaps are recorded as gain or loss on interest rate swaps. The fair value of interest rate swaps is based upon the estimated net present value of cash flows.

Borrowings totaled \$71.7 million at September 30, 2013 compared to \$47.6 million at December 31, 2012. Pawnee was utilizing U.S.\$70.2 million of its credit facility at September 30, 2013 compared to U.S.\$48.3 million at December 31, 2012. The increase in the borrowings reflects the final 2012 dividend payment to Chesswood which must be taken by the end of April of the following year, and tax payments for 2012 and 2013. At September 30, 2013, approximately U.S.\$7.2 million (December 31, 2012 – U.S.\$8.1 million) that could have been sent up to Chesswood was still at Pawnee, being utilized to fund portfolio growth and to lower interest costs.

In July 2012, Pawnee renewed and expanded its credit facility, the credit facility limit was increased by U.S.\$30.0 million to U.S.\$85.0 million, while the accordion feature of the loan agreement has been increased to U.S.\$115.0 million from U.S.\$85.0 million. Pawnee's borrowings under the credit facility are subject to, among other things, adhering to certain percentages of eligible gross lease/loan receivables, and the maintenance of a minimum debt to tangible net worth ratio. This credit facility is secured by substantially all of Pawnee's assets, contains negative covenants including the maintaining of leverage and interest coverage ratios, requires Pawnee to mitigate its interest rate risk by entering interest rate swaps for a notional amount not less than 50% of the outstanding amount, and matures on July 24, 2016. Pawnee was in full compliance with all its bank covenants during the period.

Pawnee's syndicate of lenders is in the process of finalizing amendments to the current banking agreement that will provide Windset with access to a maximum of US\$5.0 million of capital from Pawnee's credit facility. No significant changes are expected to Pawnee's covenants under the credit facility, as a result of this new availability.

The \$11.6 million (December 31, 2012 – \$11.0 million) in customer security deposits relates to security deposits held by Pawnee. Pawnee's primary contracts requires that the lessee/borrower provide two payments as security deposit (not advance payments), which are held for the full term of the lease and then returned or applied to the purchase option of the equipment at the lessee's request, unless the lessee has previously defaulted (in which case the deposit is applied against the lease receivable). Historically, a very high percentage of lessees' deposits are either applied to the purchase option of the leased equipment at the end of the lease term or used to offset charge-offs. Approximately \$371,000 of the increase is the result of the change in the foreign exchange rate.

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FOR THE THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2013

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Future taxes payable at September 30, 2013 totaled \$22.5 million compared to \$25.3 million at December 31, 2012, a decrease of \$2.8 million. The decrease in future taxes payable is the result of a future tax reduction of approximately \$3.6 million and a \$0.8 million increase as a result of the change in the foreign exchange rate.

Pawnee has benefited from the accelerated bonus depreciation rules introduced in 2007 as part of the U.S. Economic Stimulus Act and has therefore been able to utilize a portion of operating cash flows normally used to pay taxes, to fund portfolio growth. While the “fiscal cliff” legislation, passed in early January 2013, extended bonus depreciation until the end of 2013, Pawnee will be required to pay taxes in 2013, after having taken full advantage of available bonus depreciation. Pawnee expects to make tax installment payments throughout 2013. The actual taxes payable for 2013 will be dependent on the growth of its lease portfolio in 2013 and is inherently difficult to predict. Pawnee has sufficient capital resources, including its line of credit, through which to satisfy its taxation obligations and fund its portfolio growth.

Tax at Pawnee is provided for using the asset and liability method of accounting. This method recognizes future tax assets and liabilities that arise from differences between the accounting basis of the subsidiary’s assets and liabilities and their corresponding tax basis.

At September 30, 2013, there were 9,958,882 Common Shares outstanding (excluding the shares issuable in exchange for the Exchangeable Securities, as defined below) with a book value of \$45.1 million. Including the Exchangeable Securities, Chesswood would have had 11,437,419 Common Shares outstanding.

In August 2012, the Board of Directors approved the repurchase and cancellation of up to 658,943 of the Company’s outstanding Common Shares for the period commencing August 25, 2012 and ending on August 24, 2013. During the nine months ended September 30, 2013, no Common Shares had been repurchased under this normal course issuer bid. In August 2013, the Board of Directors approved the repurchase and cancellation of up to 688,614 of the Company’s outstanding Common Shares for the period commencing August 25, 2013 and ending on August 24, 2014. During the period, no Common Shares had been repurchased under the renewed normal course issuer bid. Decisions regarding the timing of purchases are based on market conditions and other factors.

Non-controlling interest is comprised of the Exchangeable Securities, being the 1,274,601 Class B common shares and 203,936 Class C common shares of Chesswood U.S. Acquisitionco Ltd. (“U.S. Acquisitionco”), which were issued as partial consideration for the acquisition of Pawnee and are fully exchangeable at any time for Common Shares, on a one-for-one basis, through a series of steps. Attached to the Exchangeable Securities are Special Voting Shares of the Company which provide the holders of the Exchangeable Securities voting equivalency to holders of Common Shares. Under IAS 27, the Exchangeable Securities must be shown as non-controlling interest because they are equity in a subsidiary not attributable, directly or indirectly, to the parent (even though they have no voting powers in the subsidiary only in the parent company and are fully exchangeable into the equity of the parent for no additional consideration and receive the same dividends as the common shares of the parent company). When the non-controlling interest was moved from Other liabilities back to the shareholders’ equity section on January 1, 2011 (the date the Fund converted to a corporation), per IFRS, the value attributed to the non-controlling interest was just the fair value of the equivalent Common Shares (closing value of Fund Units on the Toronto Stock Exchange on December 31, 2010) as the Exchangeable Securities are fully exchangeable into Common Shares. Their portion of the cumulative income and dividends from May 2006 to January 1, 2011 was not allocated to non-controlling interest; however, their portion of income and dividends has since been allocated to non-controlling interest.

Reserve represent the accumulated share-based compensation expensed over the vesting term for options and restricted share units unexercised at September 30, 2013.

Accumulated other comprehensive loss is the cumulative translation difference between the exchange rate on January 1, 2010, the IFRS adoption date and the exchange rate on September 30, 2013 of self-sustaining foreign operations net assets.

## **LIQUIDITY AND CAPITAL RESOURCES OVERVIEW**

The primary sources of cash for the Company and its subsidiaries have been cash flows from operating activities, and borrowings under its various subsidiaries’ credit facilities. The primary uses of cash for the Company and its subsidiaries are to fund equipment leases and loans, long-term debt principal repayments and dividends.

The Company’s subsidiaries’ objective is to maintain low cash balances, investing any free cash in their operations as needed and using any excess to pay down debt on the primary financing facilities. The subsidiaries fund working capital needs, lease and loan originations and growth using advances under credit facilities available when operating cash flow is not sufficient.

**FOR THE THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2013**

At September 30, 2013, the Company's operating units had \$16.0 million in additional borrowings available under various credit facilities to fund business operations; however, Chesswood anticipates injecting up to \$2.0 million of additional equity into Pawnee during 2013 to support its growth.

The Company itself does not have any credit facility. The subsidiaries' respective credit facilities are used to provide funding for the subject subsidiary's operations (i.e. to provide financing for the purchase of assets which are to be the subject of leases and loans or to acquire vehicle inventory and support working capital), other than Case Funding which is in the process of seeking a banking partner. The credit facilities are not intended to directly fund dividends by the Company (and these facilities generally limit the amount which can be distributed to the Company to the net income of the subject subsidiary).

Sherway is developing plans for a re-imaging upgrade of its dealership. While not final, the current estimated costs for the project are between \$2.0 million and \$2.5 million. Initial funding for the re-imaging upgrade will be funded by Sherway's bank. Once complete, a large portion of the costs will be reimbursed by Acura Canada. The construction is currently expected to start in late 2013 or early 2014.

Pawnee has benefited from the accelerated bonus depreciation rules introduced in 2007 as part of the U.S. Economic Stimulus Act and has therefore been able to utilize a portion of operating cash flows normally used to pay taxes, to fund portfolio growth. While the "fiscal cliff" legislation, passed in early January 2013, extended bonus depreciation until the end of 2013, Pawnee will be required to pay taxes in 2013, after having taken full advantage of available bonus depreciation. Pawnee expects to make tax installment payments throughout 2013. The actual taxes payable for 2013 will be dependent on the growth of its lease portfolio in 2013 and is inherently difficult to predict. Pawnee has sufficient capital resources, including its line of credit, through which to satisfy its taxation obligations and fund its portfolio growth.

The following are the contractual principal payments and maturities of financial liabilities and other commitments:

(\$ thousands)	2013	2014	2015	2016	2017 +	Total
Accounts payable and other liabilities	\$7,588	\$26	\$29	\$31	\$14	<b>\$7,688</b>
Vehicle financing	5,969	-	-	-	-	<b>5,969</b>
Interest rate swaps	-	224	867	183	257	<b>1,531</b>
Borrowings (a)	-	-	-	71,667	-	<b>71,667</b>
Customer security deposits (b)	1,177	2,943	3,056	2,493	1,953	<b>11,622</b>
	<b>\$14,734</b>	<b>\$3,193</b>	<b>\$3,952</b>	<b>\$74,374</b>	<b>\$2,224</b>	<b>\$98,477</b>
Other financial commitments ( c)	205	823	796	739	360	<b>2,923</b>
<b>Total commitments</b>	<b>\$14,939</b>	<b>\$4,016</b>	<b>\$4,748</b>	<b>\$75,113</b>	<b>\$2,584</b>	<b>\$101,400</b>

- a. Pawnee's financing credit facility is a line-of-credit; as such the balance can fluctuate. The credit facility matures in 2016. The interest rate has a floating component, thus the interest payments are dependent on the balance of the line of credit and the interest rate at any point of time.
- b. The Company's experience has shown that the actual contractual payment streams will vary depending on a number of variables including: prepayment rates, charge-offs and modifications. Accordingly, the scheduled contractual payments of customer security deposits shown in the table above are not to be regarded as a forecast of future cash payments.
- c. The Company and its subsidiaries are committed to future minimum rental payments under existing leases for premises, excluding occupancy costs and property tax, expiring in 2015 and 2017. The leases contain renewal options for an additional term of 5 years.

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FOR THE THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2013

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The Company has no material “off-balance sheet” financing obligations, except for long-term premises lease agreements. Other commitments are disclosed in Note 30 of the annual consolidated financial statements.

### **Cash Sources and Uses**

The statement of cash flows, which is compiled using the indirect method, shows cash flows from operating, investing, and financing activities, and the Company’s cash and cash equivalents at the beginning and end of the year. Cash flows in foreign currencies have been translated at the average rate for the period. Cash flow from operating activities comprises net income (loss) adjusted for non-cash items, changes in working capital and operational net assets. Receipts and payments with respect to tax are included in cash from operating activities. The Company considers net investment in leases, net investment in leases – pledged, legal finance receivables, vehicle financing, borrowings, securitization debt and customer security deposits as operational assets and liabilities as they directly relate to our core business. The changes in these operational assets and liabilities are shown in cash flows from operating activities and the associated interest revenue and interest expenses are included in operating activities and not investing or financing activities. Cash flow from investing activities comprises payments relating to the acquisition of companies and property and equipment. Cash flow from financing activities comprises payment of dividends, proceeds from stock issues, and the purchase and sale of treasury stock.

#### *For the nine months ended September 30, 2013*

The Company’s operations generated cash flow from operations before the changes in operating assets and liabilities of \$23.3 million during the nine months ended September 30, 2013 compared to \$18.7 million in the nine months ended September 30, 2012, an increase of \$4.6 million compared to the same period in the prior year.

The Company’s operations generated cash flow from operations of \$5.8 million during the nine months ended September 30, 2013 compared to \$5.3 million in the nine months ended September 30, 2012, an increase of \$517,000 compared to the same period in the prior year. Chesswood had net tax payments of \$11.4 million in the nine months ended September 30, 2013 compared to \$1.9 million in the same period in the prior year. The amount of cash flow Chesswood directed to the growth in Case Funding’s legal finance portfolio in the nine month period increased by \$1.0 million year-over-year.

Capital expenditures totaled \$466,500 (2012 – \$190,000) during the nine months ended September 30, 2013.

The Company paid dividends to the holders of Common Shares and Exchangeable Securities in the amount of \$6.0 million during the nine months ended September 30, 2013 compared to \$5.3 million in the same period in the prior year; an increase of \$713,000 due to a higher number of shares outstanding and higher dividend per share amounts year-over-year.

In total, in the nine months ended September 30, 2013, there was a decrease in cash of \$0.4 million compared to a decrease of \$0.8 million in the same period in the prior year. Pawnee could have utilized its credit facility to fund more of its portfolio growth and tax payments, however, as Chesswood had sufficient funds, Pawnee retained the funds that would otherwise be paid out in dividends to Chesswood. At September 30, 2013, approximately U.S.\$7.2 million (2012 – U.S.\$7.0 million) that is permitted to be sent up to Chesswood was still at Pawnee, being utilized to fund portfolio growth and lower interest costs.

#### *For the three-months ended September 30, 2013*

The Company’s operations generated cash flow from operations before the changes in operating assets and liabilities of \$8.1 million during the three-months ended September 30, 2013 compared to \$6.4 million in the three months ended September 30, 2012, an increase of \$1.7 million compared to the same period in the prior year.

The Company’s operations utilized cash flow of \$0.3 million during the three-months ended September 30, 2013 compared to \$0.7 million in the three months ended September 30, 2012, a decrease of \$396,000 compared to the same period in the prior year. In the three month period, to fund the increase in net investment in leases, equipment finance agreements and tax instalments of \$9.9 million, Pawnee utilized \$3.1 million of their line-of-credit. The amount of cash flow Chesswood directed to the growth in Case Funding’s legal finance portfolio in the three month period increased by \$811,000 year-over-year.

Capital expenditures totaled \$137,332 (2012 – \$111,000) during the three-months ended September 30, 2013.

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FOR THE THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2013

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The Company paid dividends to the holders of Common Shares and Exchangeable Securities in the amount of \$2.1 million during the three-months ended September 30, 2013 compared to \$1.9 million in the same period in the prior year; an increase of \$190,000 due to a higher number of shares outstanding and higher dividend per share amounts year-over-year.

In total, in the three-months ended September 30, 2013, there was a decrease in cash of \$2.4 million compared to \$2.7 million in the same period in the prior year. At September 30, 2013, approximately U.S.\$7.2 million (2012 – U.S.\$7.0 million) that is permitted to be sent up to Chesswood was still at Pawnee, being utilized to fund portfolio growth and lower interest costs.

Chesswood's directors will continue to review cash flow and cash position, to determine appropriate changes, if any, to the dividend policy going forward. Chesswood's cash flow may or may not attain the levels necessary to generate the current level of dividends.

Chesswood expects that current operations and planned capital expenditures for the foreseeable future of its subsidiaries will be financed using funds generated from operations, existing cash, and funds available under existing and/or new credit facilities. Chesswood may require additional funds to finance future acquisitions and support significant internal growth initiatives such as Case Funding's operations and originations and Pawnee's portfolio growth. It will seek such additional funds, if necessary, through public or private equity or debt financings from time to time, as market conditions permit.

### **Financial Covenants, Restrictions and Events of Default**

The Company's operating subsidiaries are subject to bank and/or manufacturer covenants relative to leverage and/or working capital, other than Case Funding and Lease-Win, which either have no banking facility or no longer has or needs a banking facility.

Pawnee funds its business primarily through variable rate borrowings and has a revolving credit facility for up to U.S.\$85.0 million which can, subject to certain conditions, be extended to U.S.\$115.0 million. As of September 30, 2013, Pawnee had used approximately U.S.\$70.2 million of its available borrowing under this facility (U.S.\$48.3 million as of December 31, 2012). Pawnee's ability to access funding at competitive rates through various economic cycles enables it to maintain the liquidity necessary to manage its business, and its ability to continue to access funding is an important condition to its future success. Pawnee is required to purchase fixed interest rate hedges for at least 50% of the outstanding balance under its credit facility, and as of September 30, 2013 Pawnee has hedged U.S.\$45.0 million, representing approximately 64.1% of the U.S.\$70.2 million outstanding under the credit facility.

Pawnee's syndicate of lenders is in the process of finalizing amendments to the current banking agreement that will provide Windset with access to a maximum of US\$5.0 million of capital from Pawnee's credit facility. No significant changes are expected to Pawnee's covenants under the credit facility, as a result of this new availability.

Pawnee's secured borrowing agreement has financial covenants and other restrictions with which it must comply in order to obtain continued funding and avoid default. Events of default under these arrangements include a change in control without lender-approval.

Advances on the revolving facility may be drawn at any time, subject to compliance with borrowing base calculations and compliance with the covenants set out therein. As of September 30, 2013, U.S.\$70.2 million was outstanding under the facility and Pawnee had capacity to draw up to and in excess of the U.S.\$85.0 million commitment and remain within the borrowing base under the facility.

Pawnee is restricted in its ability to merge, acquire companies or be acquired, or incur additional debt without lender approval. Furthermore, dividends are limited to compliance with all bank covenants and may not exceed 95% of Pawnee's consolidated net income, as determined in accordance with U.S. GAAP, with a few adjustments, including mark-to-market adjustments for interest rate swaps.

Pawnee is subject to the risk of increases in interest rates as the credit facility used to fund the business operations has a variable interest rate component, while the yields on its equipment leases and loans (EFA's) are fixed. Pawnee seeks to mitigate that risk through the use of swap agreements that effectively convert floating rate debt to fixed rates.

Pawnee's current funding agreement expires on July 24, 2016. Pawnee has successfully renewed its funding facility on numerous occasions.

FOR THE THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2013

## Dividends to Shareholders

The Company declared cash dividends during the nine months ended September 30, 2013 as follows:

<u>Shareholder Record Date</u>	<u>Per Share</u>
January 31, 2013	\$ 0.055
February 28, 2013	\$ 0.060
March 31, 2013	\$ 0.060
April 30, 2013	\$ 0.060
May 31, 2013	\$ 0.060
June 30, 2013	\$ 0.060
July 31, 2013	\$ 0.060
August 31, 2013	\$ 0.060
September 30, 2013	\$ 0.060
	<u>\$ 0.535</u>

## Dividend Policy

The Company's policy is to pay monthly dividends to shareholders of record on the last business day of each month by the 15<sup>th</sup> of the following month (or the next business day thereafter if the 15<sup>th</sup> is not a business day).

The amount of any dividends payable by Chesswood is at the discretion of its board of directors, is evaluated on an ongoing basis, and may be revised subject to business circumstances and expected capital requirements depending on, among other things, Chesswood's earnings, financial requirements for its operating entities, growth opportunities, the satisfaction of applicable solvency tests for the declaration and payment of dividends and other conditions existing from time to time.

## OUTLOOK

We continue to pursue growth initiatives in each of our businesses, while the U.S. economy generates performance metrics that can best be described as "mixed", maintaining overall economic uncertainty.

During the third quarter Pawnee's market began to experience an increase in competition, including pricing pressure, after a period of relative uniformity in assessing and pricing appropriately for credit risk.

The small ticket (third-party brokered) market of the equipment finance industry has experienced these competitive dynamics in the past. The years leading up to the dramatic correction in our market at the time of the financial crisis in 2007-2008 were characterized by aggressive pricing of risk and a general widening of credit appetites across the market. During this period, Pawnee remained diligent in adhering to its risk adjusted pricing, and approved and funded transactions that met its own underwriting guidelines, despite pressures to follow the competition. This approach allowed Pawnee to successfully steer its way through that turbulent time.

Our approach as this market undergoes change remains the same – adhere to our underwriting guidelines while continuously monitoring and analyzing portfolio performance in depth. Our analysis always includes looking for areas within the portfolio where performance would allow us to grow, while taking on acceptable risk.

If this latest mismatch of credit quality and pricing remains in effect, we would expect it to affect originations in certain segments of our portfolio.

## CRITICAL ACCOUNTING POLICIES AND ESTIMATES

Understanding the Company's accounting policies is essential to understanding the results of the Company's operations and financial condition. The Company's significant accounting policies are described in Note 3 to the Company's consolidated financial statements for the year ended December 31, 2012. The preparation of these financial statements requires us to make



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FOR THE THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2013

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estimates and judgments that affect reported amounts of assets and liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities at the date of our financial statements. We base our estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Critical accounting policies are defined as those that are reflective of significant judgments and uncertainties and the most significant of which are described below.

***Investment in Leases***

The leases entered into by the Company are considered to be finance leases in nature, based on an evaluation of all the terms and conditions and the determination that the Company has transferred substantially all the risks and rewards of legal ownership of the asset to the lessee. Interest revenue on finance leases is recognized under the effective interest method. The effective interest method of income recognition applies a constant rate of interest equal to the internal rate of return on the lease.

***Allowance for Doubtful Accounts***

The carrying value of investment in leases and EFAs is net of allowance for doubtful accounts. Quantifying the impairment is based on the estimates of the carrying value that will ultimately not be collected where there is objective evidence of impairment.

Pawnee's lease receivables and EFAs are each composed of a large number of homogenous leases and loans (EFAs are classified as loans for accounting purposes), with relatively small balances made to inherently risky borrowers. Pawnee charges-off leases and EFAs when they become 154 days contractually past due, unless information indicates that an earlier charge-off is warranted. A high percentage of charge-offs are made before the subject leases and loans reach 154 days contractually past due.

Pawnee's allowance for doubtful accounts on Chesswood's consolidated financial statements is comprised of the net investment in leases and EFAs value that is over 30 days delinquent, plus any leases or loans identified as impaired less than 30 days delinquent and approximately 10% of the 1-30 day delinquent leases (those considered most likely to fall into the over 30 days delinquent category by the next month).

Under IFRS, an allowance can only be set up if there is objective evidence that the impairment has already occurred; potential losses expected as a result of future events, no matter how likely based on past historical evidence, are not allowed to be recognized. As only a small percentage of the total lease and loan receivable portfolio have monthly payments that are past due at any one reporting date, the portion of the lease and loan receivables that shows observable objective evidence of impairment at any one reporting date is quite small, despite long-term historical experience that indicates that future charge-offs with respect to the current lease and loan receivable will typically exceed the level of observable impairment, in a matter of months.

Projections of Pawnee's probable net credit losses are inherently uncertain, and as a result we cannot predict with certainty the amount of such losses. Changes in economic conditions, the risk characteristics and composition of the portfolio, bankruptcy laws, and other factors could impact Pawnee's actual and projected net credit losses and the related allowance for doubtful accounts.

***Legal finance receivables***

Attorney loans and medical lien financing are deemed to be a financial asset as they are a contractual right to receive cash from another entity and are considered to be loans and receivables for accounting purposes, based on an evaluation of all the terms and conditions of the contracts. The contracts are deemed to have fixed or determinable payments, in that the payments are due when the underlying cases are settled however the date as to which that will happen is not known and is estimated. Loans and receivables are accounted for at amortized cost using the effective interest method; however the effective interest rate is calculated using estimated cash flows based on an estimated settlement dated.

Plaintiff advances are deemed to be a financial asset as they are a contractual right to receive cash from another entity and are considered to be available-for-sale financial assets for accounting purposes, based on an evaluation of all the terms and conditions of the contracts. The terms of the plaintiff advances are on a non-recourse basis, and payment depends on the

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success and potential claim size. Thus, the terms may limit the expected cash flows and other than for credit deterioration, they are deemed not to be loans and receivables. Available-for-sale financial assets are valued at fair value, the accretion in value is recognized based on the effective interest method and recognized into finance income, any changes in fair value are recorded in other comprehensive income until realized.

Under IFRS, an allowance for the collectability of the legal finance receivables can only be set up if there is objective evidence that the impairment has already occurred; potential losses expected as a result of future events, no matter how likely based on past historical evidence or known uncertainties with this type of receivable, are not allowed to be recognized. The collectability of loans and/or advances made by Case Funding depends on litigation outcomes in the form of judgments and/or settlements. Once an advance/loan is made, the timing of the collection cycle is out of Case Funding's control. Therefore, the timing of actual collections will be irregular. At September 30, 2013, Case Funding is not aware of any situation where the collection of a receivable is doubtful and thus there is no observable objective evidence of impairment and therefore no basis for establishing an allowance for doubtful accounts under IFRS; however historical experience and the uncertainties involved would indicate that Case Funding will not collect 100% of the loans and advances.

#### ***Impairment of Goodwill***

Goodwill is evaluated for impairment on an annual basis, or more frequently if certain events or circumstances exist. The Company's impairment test of goodwill is based on the value-in-use which is estimated using a discounted cash flow model. The cash flows are derived from budgets for the next five years, excluding restructuring activities and future investments. Impairment testing is applied on an individual asset basis unless an asset does not generate cash inflows that are largely independent of the cash inflows generated by other assets or groups of assets. None of the Company's non-financial assets generate independent cash inflows and therefore all non-financial assets are allocated to cash generating units ("CGU") for purposes of assessing impairment.

CGUs are defined as the smallest identifiable group of assets that generate cash inflows that are largely independent of the cash inflows from other assets or groups of assets. Impairment losses are recognized when the carrying amount of a CGU exceeds the recoverable amount, which is the greater of the CGU's fair value less cost to sell and its value in use. Value-in-use is the present value of the estimated future cash flows from the CGU discounted using a pre-tax rate that reflects current market rates and the risks inherent in the business of each CGU. If the recoverable amount of the CGU is less than its carrying amount, the CGU is considered impaired and is written down to its recoverable amount. The impairment loss is allocated to reduce the carrying amount of the assets of the CGU, first to reduce the carrying amount of the CGU's goodwill and then to the other assets of the CGU allocated pro-rata on the basis of the carrying amount of each asset. Other than the cash flow estimates, the value-in-use is most sensitive to the discount rate used and the growth rate applied beyond the five year estimate. Changes in these estimates and assumptions could have a significant impact on the value-in-use and/or goodwill impairment.

#### ***Contingent consideration and bonus***

Contingent consideration and bonus relates to the Incentive Payment Amount (as defined below) on the acquisition of Case Funding. The consideration is payable in the event that Case Funding's normalized net income ("NNI") for the 25th through 36th months following the Acquisition Date (June 10, 2011) achieves the targeted amount of approximately U.S.\$4.7 million (the "Targeted Amount"), whereby an amount of U.S.\$1.4 million (the "Incentive Payment Amount") (or an identical percentage adjusted portion of the Incentive Payment Amount if NNI is less than, but at least 90% of, the Targeted Amount) will be paid no later than the 38th month. It was determined at December 31, 2012 that the probability that the Targeted Amount would be reached was minimal.

The estimate of the fair value of contingent consideration and bonus payable requires very subjective assumptions to be made of various potential operating result scenarios and discount rates. Although the Company believes that there will be no Incentive Payment Amount due in June 2014, it will continue to periodically review NNI results and an updated assessment of various probability weighted projected NNI scenarios. If circumstances change and the Company determines that an earn-out payment may be due, such future revisions may materially change the estimate of the fair value of contingent consideration and therefore materially affect the Company's future financial results.

***Share-based Payments***

The Black-Scholes model is used to fair value options issued by the Company. The model requires the use of subjective assumptions including the expected share price volatility. In addition, the options issued have characteristics different from those of traded options so the Black-Scholes option-pricing model may not provide a reliable single measure of the fair value of options issued. Changes in the subjective assumptions can have a material effect on the fair value estimate.

***Interest Rate Swaps***

Hedge accounting requires recognition of the fair value of all derivative instruments on the statement of financial position as either assets or liabilities. Changes in a derivative's fair value are recognized currently in earnings unless specific hedge accounting criteria are met. Gains and losses on derivative hedging instruments must be recorded in either other comprehensive income or current earnings, depending on the nature and designation of the instrument.

Pawnee's interest rate swaps are not considered trading instruments as Pawnee intends to hold them until maturity. Nonetheless, the interest rate swaps do not qualify as a hedge for accounting purposes, and are therefore recorded as separate derivative financial instruments. Accordingly, the estimated fair value of the interest rate swaps is recorded as an asset or a liability on the accompanying consolidated statement of financial position. Payments made and received pursuant to the terms of the interest rate swaps are recorded as an adjustment to interest expense, and adjustments to the fair value of the interest rate swaps are recorded as gain or loss on interest rate swaps. The fair value of interest rate swaps is based upon the estimated net present value of cash flows.

***Taxes***

Pawnee and Lease-Win use the asset and liability method to account for taxes. Under the asset and liability method, deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax basis. Deferred tax assets and liabilities are measured using enacted 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 deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. The measurement of deferred tax assets is reduced, if necessary, by a valuation allowance for future tax benefits for which realization is not considered more likely than not. Pawnee and Lease-Win account for their lease arrangements as operating leases for federal tax reporting purposes. This results in temporary differences between financial and tax reporting for which deferred taxes have been provided.

Significant management judgment is required in determining the provision for taxes, deferred tax assets and liabilities and any necessary valuation allowance recorded against net deferred tax assets. The process involves summarizing temporary differences resulting from the different treatment of items, for example, leases for tax and accounting purposes. These differences result in deferred tax assets and liabilities, which are included within the consolidated statement of financial position. Management must then assess the likelihood that deferred tax assets will be recovered from future taxable income or tax carry-back availability and, to the extent management believes recovery is not probable, a valuation allowance must be established. To the extent that we establish a valuation allowance in a period, an expense must be recorded within the tax provision in the statement of income. The Company's estimate of its future taxes will vary based on actual results of the factors described above, and such variations may be material.

**FUTURE ACCOUNTING CHANGES*****Financial Instruments: Presentation***

IAS 32, *Financial Instruments: Presentation* has been amended to include additional presentation requirements for financial assets and liabilities that can be offset in the statement of financial position. The effective date for the amendments to IAS 32 is annual periods beginning on or after January 1, 2014. The revised standards relates only to presentation and will not impact the financial results of the Company.

***Financial Instruments (Classification and Measurement)***

IFRS 9, *Financial Instruments* will replace IAS 39, *Financial Instruments: Recognition and Measurement*. IFRS 9 uses a single approach to determine whether a financial asset is measured at amortized cost or fair value. The approach in IFRS 9 is based on how an entity manages its financial instruments in the context of its business model and the contractual cash flow characteristics of the financial assets. The new standard also requires a single impairment method to be used, replacing the multiple impairment methods in IAS 39. Most of the requirements in IAS 39 for classification and measurement of financial

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liabilities were carried forward unchanged to IFRS 9. Mandatory Effective Date of IFRS 9 and Transition Disclosures, issued in December 2011, deferred the effective date to annual periods beginning on or after January 1, 2015, with earlier adoption permitted.

## **RISK FACTORS**

An investment in Common Shares entails certain risk factors that should be considered carefully.

Chesswood operates in a dynamic environment that involves various risks and uncertainties, many of which are beyond our control and which could have an effect on our business, revenues, operating results, cash flow and financial condition. Readers should carefully review the risk factors in the Company's annual information form filed with various Canadian securities regulatory authorities through SEDAR (the System for Electronic Document Analysis and Retrieval) at [www.sedar.com](http://www.sedar.com), a summary of which are set out below.

### ***Dependence on Key Personnel***

Our operating companies depend to a large extent upon the abilities and continued efforts of their key operating personnel and senior management teams.

### ***Relationships with Brokers and Other Origination Sources***

Pawnee has formed relationships with hundreds of origination sources, comprised primarily of equipment finance brokerage firms. Pawnee relies on these relationships to generate applications and originations. The failure to maintain effective relationships with its brokers and other origination sources or decisions by them to refer transactions to, or to sign contracts with, other financing sources could impede Pawnee's ability to generate transactions.

Similarly, the business models of Case Funding and Windset depend to a large extent on referral relationships.

### ***Risk of Future Legal Proceedings***

Our operating companies are threatened from time to time with, or are named as defendants in, or may become subject to, various legal proceedings, fines or penalties in the ordinary course of conducting their respective businesses. A significant judgment or the imposition of a significant fine or penalty on an operating company (or on a company engaged in a similar business, to the extent the operating company operates in a similar manner) could have a material adverse impact on our business, financial condition and results of operations, and on the amount of cash available for dividends to our shareholders.

### ***Interest Rate Fluctuations***

Our operating companies (and, in particular, Pawnee and Windset) are exposed to fluctuations in interest rates under their borrowings. Increases in interest rates (to the extent not mitigated by interest hedging arrangements) may have a material adverse impact on our businesses, financial condition and results of operations, and on the amount of cash available for dividends to our shareholders.

Pawnee and Windset's leases and loans are written at fixed interest rates and terms. Pawnee and Windset, generally, finances their activities using both fixed rate and floating rate funds. To the extent Pawnee and Windset finances fixed rate leases and loans with floating rate funds, they are exposed to fluctuations in interest rates such that an increase in interest rates could narrow or eliminate the margin between the yield on a lease and loan and the effective interest rate paid by the borrower. While Pawnee and Windset enters into interest rate swaps to mitigate rate fluctuation risk, there can be no assurances that these arrangements will be sufficient to fully protect Pawnee and Windset against interest rate risks, or that Pawnee and Windset will be able to maintain such arrangements on a continuing basis.

### ***Portfolio Delinquencies; Inability to Underwrite Lease and Loan Applications***

Pawnee's receivables consist primarily of lease and loan receivables originated under programs designed to serve smaller, often owner-operated businesses that have limited access to traditional financing. There is a high degree of risk associated with equipment financing for such parties. The typical borrower in Pawnee's portfolio is a start-up business that has not established business credit or a more established business that has experienced some business or personal credit difficulty at some time in its history. As a result, such leases entail a relatively higher risk and may be expected to experience higher

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levels of delinquencies and loss levels. Pawnee cannot guarantee that the delinquency and loss levels of its receivables will correspond to the historical levels Pawnee has experienced on its portfolio and there is a risk that delinquencies and losses could increase significantly.

In addition, since defaulted leases and loans and certain delinquent leases and loans cannot be used as collateral under its variable rate financing facilities, higher than anticipated lease defaults and delinquencies could adversely affect Pawnee's liquidity by reducing the amount of funding available to it under these financing arrangements. Furthermore, increased rates of delinquencies or loss levels could result in adverse changes to the terms of future financing arrangements, including increased interest rates payable to lenders and the imposition of more burdensome covenants and increased credit enhancement requirements.

Analogous risks are faced by Case Funding and Windset in their business.

***Deterioration in Economic or Business Conditions; Impact of Significant Events and Circumstances***

Our operating companies' results may be negatively impacted by various economic factors and business conditions, including the level of economic activity in the markets in which they operate. To the extent that economic activity or business conditions deteriorate, delinquencies and credit losses may increase. Delinquencies and credit losses generally increase during economic slowdowns or recessions such as that recently experienced in the United States. As Pawnee and Windset extend credit primarily to small businesses, many of their customers may be particularly susceptible to economic slowdowns or recessions, and may be unable to make scheduled lease payments during these periods. Unfavourable economic conditions may also make it more difficult for Pawnee and Windset to maintain new origination volumes and the credit quality of new leases and loans at levels previously attained. Unfavourable economic conditions could also increase funding costs or operating cost structures, limit access to credit facilities, securitizations and other capital markets or result in a decision by lenders not to extend further credit. Sherway LP, as the operator of a premium brand, new car dealership, could also be negatively affected by deteriorating economic conditions which result in reduced new car sales.

In addition, the leasing and working capital loan industries generally may be affected by changes in accounting treatment for leases and loans, and negative publicity with respect to, among other things, fraud or deceptive practices by certain participants in the industry. Greater governmental scrutiny is also a risk, especially as to the tax treatment of certain transaction structures or other aspects of these transactions that, if changed, could result in additional tax, fee or other revenue to that governmental authority. Any of these factors may make leasing less attractive or diminish the profitability of the existing financing alternatives offered by our operating companies.

In addition to being impacted by factors or conditions in the United States, political economic or other significant events or circumstances outside of North America (whether political unrest which impacts upon the prices of oil and other commodities or otherwise) can ultimately significantly impact upon North American economic conditions which, in turn, could result in the adverse implications described in the first paragraph under this heading. Similarly, natural disasters in any relevant place in the world may directly (through impact on supplies of goods or equipment to our businesses) or indirectly impact upon our operations or results.

***Losses from Leases and Loans***

Losses from leases and loans in excess of Pawnee's expectations would have a material adverse impact on our businesses, financial condition and results of operations, and on the amount of cash available for dividends to our shareholders.

Changes in economic conditions, the risk characteristics and composition of the portfolio, bankruptcy laws, and other factors could impact Pawnee's actual and projected net credit losses and the related allowance for credit losses. Should there be a significant change in the above noted factors, then Pawnee may have to set aside additional reserves which could have a material adverse impact on their respective business, financial condition and results of operations and on the amount of cash available for dividends to our shareholders.

Determining the appropriate level of the allowance is an inherently uncertain process and therefore the determination of this allowance may prove to be inadequate to cover losses in connection with a portfolio of leases and loans. Factors that could lead to the inadequacy of an allowance for credit losses may include the inability to appropriately underwrite credit risk of new originations, effectively manage collections, or anticipate adverse changes in the economy or discrete events adversely affecting specific customers, industries or geographic areas.

Analogous risks are faced by Case Funding and Windset in their business.

***Adverse Events or Legal Determinations in Areas With High Geographic Concentrations of Leases or Loans***

If judicial or other governmental rulings or actions or interpretations of laws adverse to the equipment finance business in general or to business practices engaged in by Pawnee, or adverse economic conditions or the occurrence of other significant events such as natural disasters and terrorist attacks, were to occur in a geographic region with a high concentration of leases/loans or equipment financed from Pawnee, there could be a material adverse impact on our business, financial condition and results of operation, and the amount of cash available for dividends to our shareholders.

Analogous risks are faced by Case Funding and Windset in their business.

***External Financing***

Our operating subsidiaries depend and will continue to depend on the availability of credit from external financing sources to continue to finance new leases/loans, refinance existing leases/loans and satisfy their other working capital needs. The operating subsidiaries may be unable to obtain additional financing on acceptable terms or at all. If any or all of their funding sources become unavailable on acceptable terms or at all, or if any of their credit facilities are not renewed or re-negotiated upon expiration of their terms, the operating subsidiaries may not have access to the financing necessary to conduct their respective businesses, which would limit their ability to finance their operations.

Although Chesswood is providing Case Funding with funds for its initial financing, and the initial financing for Windset is being accessed through Pawnee's credit facilities, the long-term success of Case Funding and Windset will require that each obtains external financing on acceptable terms.

***“Characterization” Risks***

If an applicable court or regulatory authority were to make an adverse finding, or take an adverse action on the basis that one of Pawnee's form of lease is not a true lease for commercial law, tax law, or other legal purposes, adverse consequences could result with respect to leases entered into in such form including the loss of preferred creditor status (which would impact upon Pawnee's rights to recover on its claim), limitations on finance charges and other fees that can be enforced, and additional federal, state and other (income or sales) taxes payable by Pawnee.

Case Funding's non-recourse advances may be re-characterized as loans or determined to be improper fee-splitting, which would adversely affect the collectability of the advances, and the ability to generate future advance originations.

***Defenses to Enforcement of a Significant Number of Leases and Loans***

Certain defenses and recovery impediments are more common in micro and small-ticket equipment finance transactions than with respect to equipment finance providers in other segments of the equipment finance industry. Management believes that certain of these risks are sufficiently addressed in Pawnee's existing documentation and related business practices. However, there are other risks that Pawnee has not addressed for various reasons, including that certain of these risks are not susceptible to being addressed either at all, or without incurring cost inefficiencies or taking other measures deemed unacceptable by Pawnee's management based on a risk-reward assessment. Pawnee has never experienced any material occurrence of these risks nor have these risks historically had a material adverse impact on Pawnee. However, there is no assurance that these risks will not have a material adverse impact on Pawnee's business, financial condition and results of operations in the future.

***Origination, Funding and Administration of Transactions***

Pawnee's origination, funding and transaction administration practices could result in certain vulnerabilities in its enforcement rights. For example, certain of Pawnee's leases are assignments of transactions already documented by its lease brokers. Acquiring leases by this “indirect” process subjects Pawnee to various risks, including risks that might arise by reason of the broker's insolvency, administrative inadequacies or fraudulent practices, as well as any third party claims against the broker or its rights with respect to the assigned lease or loan. Any of these broker related risks can impair Pawnee's rights with respect to recovering the rents and/or property under its leases and loans. Pawnee has not been involved in any claims or litigation in relation to such risks and Pawnee does not conduct lien searches in the name of, require lien releases from, or file financing statements against the lease broker.

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If the lessee/borrower or broker is the party to whom the vendor of the equipment has agreed to sell the property at the time of its delivery, then, under applicable commercial law, the lessee/borrower or broker, as applicable, may be deemed to have acquired title to the property prior to Pawnee's having funded the transaction. It has not been Pawnee's practice to ensure that the title to the leased property has not already passed or to obtain assurances that it is acquiring good title to that property free of liens and other third party claims. The manner in which Pawnee purchases the equipment is typical in this market segment, especially with respect to similarly situated equipment financing providers. Pawnee has not yet faced any meaningful challenge or adverse consequence from this practice, but there can be no assurance that such a challenge or consequence will not occur in the future.

In most circumstances where the equipment is less than U.S.\$15,000 (or U.S.\$10,000 if for a home business) for Pawnee's core product and U.S.\$35,000 for the "B+" product, Pawnee's practice of requiring only a verbal confirmation that the property has been delivered and irrevocably accepted under the subject lease or loan, and/or inspecting the property to confirm the same, could make Pawnee vulnerable to certain defenses. By way of example, Pawnee's deemed failure to deliver conforming property under the lease or loan documents could be a defense to a lessee/borrower's "unconditional" obligation to pay the rents and certain other amounts. Pawnee has not suffered any material losses relating to these practices, however, there can be no assurance that it would not in the future.

***Changes in Governmental Regulations, Licensing and Other Laws and Industry Codes of Practice***

Equipment finance companies are subject to laws and regulations relating to extending financing generally and are also members of industry associations which have adopted, among other things, codes of business practice. Laws, regulations and codes of business practice may be adopted with respect to existing leases and loans or the leasing, marketing, selling, pricing, financing and collections processes which might increase the costs of compliance of Pawnee, or require it to alter its respective business, strategy or operations, in a fashion that could hamper Pawnee's ability to conduct business in the future.

A change in laws applicable to tort claims may reduce the availability of appropriate cases for Case Funding to underwrite.

***State Licensing Requirements***

If an applicable court or regulatory authority were to make an adverse finding or otherwise take adverse action with respect to Pawnee, Windset or Case Funding based on their failure to have a finance lender's or other license or registration required in the applicable state, Pawnee, Windset or Case Funding would have to change business practices and could be subject to financial or other penalties.

***Fees, Rates and Charges***

Pawnee and Windset's documents often require payment of late payment fees, late charge interest, and other charges either relating to the non-payment, or enforcement of its leases and loans. Case Funding's attorney loans also include similar provisions. It could be determined that these fees and/or the interest rates charged exceed applicable statutory or other legal limits. If the charges are deemed to be punitive and not compensatory, or to have other attributes that are inconsistent with, or in violation of, applicable laws, they could be difficult to enforce. A number of charges payable with respect to equipment finance transactions in the micro and small-ticket equipment finance market have been the subject of litigation by customers against financing parties over the past few years. Although our subsidiaries are not currently the subject of any such litigation, there can be no assurance that a lessee/borrower or a group of lessees/borrowers will not attempt to bring a lawsuit against our subsidiaries in relation to fees and charges, which our subsidiaries may or may not be successful in defending.

Pawnee, Windset and Case Funding believe that fee programs are designed and administered so as to comply with legal requirements and are within the range of industry practices in their market segments. Nevertheless, certain attributes of these fees or charges, and their practices, including that its leases and loans typically provide for several different fees and charges resulting in a substantial amount of fee income and the possibility that the fees and charges may exceed actual costs involved or may otherwise be deemed excessive, could attract litigation, including class actions, that would be costly even if our subsidiaries were to prevail and as to which no assurance can be given of their successful defense. In addition to the risk of litigation, fee income is important to our subsidiaries and the failure of our subsidiaries to continue to collect most or all of these fees could have a material adverse impact on our business, financial condition and results of operations, and on the amount of cash available for dividends to our shareholders.

***Possible Acquisitions***

The growth strategy for the Company includes seeking out acquisitions in the financial services industries. Acquisitions, if they occur, may increase the size of the operations as well as increase the amount of indebtedness that may have to be serviced by Chesswood and its subsidiaries. There is no assurance that such acquisitions can be made on satisfactory terms, or at all. The successful integration and management of acquired businesses involve numerous risks that could adversely affect the growth and profitability of Chesswood and its subsidiaries. There is no assurance that such acquisitions (including Case Funding) will be successfully integrated.

***Insurance***

To ensure that the lessor or funder of the leased or financed property suffering a loss receives the related insurance proceeds, the lease or loan also requires that the lessor or funder be named as a loss payee under the requisite casualty coverage. However, each lessee/borrower is ultimately relied upon to obtain and maintain the required coverage for financed equipment but there is no certainty that they will obtain the requisite coverage either conforming to the requirements of the lease or loan, or at all. Additionally, there are often policy provisions including exclusions, deductibles and other conditions that by their terms, or by reason of a breach, could limit, delay or deny coverage. There can be no assurance that any insurance will protect our operating company's interest in the equipment, and the failure by the lessee/borrower to obtain insurance or the failure by the operating companies to receive the proceeds from such insurance policies could have a material adverse impact on our business, financial condition and results of operations, and on the amount of cash available for dividends to our shareholders.

***Lessor Liability***

There is a risk that a lessor, such as Pawnee, could be deemed liable for harm to persons or property in connection with, among other things, the ownership or leasing of the leased property, or the conduct or responsibilities of the parties to the lease relating to that property. The liability may be contractual (such as warranties regarding the equipment), statutory such as federal, state or provincial environmental liability or pursuant to various legal theories (such as negligence). There have been cases in which a lessor has been held responsible for damage caused by leased property without a showing of negligence or wrong-doing on the lessor's part. Even if a lessor ultimately succeeds in defending itself or settling any related litigation, the related costs and any settlement amount could be significant.

***Liability for Misuse of Leased Equipment***

There is no practical manner to ensure that leased equipment or a leased vehicle will be used, maintained or caused to comply with applicable law. Pawnee requires its lessees to deliver evidence of compliance with same as a condition to funding but has no assurance that a lessee will take the appropriate actions during the lease term to address any use, maintenance or compliance issues which may arise. A lessee's conduct (or lack thereof) could subject Pawnee, as applicable, to liability to third parties.

***Estimates Relating to Value of Leases***

Based on the particular terms of a lease, equipment finance companies estimate the residual value of the financed equipment, which is recorded as an asset on its statement of financial position. At the end of the lease term, equipment finance companies seek to realize the recorded residual for the equipment by selling the equipment to the lessee or in the secondary market or through renewal of the lease by the lessee. The ultimate realization of the recorded residual values depends on numerous factors, including: accurate initial estimate of the residual value; the general market conditions and interest rate environment at the time of expiration of the lease; the cost of comparable new equipment; the obsolescence of the leased equipment; any unusual or excessive wear and tear on or damage to the equipment; and the effect of any additional or amended government regulations.

If Pawnee (in connection with those leases where the lessee is not obligated to either purchase the equipment or guarantee the residual value of the equipment at the end of the term of the lease) is unable to accurately estimate or realize the residual values of the leased equipment subject to their leases, the amount of recorded assets on its statement of financial position will have been overstated.



***Competition From Alternative Sources of Financing***

The business of micro and small-ticket equipment finance in the United States is highly fragmented and competitive. Pawnee focuses its business on the segment of the micro and small-ticket equipment finance market involving start-up businesses that have not established business credit or established businesses that have experienced some credit difficulty in their history that do not meet the credit standards of more traditional financing sources. Pawnee's main competition comes from leasing companies, home equity loans, and credit cards.

If Pawnee expands its suite of products to target potential lessees with higher credit scores or if the creditworthiness of its potential customers increases for various external reasons, it can expect to face competition from more traditional financing sources as well, including: national, regional and local finance companies; captive finance and equipment finance companies affiliated with major equipment manufacturers; and financial services companies, such as commercial banks, thrifts and credit unions.

Many of the firms and institutions providing financing alternatives are substantially larger than Pawnee and have considerably greater financial, technical and marketing resources. Some of them may have a lower cost of funds and access to funding sources that are unavailable to Pawnee. A lower cost of funds could enable a competitor to offer leases with pricing lower than that of Pawnee, potentially forcing Pawnee to decrease its prices or lose origination volume. In addition, some financing sources may have higher risk tolerances or different risk assessments, which could allow them to establish more origination sources and customer relationships to increase their market share. Please also see "Outlook" above.

Further, because there are fewer barriers to entry with respect to the micro and small-ticket equipment finance market, new competitors could enter this market at any time, especially if an improvement in the economy leads to a greater ability of small businesses to establish improved levels of creditworthiness.

Similarly, competition from a variety of other funding sources may result in a decrease in demand for Case Funding's or Windset's financing products.

***Fraud by Lessees, Borrowers, Vendors or Brokers***

While Pawnee makes every effort to verify the accuracy of information provided to it when making a decision whether to underwrite a lease or loan and has implemented systems and controls to protect itself against fraud, in a small number of cases in the past Pawnee has been a victim of fraud by lessees/borrowers, vendors and brokers. In cases of fraud, it is difficult and often unlikely that Pawnee will be able to collect amounts owing under a lease or loan or repossess the related equipment. Increased rates of fraud could have a material adverse impact on our business, financial condition and results of operations, and on the amount of cash available for dividends to our shareholders. Windset and Case Funding face analogous risks.

Case Funding may face similar risks with respect to information provided to it by attorneys and plaintiffs.

***Protection of Intellectual Property***

Chesswood's operating subsidiaries continually develop and improve their brand recognition, which are an important factor in maintaining a competitive position. No assurance can be given that others will not independently develop substantially similar branding. Despite the efforts of our operating subsidiaries to protect their proprietary rights, unauthorized parties may attempt to obtain and use information that they regard as proprietary. Stopping unauthorized use of such proprietary rights may be difficult, time-consuming and costly. There can be no assurance that our operating subsidiaries will be successful in protecting their proprietary rights.

***Uncertainty of outcome of cases***

The returns on loans and/or advances made by Case Funding, and thus the returns for Chesswood, depend on litigation outcomes in the form of judgments or settlements. Litigation of individual cases entails a large degree of uncertainty, including (1) the legal liability of the defendant, (2) the level of actual or perceived damages assessed by a judge or a jury, (3) the ability of the defendant, or the defendant's insurance company, to pay a settlement or judgment, (4) the abilities of plaintiff's counsel, (5) the assessment of fault and causation, (6) the legal nature of the claim, and (7) the amount of monetary damages ultimately awarded. It is also possible that a claimant may die or abandon his or her case, that the lawyer may

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abandon the plaintiff's case, or that the defendant, the law firm, or the defendant's insurance carrier may declare bankruptcy. Case Funding is also reliant on the capabilities of the attorneys handling the cases in which it provides funding to effectively litigate claims with due skill and care. If an attorney fails to perform his or her duties effectively, the outcome of the case could be negatively impacted, which could have a material adverse effect on Case Funding's level of returns. Any negative event, including but not limited to those described above, may prevent Case Funding from realizing expected returns. While Case Funding undertakes to review the capabilities, experience and track records of the attorneys litigating cases it is considering for its loans, there is no guarantee that the actual outcome of a case will be in line with the expected outcome of that case, and Case Funding will not have any right to control, influence or manage the litigation or settlement of a case. Although Case Funding will seek to weigh such uncertainties in the due diligence conducted before making a funding decision, and intends to reduce risk by funding in a broad array of cases, there can be no assurance that the outcome of any given litigated claim or basket of claims can be predicted, whether or not the probabilities were correctly assessed by Case Funding.

***Uncertainty in the timing of litigation settlements and awards***

The nature of litigation recoveries, including the timing and amounts recovered, are outside the control of Case Funding. Individual claims may be resolved over drastically varying times: for example, as short as one month, or longer than three years. Case Funding will be required to wait for an indeterminate period of time after an advance/loan is made to fully collect money from judgment recoveries. Once an advance/loan is made, the collection cycle is out of Case Funding's control. Therefore, there is no assurance as to collection times, and collections will likely be irregular. Also, there is no guarantee that Case Funding will be able to achieve results that will permit it to generate any particular rates of return in any given period. Case Funding may experience significant fluctuations in its operating results and cash flows from period to period due to a number of factors, including the changes in value of the advances/loans that it makes, and the collection and recognition of recoveries of its loans and returns. This may affect the amount of funds available each quarter for dividend payments.

***Case Funding may have difficulty collecting on its investments***

If plaintiffs or law firms to which Case Funding has loaned funds, do not pay Case Funding pursuant to the terms of the loans/advances made, Case Funding may be required to pursue costly legal actions to collect. It is also possible that a plaintiff's attorney or a law firm may attempt to renegotiate the ultimate amount owed to Case Funding. In these cases, Case Funding may accept a smaller return than anticipated in order to accommodate and maintain business relationships or avoid litigation. In either event, the failure of Case Funding to collect or the necessity of legal action to collect could ultimately harm or reduce the potential cash flow.

***Limited underwriting experience of, or underwriting errors, by Case Funding***

Case Funding has a limited history of precedents upon which to base its case evaluation. While the Company believes that Case Funding's management and underwriters have the experience to evaluate plaintiffs, cases, and attorney loans, Case Funding itself is a newer entity and thus has limited history in underwriting upon which shareholders may rely. There is no guarantee that Case Funding will be able to successfully assess the merits of all cases in which it provides funding, which, in turn, could adversely affect the financial results and cash flows of the business and/or Chesswood.

Case Funding may fail to correctly apply its own underwriting standards to a loan and/or advance, or may fail to account for or identify a material risk factor which could impact the success or value of a loan and/or advance hereby impacting the value of the Company's interests in such a loan and/or an advance.

***Case Funding may be unable to obtain key information about cases***

Case Funding's need for information about a case during its due diligence review may potentially result in an adverse outcome on the examined case. In general, communications between a client and the client's attorney are privileged. However, Case Funding requires certain information to assess the case. Case Funding keeps such information and communications confidential, but a court may determine that the disclosure of such communications to Case Funding amounts to a waiver by the client of the privilege attached to such information or documents. If this were to occur, the defendant may have the right to discover such communications and use them against the plaintiff in the course of the lawsuit. Alternatively, the prospect of a waiver of privilege may cause the plaintiff or the plaintiff's attorney to withhold key

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information about the case from Case Funding in order to preserve the privilege. Therefore, the inability of Case Funding to obtain the information it needs to assess the case, or the possibility that privileged information could be discoverable by the defendants and used against the plaintiff, may increase the likelihood of negative outcomes on a loan and/or advance in that case.

***Ethics and legal restrictions vary by state***

There have traditionally been legal and professional ethics restrictions on legal financing in the United States. These include the general prohibition from purchasing claims from plaintiffs (known as maintenance, as well as a form of maintenance called champerty), restrictions on assignment of certain kinds of claims, and ethical restrictions on participating in a lawyer's contingent fee interests (including ethical rules against sharing fees with non-lawyers). Maintenance prohibits the maintaining, supporting, promoting or assisting of another person's lawsuit, with money or otherwise. Champerty makes it illegal for a stranger to acquire a party's right to sue. Different states impose rules regarding champerty. If Case Funding were to be found in violation of a state's maintenance or champerty laws it could have a material adverse effect on the results of its loans and/or advances. Courts in any or all of the jurisdictions in which the loans and/or advances are made may conclude that Case Funding's loans and/or advances constitute "champerty" or "maintenance." Such a conclusion could make agreements with plaintiffs voidable, subject to fines or other sanctions, or otherwise negatively impact results. Due to these and similar rules, a number of states will not permit loans and/or advances like those Case Funding would typically make, and therefore Case Funding is limited in which states it may make loans and/or advances, which reduces the available funding opportunities. In other states, the funding of legal claims has not been considered by the courts or ethics authorities, nor specifically addressed by statute. In these situations, Case Funding may rely only on its own analysis as to the legality of loans and/or advances in these jurisdictions. Regardless of its analysis as to such legality, in jurisdictions where no legal or ethical guidance is available, Case Funding's loans and/or advances may be open to challenge, a reduction in value, or even cancellation, which would adversely impact financial results and the cash flow.

United States federal or state governmental bodies may enact laws limiting the rights of injured victims to sue or be compensated under some or all circumstances. Any such action could substantially limit or prevent entirely future funding opportunities for Case Funding. Changes in law or ethical rules in jurisdictions where restrictions on the types of loans and/or advances made by Case Funding currently do not apply could further reduce or limit opportunities for Case Funding to make loans and/or advances, or could result in the diminution or elimination of the value of the loans and/or advances already made by Case Funding in those jurisdictions.

***Evaluation and disclosure of cases and case performance***

Details of actual cases that Case Funding has funded in or intends to fund in will not be disclosed on a named basis to Shareholders, and in any event not all information relevant to the evaluation of any case will be permitted by law or professional ethics codes of conduct to be made available to Case Funding or the Shareholders. In particular, any sharing with Case Funding or the Shareholders of confidential information protected by attorney-client privilege or by attorney work-product doctrine could waive all protection of that information. Such waiver could severely damage the value of the underlying claim by giving the opponent access to sensitive information. Any agreement to share with Shareholders any information and evidence related to the case could preclude the plaintiff from entering into confidentiality agreements with co-plaintiffs in the same matter. Such sharing could also make discovery from the adverse party problematical as most discovery is covered by court-issued protective orders that ensure the confidentiality of all parties. A breach of a protective order could subject a party to serious sanctions that would impact the value of the underlying claim. In some instances, case settlements and case prospects will be confidential and/or subject to lawyer-client privilege. Accordingly, Shareholders will not have an opportunity to evaluate for themselves cases in which Case Funding intends to or does fund, and therefore Shareholders will be dependent upon the judgment and ability of Case Funding. The valuation of each potential loan or advance will be subject to policies adopted by Case Funding and may not reflect the actual financial prospects of such loan or advance at any given time.

***Concentration risk***

Certain loans may represent a significant proportion of Case Funding's total assets. As a result, the impact on Case Funding's performance and the potential returns will be more adversely affected if any one of those loans were to perform badly, than would be the case if Case Funding's portfolio of loans were more diversified.

***Failure of Computer and Data Processing Systems***

Our operating companies are dependent upon the successful and uninterrupted functioning of their computer and data processing systems. The failure of these systems could interrupt operations or materially impact upon the ability of our operating subsidiaries to originate and service their lease and loan portfolio and (in the case of Pawnee and Windset) broker networks. If sustained or repeated, a system failure could negatively affect these operations. Pawnee and Windset maintains confidential information regarding lessees and borrowers in their computer systems. This infrastructure may be subject to physical break-ins, computer viruses, programming errors, attacks by third parties or similar disruptive problems. A security breach of computer systems could disrupt operations, damage reputation and result in liability.

***Competition in the Automobile Retailing Industry***

The automobile retailing industry is competitive. In large metropolitan areas, consumers have a number of choices in deciding where to purchase a new or used vehicle and where to have such vehicle serviced.

***Manufacturers' Control Over Dealerships and the Acura Framework Agreement***

Automobile dealerships operate pursuant to dealer agreements with automobile manufacturers. Through the terms and conditions of these dealer agreements, automobile manufacturers exert considerable influence over the operations of dealerships.

The success of an automobile dealership is highly dependent upon the overall success of the line of vehicles that each dealership sells. Sherway LP's business is affected to varying degrees by the demand for its manufacturer's vehicles, and by the financial condition, management, marketing, production and distribution capabilities of such manufacturers. In addition, the timing, structure and amount of manufacturer incentives may impact the timing and profitability of sales transactions. Events such as labour disputes and other production disruptions that may adversely affect a manufacturer may also adversely affect Sherway LP. Similarly, the delivery of vehicles from manufacturers later than scheduled or diminished availability to Sherway LP of popular makes, models and/or accessories, which may occur particularly during periods of new product introductions, can lead to reduced sales during such periods. Moreover, any event that causes adverse publicity involving such manufacturers may have an adverse effect on Sherway LP.

***Security Risks***

Despite implementation of network security measures similar to most other on-line e-commerce sites, the infrastructure of the cars4U.com website and the Company's management network is potentially vulnerable to computer break-ins and similar disruptive problems.

***Cyclicality and Seasonality***

Sales of motor vehicles, particularly new vehicles, historically have been subject to cyclical and seasonal variations. Management believes that the industry is affected by many factors, including general economic conditions, consumer confidence, and the level of personal discretionary spending, interest rates and credit availability. There can be no assurance that the industry will not experience sustained periods of decline in vehicle sales, particularly new vehicle sales, in the future.

***Imported Products***

A significant portion of the new vehicle business of the Sherway LP dealership involves the sale of vehicles, parts or vehicles composed of parts that are manufactured outside North America. As a result, the operations of the Sherway LP dealership are subject to customary risks of selling imported merchandise, including fluctuations in the value of currencies, changes in import duties, exchange controls, trade restrictions, work stoppages and general political and economic conditions in foreign countries.

***Environmental Matters***

Sherway LP is subject to a wide range of federal, provincial and local environmental laws and regulations, including those governing discharges to the air and water, the storage of petroleum substances and chemicals, the handling and disposal of wastes and the remediation of contamination arising from spills and releases. As with automobile dealerships generally, and parts, service and collision service centre operations in particular, Sherway LP's business involves the generation, use, handling and disposal of hazardous or toxic substances or wastes.

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FOR THE THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2013

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Environmental laws and regulations have become very complex and it has become very difficult for businesses that routinely handle hazardous and non-hazardous wastes to achieve and maintain full compliance with all applicable environmental laws. From time to time, Sherway LP can be expected to experience incidents and encounter conditions that will not be in compliance with environmental laws and regulations.

However, Sherway LP has not been subject to any material environmental liabilities in the past and it is not anticipated that any material environmental liabilities will be incurred by it in the future. In addition, to minimize the risk of environmental liability related to acquired dealerships, Sherway LP intends to obtain environmental studies on such dealerships as a condition to their acquisition.

Environmental laws and regulations and their interpretation and enforcement are changed frequently and the trend of more expansive and stricter environmental legislation and regulations is likely to continue. Hence, there can be no assurance that compliance with environmental laws or regulations or the future discovery of unknown environmental conditions will not require additional expenditures or that such expenditures would not be material.

***Risks Related to our Structure and Exchange Rate Fluctuations***

The dividends expected to be paid to our shareholders will be denominated in Canadian dollars, however, a significant percentage of our revenues are expected to be derived from the U.S. dollar revenues of our U.S. operating subsidiaries, which are in U.S. dollars. Changes in the value of the U.S. dollar could have a negative impact on the amount in Canadian dollars available for dividends to our shareholders.

***Unpredictability and Volatility of Share Price***

A publicly-traded company will not necessarily trade at values determined by reference to the underlying value of its business. The prices at which the Common Shares will trade cannot be predicted. The market price of the Common Shares could be subject to significant fluctuations in response to variations in quarterly operating results and other factors. The annual yield on the Common Shares as compared to the annual yield on other financial instruments may also influence the price of Common Shares in the public trading markets. In addition, the securities markets have experienced significant price and volume fluctuations from time to time in recent years that often have been unrelated or disproportionate to the operating performance of particular issuers. These broad fluctuations may adversely affect the market price of the Common Shares.

***Leverage, Restrictive Covenants***

Pawnee and Sherway LP have third party debt service obligations under their respective credit facilities. The degree to which our subsidiaries are leveraged could have important consequences to our shareholders, including: (i) the ability of such subsidiaries to obtain additional financing for working capital in the future may be limited; (ii) a portion of the cash flow from the assets of such subsidiaries may be dedicated to the payment of the principal of and interest on their respective indebtedness, thereby reducing funds available for distribution to the Company; and (iii) certain of the respective borrowings of such subsidiaries will be at variable rates of interest, which will expose them to the risk of increased interest rates. The ability of such subsidiaries to make scheduled payments of the principal of or interest on, or to refinance, their indebtedness will depend on their future cash flow, which is subject to their respective assets, prevailing economic conditions, prevailing interest rate levels, and financial, competitive, business and other factors, many of which are beyond their control.

***Restrictions on Potential Growth***

The payout by our operating companies of a significant portion of their earnings available for distribution will make additional capital and operating expenditures dependent upon increased cash flow or additional financing in the future. Lack of those funds could limit the future growth of our operating companies and their cash flow.

***Canadian Income Tax Matters***

The income of the Company and its related entities must be computed in accordance with Canadian and foreign tax laws, as applicable, and the Company is subject to Canadian tax laws, all of which may be changed in a manner that could adversely affect the amount of distributable cash.

**United States Income Tax Matters**

There can be no assurance that U.S. federal income tax laws and administrative policies will not develop or be changed in a manner that adversely affects our shareholders.

**RELATED PARTY TRANSACTIONS**

1) Pawnee leases a 10,800 square foot office facility. The lessor is a related party because of common ownership between itself and the holders of the Class B and C common shares of U.S. Acquisitionco (the subsidiary through which the Company holds its interest in Pawnee). Minimum lease payments are U.S. \$212,890 per annum, triple net. The lease expires on April 30, 2016, and contains an option to renew for an additional five year term. The expense is included in general and administrative expense and is translated at the average exchange rate for the period. At September 30, 2013 and December 31, 2012 there was no amount payable in respect of the lease.

2) Case Funding provides Quick Cash Inc. ("Quick Cash"), an entity controlled by a director of Case Funding and the CEO of Case Funding, with personnel and facilities to manage the portfolio of existing loans managed by Quick Cash and required origination and placement services in respect of future loans (Quick Cash is prohibited from making loans, other than those which Case Funding does not wish to make and Quick Cash is responsible for all out-of-pocket third party fees and expenses relating to its business).

Payments received for services provided will be as follows:

Months	Amount
June – December 2011	Nil
January – June 2012	\$16,000/month
July 2012 – June 2013	\$4,000/month
July 2013 – June 2014	\$1,000/month

This revenue is recorded in Ancillary finance and other fee income. The amounts were determined at the time of Case Funding's acquisition and reflect negotiated market terms and the expected level of administrative services that will be provided to Quick Cash over the term of the agreement.

**CONTROLS & PROCEDURES**

Chesswood's Chief Executive Officer and Director of Finance evaluated, or caused an evaluation under their supervision, of the design and operating effectiveness of the Company's disclosure controls and procedures (as defined in National Instrument 52-109 – Certification of Disclosure in Issuers' Annual and Interim Filings) as at September 30, 2013 and have concluded that the disclosure controls and procedures were appropriately designed and have been effective, subject to the weaknesses described below.

Chesswood has also established internal controls over financial reporting (as defined in National Instrument 52-109) ("ICFR") to provide reasonable assurance regarding the reliability of the Company's financial reporting and preparation of its financial statements for external purposes in accordance with GAAP. The Company's Chief Executive Officer and Director of Finance assessed, or caused an assessment under their supervision, of the design and operating effectiveness of the Company's ICFR as at September 30, 2013 using the Committee of Sponsoring Organizations Internal Control – Integrated Framework. Based on that assessment, it was determined that the Company's ICFR was designed appropriately and was effective with the below noted exceptions.

The Company's audit committee is working with management on its independent review regime and monitoring the implementation of the other control enhancement steps envisioned below.

**Weakness of Controls**

Based on management's evaluation of controls, it was concluded that the Company's disclosure controls and procedures and its ICFR had some weaknesses. A material weakness is defined as a deficiency, or a combination of deficiencies, such that there is a reasonable possibility that a material misstatement of the Company's annual or interim consolidated financial

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FOR THE THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2013

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statements will not be prevented or detected on a timely basis. The weaknesses in disclosure controls and procedures and ICFR, and the additional processes undertaken to address such weaknesses, can be summarized as follows:

1) Segregation of Duties

Given the Company's size, it has limited resources within the finance department at head office to adequately segregate duties and to permit or necessitate the comprehensive documentation of all policies and procedures that form the basis of an effective design of ICFR. As a result, the Company is reliant on the knowledge of a limited number of employees and on the performance of mitigating procedures during its financial close process to ensure that the consolidated financial statements are presented fairly in all material respects. Although the finance department of Pawnee has staffing levels which the Company's management believes is appropriate in the context of the scope of Pawnee's operations, and although the individuals comprising the members of the Company's management and Pawnee's management responsible for financial reporting are considered to have appropriate proficiency and experience to effectively perform their respective duties, the nature and size of the Company's operations are such that the duties are performed by a small number of persons. While management of the Company believes that the flow of information and degree of consultation with the finance personnel of Pawnee is significant, in order to mitigate the risk of material misstatement in the consolidated financial statements, the Company implemented additional review and monitoring controls at head office on a monthly basis, and at Pawnee on a quarterly basis, beginning in the second quarter of 2009. In addition, further steps to cross train existing personnel have been undertaken where possible.

2) Information Technology Controls

Due to the relatively small size of the Company, the Company has not been able to maintain effective controls over certain key end user computing applications, such as spreadsheets, used in the Company's financial reporting process as well as appropriate security controls to manage access to key information. Controls pertaining to access profiles and password protocols require revision to mitigate the risk of inappropriate access to systems and applications. In addition, improvements to exception reporting are required to ensure that any unauthorized modification of the data or formulas within spreadsheets is identified and reported. It should be noted that the foregoing weaknesses relate to the Company and its systems and that Pawnee's systems are believed to be more commensurate with the scope of its operations.

Given the above noted weaknesses, the Company has performed additional analyses and other post-closing procedures to ensure the consolidated financial statements are prepared accurately and completely and that the disclosed data is in accordance with GAAP.

3) Anti-fraud controls

As a result of the lack of segregation of duties at the Company level as described above, the anti-fraud controls are limited. While management found no evidence of fraudulent activity, the Director of Finance has access to both accounting records and corporate assets, principally the operating bank account, and prepares journal entries without any independent review. Management feels the existing signing authorities and current review of bank balances is sufficient to mitigate the risk.

No changes were made to the design of the Company's ICFR during the quarter ended September 30, 2013 that would have materially affected or would be reasonably likely to materially affect the Company's ICFR.

It should be noted that a control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues, including instances of fraud, if any, have been detected. These inherent limitations include, amongst other items: (i) that management's assumptions and judgments could ultimately prove to be incorrect under varying conditions and circumstances; (ii) the impact of undetected errors; and (iii) controls may be circumvented by the unauthorized acts of individuals, by collusion of two or more people, or by management override.

The design of any system of controls is also based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential (future) conditions.

FOR THE THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2013

## MARKET FOR SECURITIES

The Common Shares are traded on the Toronto Stock Exchange under the symbol CHW. The following table summarizes the high and low sales prices of the Common Shares and the average daily trading volume for each month in the period ended September 30, 2013, as reported by the Toronto Stock Exchange.

2013	High	Low	Average Daily Volume
January	\$9.30	\$8.86	6,024
February	\$9.67	\$8.90	34,417
March	\$9.98	\$9.37	10,372
April	\$11.00	\$9.70	14,445
May	\$12.30	\$10.11	21,734
June	\$11.20	\$10.10	8,578
July	\$12.49	\$10.72	8,658
August	\$12.95	\$11.06	11,583
September	\$12.90	\$11.99	8,922
	\$12.95	\$8.86	13,689

## ADDITIONAL INFORMATION

Additional information about Chesswood is available:

- At the [www.chesswoodgroup.com](http://www.chesswoodgroup.com) website
- At the [www.sedar.com](http://www.sedar.com) website
- Via email to [investorrelations@Chesswoodgroup.com](mailto:investorrelations@Chesswoodgroup.com), or
- Via phone at 416-386-3099



**CHESSWOOD GROUP LIMITED**  
**CONDENSED CONSOLIDATED INTERIM STATEMENTS OF FINANCIAL POSITION**  
(in thousands of dollars)

	<i>Note</i>	<b>September 30, 2013</b>	<b>December 31, 2012</b>
		<i>(unaudited)</i>	<i>(audited)</i>
<b>ASSETS</b>			
Cash and cash equivalents		\$ 5,214	\$ 5,591
Accounts receivable		1,493	771
Inventories		7,128	7,881
Prepaid expenses and other assets		644	985
Finance receivables	5	150,615	124,250
Deferred tax assets		340	359
Property and equipment		1,235	893
Intangible assets		6,823	6,795
Goodwill		14,253	13,870
<b>TOTAL ASSETS</b>		<b>\$ 187,745</b>	<b>\$ 161,395</b>
<b>LIABILITIES</b>			
Accounts payable and other liabilities	10	\$ 7,688	\$ 8,260
Vehicle financing		5,969	6,199
Interest rate swaps		1,531	2,489
Borrowings		71,667	47,577
Customer security deposits		11,622	10,994
Deferred tax liabilities		22,533	25,321
		<b>121,010</b>	<b>100,840</b>
<b>SHAREHOLDERS' EQUITY</b>			
Common shares		45,051	44,215
Non-controlling interest		9,978	9,357
Reserve - share-based compensation		3,667	3,160
Accumulated other comprehensive loss		(377)	(1,883)
Retained earnings		8,416	5,706
		<b>66,735</b>	<b>60,555</b>
<b>TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY</b>		<b>\$ 187,745</b>	<b>\$ 161,395</b>

**CHESSWOOD GROUP LIMITED**  
**CONDENSED CONSOLIDATED INTERIM STATEMENTS OF INCOME**  
**FOR THE THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2013 AND 2012**  
(in thousands of dollars, unaudited)

		Three months ended September 30,		Nine months ended September 30,	
	Note	2013	2012	2013	2012
<b>Finance revenue</b>					
Interest revenue on finance leases and loans		\$ 9,506	\$ 7,766	\$ 27,425	\$ 23,072
Ancillary finance and other fee income		1,357	1,193	4,231	3,587
		<u>10,863</u>	<u>8,959</u>	<u>31,656</u>	<u>26,659</u>
<b>Finance expenses</b>					
Interest expense		1,043	859	2,927	2,567
Provision for credit losses		1,908	1,422	4,839	3,670
		<u>2,951</u>	<u>2,281</u>	<u>7,766</u>	<u>6,237</u>
<b>Finance margin</b>		<u>7,912</u>	<u>6,678</u>	<u>23,890</u>	<u>20,422</u>
<b>Revenue - automotive operations</b>		<u>14,072</u>	<u>12,515</u>	<u>37,411</u>	<u>37,131</u>
<b>Cost of sales - automotive operations</b>					
Change in inventories		(950)	2,160	754	(1,895)
Automobiles, parts, and other costs		13,135	8,746	31,539	34,390
Interest expense		33	59	124	180
		<u>12,218</u>	<u>10,965</u>	<u>32,417</u>	<u>32,675</u>
<b>Automotive gross margin</b>		<u>1,854</u>	<u>1,550</u>	<u>4,994</u>	<u>4,456</u>
<b>Gross margin before expenses</b>		<u>9,766</u>	<u>8,228</u>	<u>28,884</u>	<u>24,878</u>
<b>Expenses</b>					
Personnel expenses		2,781	2,601	8,203	7,574
Other expenses		1,945	1,673	5,369	4,981
Amortization - property and equipment		47	39	132	143
Amortization - intangible assets		—	125	169	376
		<u>4,773</u>	<u>4,438</u>	<u>13,873</u>	<u>13,074</u>
<b>Income before undernoted items</b>		<u>4,993</u>	<u>3,790</u>	<u>15,011</u>	<u>11,804</u>
Contingent consideration		—	(48)	—	(138)
Unrealized gain (loss) on interest rate swaps		47	(169)	1,037	(211)
Unrealized gain (loss) on foreign exchange		(22)	(338)	16	(151)
<b>Income before taxes</b>		<u>5,018</u>	<u>3,235</u>	<u>16,064</u>	<u>11,304</u>
Provision for taxes		(2,146)	(1,677)	(6,869)	(5,538)
<b>Net Income</b>		<u>\$ 2,872</u>	<u>\$ 1,558</u>	<u>\$ 9,195</u>	<u>\$ 5,766</u>
<b>Attributable to:</b>					
Common shareholders		\$ 2,503	\$ 1,356	\$ 8,006	\$ 5,013
Non-controlling interest		\$ 369	\$ 202	\$ 1,189	\$ 753
Basic earnings per share	15	\$ 0.25	\$ 0.14	\$ 0.81	\$ 0.51
Diluted earnings per share	15	\$ 0.23	\$ 0.13	\$ 0.76	\$ 0.49

**CHESSWOOD GROUP LIMITED**  
**CONDENSED CONSOLIDATED INTERIM STATEMENTS OF COMPREHENSIVE INCOME (LOSS)**  
**FOR THE THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2013 AND 2012**  
(in thousands of dollars, unaudited)

	<b>Three months ended September 30,</b>		<b>Nine months ended September 30,</b>	
	<b>2013</b>	<b>2012</b>	<b>2013</b>	<b>2012</b>
Net income	<b>\$ 2,872</b>	<b>\$ 1,558</b>	<b>\$ 9,195</b>	<b>\$ 5,766</b>
Other comprehensive income (loss):				
Unrealized gain (loss) on translation of foreign operations	<b>(1,329)</b>	<b>(1,387)</b>	<b>1,729</b>	<b>(1,538)</b>
Comprehensive income for the period	<b><u>\$ 1,543</u></b>	<b><u>\$ 171</u></b>	<b><u>\$ 10,924</u></b>	<b><u>\$ 4,228</u></b>
<b>Attributable to:</b>				
Common shareholders	<b>\$ (1,155)</b>	<b>\$ (1,206)</b>	<b>\$ 1,506</b>	<b>\$ (1,337)</b>
Non-controlling interest	<b>\$ (174)</b>	<b>\$ (181)</b>	<b>\$ 223</b>	<b>\$ (201)</b>

**CHESSWOOD GROUP LIMITED**  
**CONDENSED CONSOLIDATED INTERIM STATEMENTS OF CHANGES IN EQUITY**  
**FOR THE THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2013 AND 2012**  
(in thousands of dollars, unaudited)

	Note	Common Shares	Common Shares	Non- controlling interest	Share-based compensation Reserve	Accumulated other comprehensive loss	Retained earnings	Total
		(# '000s)						
<b>Shareholders' equity - December 31, 2012</b>		<b>9,843</b>	<b>\$ 44,215</b>	<b>\$ 9,357</b>	<b>\$ 3,160</b>	<b>\$ (1,883)</b>	<b>\$ 5,706</b>	<b>\$ 60,555</b>
Net income		—	—	1,189	—	—	8,006	9,195
Dividends declared		—	—	(791)	—	—	(5,296)	(6,087)
Share-based compensation		—	—	—	1,070	—	—	1,070
Exercise of restricted share units	13	46	340	—	(340)	—	—	—
Exercise of options	13	70	496	—	(223)	—	—	273
Unrealized gains on translation of foreign operations		—	—	223	—	1,506	—	1,729
<b>Shareholders' equity - September 30, 2013</b>		<b>9,959</b>	<b>\$ 45,051</b>	<b>\$ 9,978</b>	<b>\$ 3,667</b>	<b>\$ (377)</b>	<b>\$ 8,416</b>	<b>\$ 66,735</b>

	Note	Common Shares	Common Shares	Non- controlling interest	Share-based compensation Reserve	Accumulated other comprehensive loss	Retained earnings	Total
		(# '000s)						
Shareholders' equity - December 31, 2011		9,811	\$ 43,845	\$ 9,269	\$ 2,269	\$ (950)	\$ 4,447	\$ 58,880
Net income		—	—	753	—	—	5,013	5,766
Dividends declared		—	—	(702)	—	—	(4,667)	(5,369)
Share-based compensation		—	—	—	1,090	—	—	1,090
Exercise of restricted share units	13	40	306	—	(306)	—	—	—
Exercise of options	13	56	318	—	(189)	—	—	129
Repurchase of common shares under issuer bid		(59)	(262)	—	—	—	(183)	(445)
Unrealized loss on translation of foreign operations		—	—	(201)	—	(1,337)	—	(1,538)
Shareholders' equity - September 30, 2012		9,848	\$ 44,207	\$ 9,119	\$ 2,864	\$ (2,287)	\$ 4,610	\$ 58,513
Net income		—	—	421	—	—	2,802	3,223
Dividends declared		—	—	(244)	—	—	(1,626)	(1,870)
Share-based compensation		—	—	—	346	—	—	346
Exercise of restricted share units		—	—	—	—	—	—	—
Exercise of options		16	105	—	(50)	—	—	55
Repurchase of common shares under issuer bid		(21)	(97)	—	—	—	(80)	(177)
Unrealized gain on translation of foreign operations		—	—	61	—	404	—	465
<b>Shareholders' equity - December 31, 2012</b>		<b>9,843</b>	<b>\$ 44,215</b>	<b>\$ 9,357</b>	<b>\$ 3,160</b>	<b>\$ (1,883)</b>	<b>\$ 5,706</b>	<b>\$ 60,555</b>

**CHESSWOOD GROUP LIMITED**  
**CONDENSED CONSOLIDATED INTERIM STATEMENTS OF CASH FLOWS**  
**FOR THE THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2013 AND 2012**  
(in thousands of dollars, unaudited)

	<i>Note</i>	Three months ended September 30, <b>2013</b>	2012	Nine months ended September 30, <b>2013</b>	2012
<b>OPERATING ACTIVITIES</b>					
Net income		\$ 2,872	\$ 1,558	\$ 9,195	\$ 5,766
Non-cash items included in net income					
Amortization		47	164	301	519
Provision for credit losses		2,691	2,055	6,842	5,241
Share-based compensation expense		289	334	1,070	1,090
Provision for taxes		2,146	1,677	6,869	5,538
Other non-cash items	16	15	564	(931)	551
		<u>5,188</u>	<u>4,794</u>	<u>14,151</u>	<u>12,939</u>
Cash from operating activities before change in net operating assets		<u>8,060</u>	<u>6,352</u>	<u>23,346</u>	<u>18,705</u>
Change in operating net assets					
Finance receivables	16	(5,514)	(2,376)	(28,905)	(14,716)
Borrowings - net	16	3,089	(4,706)	22,251	2,544
Customer security deposits		(162)	189	255	796
Accounts receivable		(355)	316	(722)	130
Inventories		(950)	2,160	754	(1,895)
Vehicle financing proceeds (payments) - net		661	(2,257)	(230)	1,713
Prepaid expenses and other assets		141	(558)	3	(394)
Accounts payable and other liabilities		191	512	24	34
		<u>(2,899)</u>	<u>(6,720)</u>	<u>(6,570)</u>	<u>(11,788)</u>
Cash from operating activities before tax refunds and payments		5,161	(368)	16,776	6,917
Income tax refund received		426	13	446	16
Income taxes paid		(5,934)	(631)	(11,433)	(1,904)
<b>Cash from (used in) operating activities</b>		<u>(347)</u>	<u>(986)</u>	<u>5,789</u>	<u>5,029</u>
<b>INVESTING ACTIVITIES</b>					
Purchase of property and equipment		(137)	(111)	(467)	(190)
<b>Cash used in investing activities</b>		<u>(137)</u>	<u>(111)</u>	<u>(467)</u>	<u>(190)</u>
<b>FINANCING ACTIVITIES</b>					
Proceeds from exercise of options		170	82	273	129
Repurchase of common shares		—	—	—	(445)
Cash dividends paid	14	(2,055)	(1,865)	(6,024)	(5,311)
<b>Cash used in financing activities</b>		<u>(1,885)</u>	<u>(1,783)</u>	<u>(5,751)</u>	<u>(5,627)</u>
Unrealized foreign exchange gain (loss) on cash		(46)	(66)	52	(41)
Net decrease in cash and cash equivalents		(2,415)	(2,946)	(377)	(829)
Cash and cash equivalents, beginning of period		7,629	9,455	5,591	7,338
<b>Cash and cash equivalents, end of period</b>		<u>\$ 5,214</u>	<u>\$ 6,509</u>	<u>\$ 5,214</u>	<u>\$ 6,509</u>

## 1. NATURE OF BUSINESS AND BASIS OF PREPARATION

Chesswood Group Limited (the “Company”) is incorporated under the laws of the Province of Ontario. The Company’s head office is located at 4077 Chesswood Drive, Toronto, Ontario, M3J 2R8.

The Company holds all of the limited partnership units of Chesswood Holding LP (“Holding LP”). Holding LP holds a 100% interest in Chesswood Holdings Ltd. and substantially all of the limited partnership units of Sherway LP (“Sherway”). Chesswood Holdings Ltd. owns 100% of the shares of the operating company, Lease-Win Limited (“Lease-Win”) as well as 100% of the shares of Chesswood U.S. Acquisition Co Ltd. (“U.S. Acquisitionco”), a corporation which owns 100% of the shares of the operating company Pawnee Leasing Corporation (“Pawnee”), incorporated in Colorado, United States and 100% of the shares of Windset Capital Corporation (“Windset”), incorporated in Utah, United States. The Company owns all of the shares of Case Funding Inc., which operates the Company’s legal financing business in the United States.

As partial consideration for the acquisition of Pawnee in May 2006, 1,274,601 Class B shares and 203,936 Class C shares of a subsidiary (U.S. Acquisitionco) were issued (“Exchangeable Securities”). The Exchangeable Securities are non-voting shares of U.S. Acquisitionco and are fully exchangeable for Common Shares of the Company, on a one-for-one basis, for no additional consideration, through a series of steps and entitle the holders to receive the same dividends as the Common Shares. Attached to the Exchangeable Securities are Special Voting Units of the Company which provide the holders of the Exchangeable Securities voting equivalency to Company Shareholders. The Exchangeable Securities are reflected as non-controlling interest.

Through its interest in Pawnee, the Company is involved in the business of micro and small-ticket equipment financing to small businesses in the start-up and “B” credit market in the lower 48 states of the United States. Through its interest in Windset Capital Corporation (“Windset”), Chesswood is becoming involved with the business of providing working capital loans to small businesses in United States. Through its interest in Sherway LP, the Company is involved in selling, servicing and leasing Acura automobiles in the Province of Ontario. Through its interest in Lease-Win, the Company had a portfolio of automobile leases under administration, the remainder of which were sold or were paid out by the lessees during the year.

The consolidated financial statements have been prepared on the going concern and historical cost basis, except for derivative financial instruments and liabilities held for trading which have been measured at fair value. In order to improve clarity, certain items have been combined on the statements of financial position with detail provided separately in the notes.

The reporting currency is the Canadian dollar. The financial statements are presented in thousands of Canadian dollars except per share amounts. The functional currency of the Company, Holding LP, Chesswood Holdings Ltd., Sherway LP, and Lease-Win is the Canadian dollar. The functional currency of U.S. Acquisitionco, Pawnee, Windset and Case Funding is the United States dollar. The statements of income and cash flows of the subsidiaries located in the United States have been translated using the average rate for the nine months ended September 30, 2013 and 2012. The statements of financial position have been translated using the rate on the date of the statements of financial position and the exchange difference is included in other comprehensive income.

The U.S. dollar exchange rates, which have a material impact on the Company’s financial statements, are as follows:

Closing Rate As At		Average Rate For The Nine Months Ended	
September 30, 2013	December 31, 2012	September 30, 2013	September 30, 2012
<b>1.0285</b>	0.9949	<b>1.0235</b>	1.0023

## 2. CONSOLIDATION

The consolidated financial statements include the financial statements of the Company and its subsidiaries as noted above. Subsidiaries are consolidated using the purchase method from the date of acquisition, being the date on which the Company

obtains control, and continue to be consolidated as long as control is held. The financial statements of all subsidiaries are prepared for the same reporting period as the Company, using uniform accounting policies in accordance with IAS 27, *Consolidated and Separate Financial Statements*. All intra-group balances and items of income and expense resulting from intra-group transactions are eliminated in full.

Transaction costs, other than those associated with the issue of debt or equity securities, that the Company incurs in connection with a business combination are expensed as incurred.

### 3. SIGNIFICANT ACCOUNTING POLICIES

The Company's consolidated financial statements, including comparatives, are prepared in accordance with International Financial Reporting Standards ("IFRS"), as issued by the International Accounting Standards Board ("IASB"). The term IFRS also includes all International Accounting Standards ("IAS"); all interpretations of the International Financial Reporting Interpretations Committee ("IFRIC") mandatory for the fiscal year 2013 are also applied.

These condensed interim consolidated financial statements have been prepared in accordance with International Accounting Standard ("IAS") 34, *Interim Financial Reporting* on a basis consistent with the accounting policies disclosed in the audited consolidated financial statements for the year ended December 31, 2012. The condensed interim financial statements should be read in conjunction with the company's most recently issued Annual Report which includes information necessary or useful to understand the Company's businesses and financial reporting.

The condensed consolidated interim financial statements are unaudited. Financial information in this report reflects any adjustments (consisting of normal recurring adjustments) that are, in the opinion of management, necessary for a fair statement of results for the interim periods in accordance with IFRS.

The results reported in these interim consolidated financial statements should not be regarded as necessarily indicative of results that may be expected for the entire year.

The Company's significant accounting policies were presented as Note 3 to the Consolidated Financial Statements for the fiscal year ended December 31, 2012 included in that report, and have been consistently applied in the preparation of these interim financial statements except for the following.

#### **Accounting standards adopted in the current year**

The following amendments to standards were adopted in the current year:

##### *Financial Instruments: Disclosures - Offsetting Financial Assets and Financial Liabilities*

Amendments to *IFRS 7 Financial Instruments: Disclosures* introduced enhanced disclosure around the transfer of financial assets and associated risks to include additional disclosure requirements for financial assets and liabilities that can be offset in the statement of financial position. The effective date for the amendments to IFRS 7 was annual periods beginning on or after January 1, 2013. There was no impact of these amendments on the Company's results of operations and financial position.

##### *Consolidated Financial Statements*

IFRS 10, *Consolidated Financial Statements*, will replace IAS 27 and SIC-12 (*Consolidation – Special Purpose Entities*). The new standard provides a single model for consolidation based on control, which exists when an investor has the power to control, is exposed to or has the right to variable returns from its involvement with the investee and has the current ability to affect those returns through its power over the investee. The standard also provides guidance on how to evaluate power to control. IFRS 10 was effective for annual periods beginning on or after January 1, 2013. IFRS 10 had no impact on the Company's results of operations and financial position.

*Disclosure of interests in other entities*

IFRS 12, *Disclosure of Interests in Other Entities*, includes amended disclosure requirements relating to subsidiaries, joint agreements, and associates. Additional disclosures include judgments and assumptions made in determining how to classify involvement with another entity, interests that non-controlling parties have in the consolidated entities, and the nature and risks associated with interests in other entities. The standard was effective for annual periods beginning on or after January 1, 2013. IFRS 12 had no impact on the Company's results of operations and financial position.

*Fair value measurement*

IFRS 13, *Fair Value Measurement*, establishes a single source of guidance for fair value measurements for financial reporting purposes and also requires enhanced disclosures in both annual and interim financial statements. The standard is effective for annual periods beginning on or after January 1, 2013. IFRS 13 had no impact on the Company's results of operations and financial position.

**4. ACCOUNTING STANDARDS ISSUED BUT NOT YET EFFECTIVE***Financial Instruments: Presentation*

IAS 32, *Financial Instruments: Presentation* has been amended to include additional presentation requirements for financial assets and liabilities that can be offset in the statement of financial position. The effective date for the amendments to IAS 32 is annual periods beginning on or after January 1, 2014. The revised standard relates only to presentation and will not impact the financial results of the Company.

*Financial Liabilities: Measurement*

In October 2010, the IASB issued *IFRS 9 Financial Instruments*, which represents the completion of the first part of a three-part project to replace *IAS 39 Financial Instruments: Recognition and Measurement* with a new standard. As per the new standard, an entity choosing to measure a liability at fair value will present the portion of the change in its fair value due to changes in the entity's own credit risk in the other comprehensive income or loss section of the entity's statement of comprehensive loss, rather than within profit or loss. Additionally, IFRS 9 includes revised guidance related to the de-recognition of financial instruments. IFRS 9 applies to financial statements for annual periods beginning on or after January 1, 2015, with early adoption permitted. The Company plans to adopt these new standards when they become effective and is currently assessing the impact of this standard.

*Financial Instruments (Classification and Measurement)*

IFRS 9, *Financial Instruments* will replace *IAS 39, Financial Instruments: Recognition and Measurement*. IFRS 9 uses a single approach to determine whether a financial asset is measured at amortized cost or fair value. The approach in IFRS 9 is based on how an entity manages its financial instruments in the context of its business model and the contractual cash flow characteristics of the financial assets. The new standard also requires a single impairment method to be used, replacing the multiple impairment methods in IAS 39. Most of the requirements in IAS 39 for classification and measurement of financial liabilities were carried forward unchanged to IFRS 9. Mandatory Effective Date of IFRS 9 and Transition Disclosures, issued in December 2011, deferred the effective date to annual periods beginning on or after January 1, 2015, with earlier adoption permitted.



## 5. FINANCE RECEIVABLES

Finance receivables comprise:

	Note	September 30, 2013	December 31, 2012
		(\$ thousands)	
Net investment in leases	6	\$ 124,791	\$ 111,905
Equipment financing agreements	7	16,756	6,700
Legal finance receivables	9	9,068	5,645
		<u>\$ 150,615</u>	<u>\$ 124,250</u>

## 6. NET INVESTMENT IN LEASES

(a) Net investment in leases includes the following:

	September 30, 2013	December 31, 2012
	(\$ thousands)	
Total minimum lease payments for non-securitized leases	\$157,598	\$140,297
Residual values of leased equipment	18,903	17,923
	<u>\$176,501</u>	<u>\$158,220</u>
Initial direct costs of lease acquisition	9,172	8,447
Unearned income	(57,360)	(51,871)
<b>Net investment in leases before allowance for doubtful accounts</b>	<b>\$128,313</b>	<b>\$114,796</b>
Allowance for doubtful accounts (b)	(3,522)	(2,891)
<b>Net investment in leases</b>	<b>\$124,791</b>	<b>\$111,905</b>
Current portion	43,138	46,432
Net investment in leases – long-term portion	<u>\$81,653</u>	<u>\$65,473</u>

(b) The activity in the allowance for doubtful accounts is as follows:

	Nine months ended September 30,	
	2013	2012
	(\$ thousands)	
Balance, beginning of period	\$ 2,891	\$ 2,424
Provision for credit losses	4,572	3,634
Impact of change in foreign exchange rates	100	(81)
Charge-offs	(6,034)	(4,961)
Recoveries	1,993	1,570
Balance, end of period	<u>\$ 3,522</u>	<u>\$ 2,586</u>

## 7. EQUIPMENT FINANCING AGREEMENTS

	September 30, 2013	December 31, 2012
	(\$ thousands)	
Equipment financing agreements (“EFAs”)	\$ 16,931	\$ 6,742
Allowance for doubtful accounts (a)	(175)	(42)
<b>Equipment financing agreements</b>	<b>\$ 16,756</b>	<b>\$ 6,700</b>
Current portion	5,883	1,617
Equipment financing agreements – long-term portion	<u>\$ 10,873</u>	<u>\$ 5,083</u>

- (a) Pawnee’s leases and EFA’s each are composed of a large number of homogenous agreements respectively, with relatively small balances. Pawnee’s underwriting requirements and standards for EFAs are the same as those required for leases. The activity in the allowance for doubtful accounts is as follows:

	Nine months ended September 30, 2013	2012
	(\$ thousands)	
Balance, beginning of period	\$ 42	\$ —
Provision for credit losses	255	—
Impact of change in foreign exchange rates	2	—
Charge-offs	(135)	—
Recoveries	11	—
Balance, end of period	<u>\$ 175</u>	<u>\$ —</u>

## 8. FINANCE RECEIVABLES PAST DUE

Pawnee’s lease receivables and EFA’s each are composed of a large number of homogenous leases and EFAs respectively, with relatively small balances. Thus, the evaluation of the allowance for credit losses is performed collectively for the lease receivable and EFA portfolio.

The following aging of net investment in leases and EFAs before allowance for doubtful accounts represents the full carrying value of the leases and EFAs not just the lease payments that are past due. The net investment in leases and EFAs presented excludes the \$11.6 million (December 31, 2012 - \$11.0 million) in security deposits from borrowers, potential proceeds from repossessed collateral in vehicles and equipment, and potential recoveries from personal guarantees that would offset any charge-offs. An estimate of the fair value for the collateral cannot reasonably be determined.

	September 30, 2013				
(\$ thousands)	Current	1-30 days	31 - 60 days	61 - 90 days	Over 90 days
Equipment leases	\$ 121,799	\$ 3,569	\$ 1,326	\$ 486	\$ 1,133
EFA's	16,633	164	54	22	58
	138,432	3,733	1,380	508	1,191
Impaired	150	306	263	233	1,191
Past due but not impaired	\$ —	\$ 3,427	\$ 1,117	\$ 275	\$ —

	December 31, 2012				
(\$ thousands)	Current	1-30 days	31 - 60 days	61 - 90 days	Over 90 days
Equipment leases	\$ 109,454	\$ 2,752	\$ 1,335	\$ 372	\$ 883
EFA's	6,699	-	43	-	-
	116,153	2,752	1,378	372	883
Impaired	44	90	436	87	883
Past due but not impaired	\$ —	\$ 2,662	\$ 942	\$ 285	\$ —

## 9. LEGAL FINANCE RECEIVABLES

Legal finance receivables consist of:

	September 30, 2013	December 31, 2012
	(\$ thousands)	
Attorney loans and medical liens	\$ 4,101	\$ 2,296
Plaintiff advances (note 17 (a)(b)(c))	4,967	3,349
<b>Legal finance receivables</b>	<b>\$ 9,068</b>	<b>\$ 5,645</b>
Current portion (i)	5,685	2,728
Legal finance receivables – long-term portion	<b>\$ 3,383</b>	<b>\$ 2,917</b>

It was determined that there is no objective evidence that any of the attorney loans or medical liens are individually impaired at September 30, 2013 and December 31, 2012, thus an allowance for doubtful accounts was not recognized.

- (i) The contracts are deemed to have fixed or determinable payments, in that the payments are due when the underlying cases are settled. However the date of settlement is unknown and therefore is estimated. The terms of the plaintiff advances are on a non-recourse basis, and payment depends on the success and potential claim size. Thus, the current portion is an estimate of future cash collections.

## 10. ACCOUNTS PAYABLE AND OTHER LIABILITIES

Accounts payable and other liabilities comprise:

	September 30, 2013	December 31, 2012
	(\$ thousands)	
Unfunded leases and EFAs	\$ 1,469	\$ 1,590
Sales tax payable	760	867
Payroll related payables and accruals	1,268	1,053
Taxes payable	1,231	1,975
Dividends payable	686	623
Withholding taxes payable	414	425
Accrued liabilities	892	631
Accounts payable	361	451
Property taxes payable on equipment leases	252	296
Deferred lease incentive	107	125
Customer deposits and prepayments	248	224
	<b>\$ 7,688</b>	<b>\$ 8,260</b>

All amounts are due within one year, except for deferred lease incentive which is being amortized over the remaining term of the leases which expire in 2017.

## 11. MINIMUM PAYMENTS

The following are the contractual principal payments and maturities of financial liabilities and other commitments:

(\$ thousands)	2013	2014	2015	2016	2017 +	Total
Accounts payable and other liabilities	\$ 7,588	\$ 26	\$ 29	\$ 31	\$ 14	<b>7,688</b>
Vehicle financing	5,969	-	-	-	-	<b>5,969</b>
Interest rate swaps	-	224	867	183	257	<b>1,531</b>
Borrowings (a)	-	-	-	71,667	-	<b>71,667</b>
Customer security deposits (b)	1,177	2,943	3,056	2,493	1,953	<b>11,622</b>
	<b>\$ 14,734</b>	<b>\$ 3,193</b>	<b>\$ 3,952</b>	<b>\$ 74,374</b>	<b>\$ 2,224</b>	<b>\$ 98,477</b>
Other financial commitments (c)	205	823	796	739	360	<b>2,923</b>
Total commitments	<b>\$ 14,939</b>	<b>\$ 4,016</b>	<b>\$ 4,748</b>	<b>\$ 75,113</b>	<b>\$ 2,584</b>	<b>\$ 101,400</b>

(a) Pawnee's financing credit facility is a line-of-credit; as such the balance can fluctuate. The credit facility matures in 2016.

(b) The Company's experience has shown that the actual contractual payment streams will vary depending on a number of variables including: prepayment rates, charge-offs and modifications. Accordingly, the scheduled contractual payments of customer security deposits shown are not to be regarded as a forecast of future cash payments.

(c) The Company and its subsidiaries are committed to future minimum rental payments under existing leases for premises, excluding occupancy costs and property tax, expiring in 2015 and 2017. The leases contain renewal options for an additional term of 5 years.

For other commitments, refer to Note 12.

## 12. CONTINGENT LIABILITIES AND OTHER FINANCIAL COMMITMENTS

### (a) *Contingent liabilities*

The Company is subject to various claims and legal actions in the normal course of its business, from various customers, suppliers and others. Since the individual value of each claim and the total value of all claims as at September 30, 2013 and December 31, 2012 were not material, additional disclosure is not required. No provision has been recognized.

### (b) *Other financial commitments*

- (i) The Company has entered into retention agreements with certain employees whereby such employees shall be entitled to certain retention severance amounts upon the occurrence of events identified in each respective agreement. Included in the retention agreement of Chesswood's Chief Executive Officer is an award of 125,000 options on the second anniversary of the agreement date, or earlier, in the case of a change of control.
- (ii) Pawnee maintains a Simple IRA Plan (the "Plan") for its employees. Pawnee's obligation is to match contributions made by participating employees up to 3.0% of their base pay. For the years ended December 31, 2012 and 2011, Pawnee's matching contributions to the Plan totaled U.S.\$51,300 and U.S.\$46,900, respectively.
- (iii) Incentive Payment Amount on the acquisition of Case Funding - The consideration is payable in the event that Case Funding's normalized net income ("NNI") for the 25th through 36th months following the Acquisition Date (June 10, 2011) achieves the targeted amount of approximately U.S.\$4.7 million (the "Targeted Amount"), whereby an amount of U.S.\$1.4 million (the "Incentive Payment Amount") (or an identical percentage adjusted portion of the Incentive Payment Amount if NNI is less than, but at least 90% of, the Targeted Amount) will be paid no later than the 38th month. It was determined at December 31, 2012 that the probability that the Targeted Amount would be reached was minimal. The estimate of the fair value of contingent consideration and bonus payable requires very subjective assumptions to be made of various potential operating result scenarios and discount rates. Although the Company believes that there will be no Incentive Payment Amount due in August 2014, it will continue to periodically review NNI results and an updated assessment of various probability weighted projected NNI scenarios. If circumstances change and the Company determines that an earn-out payment becomes due, such future revisions may materially change the estimate of the fair value of contingent consideration and therefore materially affect the Company's future financial results.

### 13. COMPENSATION PLANS

#### (a) Share Options

A summary of the number of options outstanding is as follows:

	Three months ended September 30,		Nine months ended September 30,	
	2013	2012	2013	2012
Balance, beginning of period	<b>1,476,878</b>	1,447,150	<b>1,522,900</b>	1,227,750
Granted	—	—	—	242,500
Exercised	<b>(24,250)</b>	(33,250)	<b>(70,272)</b>	(56,350)
Forfeited	<b>(10,000)</b>	—	<b>(10,000)</b>	—
Balance, end of period	<b>1,442,628</b>	1,413,900	<b>1,442,628</b>	1,413,900

During the nine months ended September 30, 2013, salaries and commission expense and reserve - share-based compensation included \$669,300 (2012 - \$856,200) relating to option expense.

During the nine months ended September 30, 2013, 70,272 options were exercised (2012 - 56,350) for total cash consideration of \$273,000 (2012 - \$128,800). On exercise, the fair value of options that had been expensed to date during the vesting period of \$223,000 (2012 - \$189,100) was transferred from share-based compensation Reserve to Common Share capital. For the options exercised in 2013, the weighted average share price at the date of exercise was \$10.87 (2012 - \$7.81).

An analysis of the options outstanding at September 30, 2013 is as follows:

Grant date	Number of options outstanding	Vested	Expiry date	Exercise price
May 10, 2006	100,000	100,000	May 9, 2016	\$ 10.00
June 23, 2009	168,900	168,900	June 22, 2019	\$ 2.06
April 13, 2010	197,728	197,728	April 13, 2020	\$ 4.49
April 25, 2011	282,500	183,625	April 24, 2021	\$ 7.79
June 10, 2011	132,500	80,000	June 9, 2021	\$ 7.73
December 6, 2011	200,000	60,000	December 6, 2021	\$ 6.14
June 25, 2012	231,000	68,250	June 24, 2022	\$ 7.45
July 9, 2012	5,000	1,500	July 8, 2022	\$ 7.42
December 6, 2012	125,000	—	December 6, 2022	\$ 8.86
	<b>1,442,628</b>	<b>860,003</b>		

At September 30, 2013, the weighted average exercise price is \$6.62 (December 31, 2012 - \$6.50) and the weighted average remaining contractual life for all options outstanding is 7.55 years (December 31, 2012 - 8.01 years). The options exercisable at September 30, 2013 have a weighted average exercise price of \$6.01 (December 31, 2012 - 630,400 options at \$5.39).

## (b) Restricted Share Units

A summary of the restricted share units outstanding is as follows:

	Three months ended September 30,		Nine months ended September 30,	
	2013	2012	2013	2012
Balance, beginning of period	<b>89,000</b>	69,000	<b>69,000</b>	57,000
Granted	—	—	<b>51,500</b>	51,500
Exercised	<b>(14,000)</b>	—	<b>(45,500)</b>	(39,500)
Balance, end of period	<b>75,000</b>	69,000	<b>75,000</b>	69,000

During the nine months ended September 30, 2013, an aggregate of 44,000 (2012 - 44,000) restricted share units (“RSUs”) were granted to directors and expire in ten years. The holders of such RSUs are not entitled to the distributions paid before the RSUs are exercised. Such RSUs vest one year from the date of issue and are to be settled by the issue of Shares. RSUs granted are in respect of future services and are expensed over the vesting period. Compensation cost is measured based on the market price of the Shares on the date of the grant of the RSUs, which was \$11.65 (2012 - \$7.45). During the nine months ended September 30, 2013 and 2012, 7,500 RSUs were granted in accordance with the Case Funding purchase agreement to a senior executive of Case Funding, the RSUs vested immediately and were exercised by the executive.

During the nine months ended September 30, 2013, personnel expense and share-based compensation reserve included \$400,400 (2012 - \$234,300) relating to RSUs.

On exercise of the 45,500 RSUs (2012 – 39,500 RSUs), during the nine months ended September 30, 2013, the value of the RSUs of \$340,100 (2012 - \$306,000) that had been expensed during the vesting period was transferred from reserve - share-based compensation to Common Share capital. For the 45,500 RSUs exercised in 2013 (2012 – 39,500 RSUs), the weighted average share price at the date of exercise was \$10.93 (2012 - \$7.33).

As of September 30, 2013, unrecognized non-cash compensation expense related to non-vested RSUs was \$327,200 (2012 - \$241,360).

The following RSUs are outstanding at September 30, 2013:

Grant date	Number of RSUs outstanding	Vested	Expiry date	Grant price
April 13, 2010	20,000	20,000	April 12, 2020	\$ 4.49
April 25, 2011	5,000	5,000	April 24, 2021	\$ 7.79
June 25, 2012	6,000	6,000	June 24, 2022	\$ 7.45
May 22, 2013	44,000	—	May 21, 2023	\$ 11.65
	<b>75,000</b>	<b>31,000</b>		

#### 14. DIVIDENDS

The following dividends were paid to Common Shareholders and Exchangeable Securities holders during the nine months ended September 30, 2013:

Record date	Payment date	Cash dividend per share (\$)	Total dividend amount (\$ thousands)
December 31, 2012	January 15, 2013	\$0.055	\$ 623
January 31, 2013	February 15, 2013	\$0.055	623
February 28, 2013	March 15, 2013	\$0.060	679
March 31, 2013	April 15, 2013	\$0.060	681
April 30, 2013	May 15, 2013	\$0.060	681
May 31, 2013	June 17, 2013	\$0.060	682
June 30, 2013	July 15, 2013	\$0.060	684
July 31, 2013	August 15, 2013	\$0.060	685
August 31, 2013	September 16, 2013	\$0.060	686
Dividends paid during the nine months ended September 30, 2013			<b>\$ 6,024</b>

#### 15. EARNINGS PER SHARE

Basic earnings per share is computed by dividing net earnings for the period by the weighted average number of shares outstanding during the period.

	Three months ended September 30,		Nine months ended September 30,	
	2013	2012	2013	2012
Weighted average number of shares outstanding	<b>9,943,203</b>	9,828,782	<b>9,891,311</b>	9,821,194
Dilutive effect of options	<b>660,770</b>	344,938	<b>590,035</b>	283,646
Dilutive effect of RSUs	<b>78,326</b>	69,000	<b>77,762</b>	55,533
Weighted average shares outstanding for diluted earnings per share	<b>10,682,299</b>	10,242,720	<b>10,559,108</b>	10,160,373

In 2012, options to purchase 980,000 shares were outstanding during the period but were not included in the calculation of diluted earnings per share due to their anti-dilutive effect for the period.



## 16. CASH FLOW SUPPLEMENTARY DISCLOSURE

	For the three months ended September 30,		For the nine months ended September 30,	
	2013	2012	2013	2012
	(\$ thousands)			
<b>Other non-cash items included in net income</b>				
Unrealized loss (gain) on interest rate swaps	\$(47)	\$169	\$(1,037)	\$211
Unrealized loss (gain) on foreign exchange	22	338	(16)	151
Amortization of deferred financing costs	40	41	122	128
Contingent consideration and bonus payable	-	48	-	138
Gain on sale of leased vehicles	-	(32)	-	(77)
	<u>\$15</u>	<u>\$564</u>	<u>\$(931)</u>	<u>\$551</u>
<b>Finance receivables</b>				
Net investments in leases	\$(1,605)	\$(330)	\$(15,904)	\$(8,650)
Equipment finance agreements	(2,828)	(1,854)	(9,784)	(4,668)
Legal finance receivables	(1,081)	(270)	(3,217)	(2,212)
Net investments in leases – pledged	-	78	-	814
	<u>\$(5,514)</u>	<u>\$(2,376)</u>	<u>\$(28,905)</u>	<u>\$(14,716)</u>
<b>Borrowings - net</b>				
Line-of-credit – Pawnee – net	\$3,089	\$(4,680)	\$22,251	\$3,251
Securitization debt payments	-	(26)	-	(707)
	<u>\$3,089</u>	<u>\$(4,706)</u>	<u>\$22,251</u>	<u>\$2,544</u>
<b>Non-cash transactions</b>				
Common shares issued on exercise of restricted units	<u>\$104</u>	<u>\$-</u>	<u>\$340</u>	<u>\$306</u>

## 17. FINANCIAL INSTRUMENTS

### a) Categories

The carrying amounts and fair values of financial instruments are allocated below to IAS 39, *Financial Instruments: Recognition and Measurement*, categories:

As of September 30, 2013	Available for sale		Loans and receivables		Other liabilities		Held for trading
	Fair value	Carrying amount	Fair value	Carrying amount	Fair value	Carrying amount	Carrying amount
(\$ thousands)							
<b>ASSETS</b>							
Cash (iii)			\$5,214	\$5,214			
Accounts receivable (iii)			\$1,493	\$1,493			
Legal finance receivables (i)(iv)	\$4,967	\$4,967	(i)	\$4,101			
<b>LIABILITIES</b>							
Accounts payable (iii)					\$7,688	\$7,688	
Vehicle financing (ii)					\$5,969	\$5,969	
Interest rate swaps (iv)							\$1,531
Borrowings (ii)					\$71,667	\$71,667	
Customer security deposits					\$11,622	\$11,622	
As at December 31, 2012	Available for sale		Loans and receivables		Other liabilities		Held for trading
	Fair value	Carrying amount	Fair value	Carrying amount	Fair value	Carrying amount	Carrying amount
(\$ thousands)							
<b>ASSETS</b>							
Cash (iii)			\$5,591	\$5,591			
Accounts receivable (iii)			\$771	\$771			
Legal finance receivables (i)(iv)	\$3,349	\$3,349	(i)	\$2,295			
<b>LIABILITIES</b>							
Accounts payable (iii)					\$8,260	\$8,260	
Vehicle financing (ii)					\$6,199	\$6,199	
Interest rate swaps (iv)							\$2,489
Borrowings (ii)					\$47,577	\$47,577	
Customer security deposits					\$10,994	\$10,994	

- (i) There is no organized market for valuing the legal finance receivables. The carrying value is the amortized cost using the effective interest rate method.
- (ii) The stated value of the vehicle financing and borrowings approximates fair values, as the interest rates attached to these instruments are representative of current market rates, for loans with similar terms, conditions and maturities.
- (iii) Carrying amounts are expected to be reasonable approximations of fair value for cash and for financial instruments with short maturities, including accounts receivable and accounts payable.
- (iv) Plaintiff advances and interest rate swaps are carried at fair value.

**b) Measurement hierarchy**

All financial instruments measured at fair value need to be categorized into one of three hierarchy levels, described below, for disclosure purposes. Each level is based on the transparency of the inputs used to measure the fair values of assets and liabilities:

- (i) Level 1 Inputs – quoted prices (unadjusted) in active markets for identical assets or liabilities that the reporting entity has the ability to access at the measurement date;
- (ii) Level 2 Inputs – inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e., as prices) or indirectly (i.e., derived from prices); and
- (iii) Level 3 Inputs – techniques which use inputs which have a significant effect on the recorded fair value for the asset or liability that are not based on observable market data (unobservable inputs).

The Company had no Level 1 financial instruments during the current or prior periods.

The fair values of financial instruments are classified using the IFRS 7, Financial Instruments: Disclosures, measurement hierarchy as follows:

	<b>September 30, 2013</b>		<b>December 31, 2012</b>	
	<b>Level 2</b>	<b>Level 3</b>	<b>Level 2</b>	<b>Level 3</b>
	<i>(\$ thousands)</i>			
<b>ASSETS</b>				
<i>Available for sale</i>				
Plaintiff advances	\$ —	\$ 4,967	\$ —	\$ 3,349
<b>LIABILITIES</b>				
<i>Held for trading</i>				
Interest rate swaps	1,531	—	2,489	—
<b>Total</b>	<b>\$ 1,531</b>	<b>\$ 4,967</b>	<b>\$ 2,489</b>	<b>\$ 3,349</b>

**c) Reconciliation of Level 3 Financial Instruments**

The following table sets forth a summary of changes in the carrying value of plaintiff advances:

Plaintiff Advances	<b>Three months ended September 30,</b>		<b>Nine months ended September 30,</b>	
	<b>2013</b>	<b>2012</b>	<b>2013</b>	<b>2012</b>
	<i>(\$ thousands)</i>			
Balance, beginning of period	\$ 4,579	\$ 1,546	\$ 3,349	\$ 915
Originations	650	844	2,099	1,600
Fair value accretion (i)	392	182	1,256	414
Fair value losses	(11)	(5)	(11)	(36)
Collections	(540)	(202)	(1,860)	(538)
Foreign exchange impact (ii)	(103)	(72)	134	(62)
Balance, end of period	<b>\$ 4,967</b>	<b>\$ 2,293</b>	<b>\$ 4,967</b>	<b>\$ 2,293</b>

- (i) Management considered that the change in fair value for plaintiff advances, which are carried at fair value, related to the amortization of interest or successful settlement of advances during the period. The fair value

accretion on plaintiff advances is included in interest revenue on finance leases and loans on statement of income.

- (ii) Difference between year-end foreign exchange rate and average exchange rate; amount included in other comprehensive income.

Fair value measurements are based on level 3 inputs of the three-level hierarchy system which indicates inputs for the assets that are not based on observable market data (unobservable inputs). Plaintiff advances are initially recorded at their fair value, equivalent to the funds advanced. Subsequent measurement of plaintiff advances will be at fair value utilizing a fair value model developed by the Company.

The principal assumptions used in the fair value model are as follows:

- Estimated duration of each plaintiff advance;
- Best estimate of anticipated outcome;
- Monthly fee per advance contract on nominal value of each plaintiff advance; and
- Market interest rate at which estimated cash flows are discounted.

The fair value of plaintiff advances is reviewed quarterly on an individual case basis. Events that may trigger changes to the fair value of each plaintiff advance include the following:

- Successful judgment of a claim in which the Company has a plaintiff advance;
- Unsuccessful judgment of a claim in which the Company has a plaintiff advance;
- Outstanding appeals against both successful and unsuccessful judgments;
- Receipt of funds to settle plaintiff advances;
- A case is dismissed with prejudice (meaning, it can never be re-filed anywhere);
- Change in monthly fee assessed on plaintiff advances; and
- Market interest rate at which estimated cash flows are discounted.

Inherent to the underwriting process is the approval for funding of cases that have a high probability of success, to be achieved either in pre-trial settlement or as a result of a judgment by a court. As of September 30, 2013, the average size of a plaintiff advance is U.S.\$10,610 (December 31, 2012 – U.S.\$8,221). The fair value estimate is inherently subjective being based largely on an estimate of the duration of plaintiff advance and its potential settlement. In the Company's opinion there is no useful alternative valuation that would better quantify the market risk inherent in the portfolio and there are no inputs or variables to which the value of the plaintiff advances are correlated.

d) ***Gains and losses on financial instruments***

The following table shows the net gains and losses arising for each IAS 39 category of financial instrument.

	<b>For the three months ended September 30,</b>		<b>For the nine months ended September 30,</b>	
	<b>2013</b>	<b>2012</b>	<b>2013</b>	<b>2012</b>
	<i>(\$ thousands)</i>			
Loans and receivables				
Provision for credit losses	\$ 1,908	\$ 1,422	\$ 4,839	\$ 3,670
Held for trading gains and (losses) on:				
Interest rate swaps	47	(169)	1,037	(211)
Net loss	<u>\$ 1,861</u>	<u>\$ 1,591</u>	<u>\$ 3,802</u>	<u>\$ 3,881</u>

e) **Financial Risk Management**

In the normal course of business, the Company manages risks that arise as a result of its use of financial instruments. These risks include credit, liquidity and market risk. Market risks can include interest rate risk, foreign currency risk and other price risk.

There have been no changes in the Company's objectives, policies or processes for managing or for measuring any of the risks to which it is exposed since the previous year end.

**18. CAPITAL MANAGEMENT**

The Company's capital is comprised of shareholders' equity which at September 30, 2013 comprised \$66.7 million (December 31, 2012 - \$60.6 million). The Company's objectives when managing capital are to safeguard the Company's ability to continue as a going concern in the long-term and to provide adequate returns for shareholders.

The Company manages the capital structure and makes adjustments in light of changes in economic conditions and the risk profile of the underlying assets. The Company uses various measures including the amount of dividends paid to shareholders.

There have been no changes in the Company's objectives, policies or processes for managing capital during the period.

**19. RELATED PARTY TRANSACTIONS**

The Company has no parent or other ultimate controlling party.

The Company had the following transactions and balances with related parties:

- (a) Pawnee, a U.S. subsidiary of the Company, leases a 10,800 square foot office facility from an entity that is controlled by the holders of the Class B and Class C shares of U.S. Acquisition Co Ltd, a non-operating subsidiary of the Company. Minimum lease payments are U.S.\$212,890 per annum, triple net. The lease expires on April 30, 2016, and contains an option to renew for an additional five year term. The expense is included in other expenses and is translated at the average exchange rate for the period. At September 30, 2013 and December 31, 2012 there was no amount payable in respect of the lease.
- (b) Case Funding provides Quick Cash Inc. ("Quick Cash"), an entity controlled by a director and the CEO of Case Funding Inc., with personnel and facilities to manage the portfolio of existing loans managed by Quick Cash and required origination and placement services in respect of future loans (Quick Cash is prohibited from making loans, other than those which Case Funding does not wish to make and Quick Cash is responsible for all out-of-pocket third party fees and expenses relating to its business). Payments received and commitments for services to be provided are as follows

Months	Amount
June – December 2011	Nil
January – June 2012	\$16,000/month
July 2012 – June 2013	\$4,000/month
July 2013 – June 2014	\$1,000/month

This revenue is recorded in Ancillary finance and other fee income. The amounts were determined at the time of Case Funding's acquisition and reflect negotiated market terms and the expected level of administrative services that will be provided to Quick Cash over the term of the agreement.

(c) **Compensation of key management**

The Company's key management consists of the President and Chief Executive Officer, Chief Financial Officer and the board of directors. Key management compensation is as follows:

	<b>Three months ended September 30,</b>		<b>Nine months ended September 30,</b>	
	<b>2013</b>	<b>2012</b>	<b>2013</b>	<b>2012</b>
	<i>(\$ thousands)</i>			
Salaries, fees and other short-term employee benefits	\$ <b>297</b>	\$ 343	\$ <b>837</b>	\$ 798
Share-based compensation	<b>227</b>	186	<b>676</b>	549
Compensation expense of key management	<u>\$ <b>524</b></u>	<u>\$ 529</u>	<u>\$ <b>1,513</b></u>	<u>\$ 1,347</u>

## 20. SEASONAL OPERATIONS

Based on past experience, the Company's automotive business follows a seasonal pattern, with revenue and net income being significantly lower in the first quarter than in other quarterly periods.

Tax expense reflects the mix of taxing jurisdictions in which pre-tax income and losses were recognized. However, because the geographical mix of pre-tax income and losses in interim periods may not be reflective of full year results, this may distort the Company's interim period effective tax rate.

## 21. SEGMENT INFORMATION

Segments are identified on the same basis that is used internally to manage and to report on performance, taking into account the products and services of each segment and the organizational structure of the Company. The Company's operations consist of three reportable segments: Equipment Leasing, Legal Financing, and Automotive Operations.

Chesswood's Equipment Leasing segment is located in the United States and is involved in small-ticket equipment leasing to small businesses in the start-up and "B" credit markets in the lower 48 states. Our Automotive Operations segment sells and services predominantly Acura automobiles and leases Acura and other brand automobiles in the province of Ontario, Canada. Our Legal Financing segment is located in the United States and is a provider of legal financing to plaintiffs and attorneys throughout the United States. At September 30, 2013, the operations of Windset had minimal impact to Chesswood financial statements and are grouped in the Equipment leasing - U.S. column. For the three and nine months ended September 30, 2013, Windset had \$89,100 in start-up expenses.

Segment information is prepared in conformity with the accounting policies adopted for the Company's financial statements.

The role of the "chief operating decision maker" with respect to resource allocation and performance assessment is embodied in the position of Chief Executive Officer. The performance of the Equipment Leasing, Legal Financing, and Automotive Operations segments is measured on the basis of net income or loss before tax. Net assets, which are defined as total segment assets less total segment liabilities, are used as the basis of assessing the allocation of resources.

When compared with the last annual financial statements, there are no differences in the basis of segmentation or in the basis of measuring segment results.

Selected information by segment and geographically is as follows:

Nine months ended September 30, 2013					
(\$ thousands)					
	Equipment Financing – U.S.	Legal Financing – U.S.	Automotive operations - Canada	Corporate overhead - Canada	Total
Interest revenue on leases and loans (a)	\$ 25,340	\$ 2,085	\$ —	\$ —	\$ 27,425
Ancillary finance and other fee income	4,084	147	—	—	4,231
Interest expense (a)	(2,927)	—	—	—	(2,927)
Provision for credit losses	(4,828)	(11)	—	—	(4,839)
<b>Finance margin</b>	<b>21,669</b>	<b>2,221</b>	<b>—</b>	<b>—</b>	<b>23,890</b>
Revenue - automotive operations	—	—	37,411	—	37,411
Cost of sales – automotive operations	—	—	(32,417)	—	(32,417)
<b>Gross margin before expenses</b>	<b>21,669</b>	<b>2,221</b>	<b>4,994</b>	<b>—</b>	<b>28,884</b>
Personnel expenses	3,080	1,015	2,229	809	7,133
Share-based compensation expense	188	147	60	675	1,070
Other expenses	2,725	485	1,494	665	5,369
Amortization	243	2	53	3	301
<b>Income before undernoted items</b>	<b>15,433</b>	<b>572</b>	<b>1,158</b>	<b>(2,152)</b>	<b>15,011</b>
Unrealized gain on interest rate swaps	1,037	—	—	—	1,037
Unrealized gain on foreign exchange	—	—	—	16	16
<b>Income before taxes</b>	<b>16,470</b>	<b>572</b>	<b>1,158</b>	<b>(2,136)</b>	<b>16,064</b>
Provision for (recovery of) taxes	6,469	—	(63)	463	6,869
<b>Net income</b>	<b>\$ 10,001</b>	<b>\$ 572</b>	<b>\$ 1,221</b>	<b>\$ (2,599)</b>	<b>\$ 9,195</b>

Net cash from (used in) operating activities	\$ 9,195	\$ (2,528)	\$ 1,353	\$ (2,231)	\$ 5,789
Net cash used in investing activities	\$ (240)	\$ (43)	\$ (184)	\$ —	\$ (467)
Net cash used in financing activities	\$ —	\$ —	\$ —	\$ (5,751)	\$ (5,751)

Total Assets	\$ 159,245	\$ 10,682	\$ 12,777	\$ 5,041	\$ 187,745
Total Liabilities	\$ 112,811	\$ 245	\$ 6,787	\$ 1,167	\$ 121,010
Finance receivables	\$ 141,547	\$ 9,068	\$ —	\$ —	\$ 150,615
Goodwill	\$ 11,062	\$ 671	\$ 2,520	\$ —	\$ 14,253
Intangible assets	\$ 5,553	\$ 381	\$ 889	\$ —	\$ 6,823
Property and equipment expenditures	\$ 240	\$ 43	\$ 184	\$ —	\$ 467

(a) includes \$470,600 in non-cash interest expense, based on the imputed interest savings on the customer security deposits, interest revenue on leases on loans is higher by the same amount.

Nine months ended September 30, 2012					
(\$ thousands)					
	Equipment Financing – U.S.	Legal Financing – U.S.	Automotive operations - Canada	Corporate overhead - Canada	Total
Interest revenue on leases and loans (a) \$	22,060	\$ 897	\$ 115	\$ —	\$ 23,072
Ancillary finance and other fee income	3,400	187	—	—	3,587
Interest expense (a)	(2,552)	—	(15)	—	(2,567)
Provision for credit losses	(3,637)	(36)	3	—	(3,670)
Finance margin	19,271	1,048	103	—	20,422
Revenue - automotive operations	—	—	37,131	—	37,131
Cost of sales – automotive operations	—	—	(32,675)	—	(32,675)
Gross margin before expenses	19,271	1,048	4,559	—	24,878
Personnel expenses	2,862	775	2,096	751	6,484
Share-based compensation expense	251	212	78	549	1,090
Other expenses	2,376	372	1,747	486	4,981
Amortization	437	3	75	4	519
Income before undernoted items	13,345	(314)	563	(1,790)	11,804
Contingent consideration and bonus	—	(138)	—	—	(138)
Unrealized loss on interest rate swaps	(211)	—	—	—	(211)
Unrealized loss on foreign exchange	—	—	—	(151)	(151)
Income before taxes	13,134	(452)	563	(1,941)	11,304
Provision for (recovery of) taxes	5,242	—	(105)	401	5,538
Net income	\$ 7,892	\$ (452)	\$ 668	\$ (2,342)	\$ 5,766
Net cash from (used in) operating activities	\$ 7,054	\$ (2,161)	\$ 2,036	\$ (1,900)	\$ 5,029
Net cash used in investing activities	\$ (120)	\$ (39)	\$ (31)	\$ —	\$ (190)
Net cash used in financing activities	\$ —	\$ —	\$ —	\$ (5,627)	\$ (5,627)
Total Assets	\$ 128,693	\$ 5,441	\$ 13,594	\$ 6,014	\$ 153,742
Total Liabilities	\$ 85,680	\$ 1,001	\$ 7,363	\$ 1,185	\$ 95,229
Finance receivables	\$ 111,275	\$ 3,697	\$ —	\$ —	\$ 114,972
Goodwill	\$ 10,580	\$ 642	\$ 2,520	\$ —	\$ 13,742
Intangible assets	\$ 5,599	\$ 364	\$ 889	\$ —	\$ 6,852
Property and equipment expenditures	\$ 120	\$ 39	\$ 31	\$ —	\$ 190

(a) includes \$508,000 in non-cash interest expense, based on the imputed interest savings on the customer security deposits, interest revenue on leases on loans is higher by the same amount.



<b>Three months ended September 30, 2013</b>					
(\$ thousands)					
	<b>Equipment Financing – U.S.</b>	<b>Legal Financing – U.S.</b>	<b>Automotive operations -Canada</b>	<b>Corporate overhead - Canada</b>	<b>Total</b>
Interest revenue on leases and loans (a) \$	8,856	\$ 650	\$ —	\$ —	\$ 9,506
Ancillary finance and other fee income	1,318	39	—	—	1,357
Interest expense (a)	(1,043)	—	—	—	(1,043)
Provision for credit losses	(1,897)	(11)	—	—	(1,908)
<b>Finance margin</b>	<b>7,234</b>	<b>678</b>	<b>—</b>	<b>—</b>	<b>7,912</b>
Revenue - automotive operations	—	—	14,072	—	14,072
Cost of sales – automotive operations	—	—	(12,218)	—	(12,218)
<b>Gross margin before expenses</b>	<b>7,234</b>	<b>678</b>	<b>1,854</b>	<b>—</b>	<b>9,766</b>
Personnel expenses	1,046	364	811	270	2,491
Share-based compensation expense	36	16	11	227	290
Other expenses	1,010	163	521	251	1,945
Amortization	26	1	19	1	47
<b>Income before undernoted items</b>	<b>5,116</b>	<b>134</b>	<b>492</b>	<b>(749)</b>	<b>4,993</b>
Unrealized gain on interest rate swaps	47	—	—	—	47
Unrealized loss on foreign exchange	—	—	—	(22)	(22)
<b>Income before taxes</b>	<b>5,163</b>	<b>134</b>	<b>492</b>	<b>(771)</b>	<b>5,018</b>
Provision for (recovery of) taxes	1,997	—	—	149	2,146
<b>Net income</b>	<b>\$ 3,166</b>	<b>\$ 134</b>	<b>\$ 492</b>	<b>\$ (920)</b>	<b>\$2,872</b>
Net cash from (used in) operating activities	\$ 435	\$ (858)	\$ 461	\$ (385)	\$ (347)
Net cash used in investing activities	\$ (50)	\$ (13)	\$ (74)	\$ —	\$ (137)
Net cash used in financing activities	\$ —	\$ —	\$ —	\$ (1,885)	\$ (1,885)
Property and equipment expenditures	\$ 50	\$ 13	\$ 74	\$ —	\$ 137
(a) includes \$148,600 in non-cash interest expense, based on the imputed interest savings on the customer security deposits, interest revenue on leases on loans is higher by the same amount.					

Three months ended September 30, 2012					
(\$ thousands)					
	Equipment Financing – U.S.	Legal Financing – U.S.	Automotive operations - Canada	Corporate overhead - Canada	Total
Interest revenue on leases and loans (a) \$	7,420	\$ 333	\$ 13	\$ —	\$ 7,766
Ancillary finance and other fee income	1,145	48	—	—	1,193
Interest expense (a)	(859)	—	—	—	(859)
Provision for credit losses	(1,419)	(5)	2	—	(1,422)
Finance margin	6,287	376	15	—	6,678
Revenue - automotive operations	—	—	12,515	—	12,515
Cost of sales – automotive operations	—	—	(10,965)	—	(10,965)
Gross margin before expenses	6,287	376	1,565	—	8,228
Personnel expenses	981	250	714	322	2,267
Share-based compensation expense	91	39	18	186	334
Other expenses	767	158	608	140	1,673
Amortization	146	3	13	2	164
Income before undernoted items	4,302	(74)	212	(650)	3,790
Contingent consideration and bonus	—	(48)	—	—	(48)
Unrealized loss on interest rate swaps	(169)	—	—	—	(169)
Unrealized loss on foreign exchange	—	—	—	(338)	(338)
Income before taxes	4,133	(122)	212	(988)	3,235
Provision for (recovery of) taxes	1,607	—	(75)	145	1,677
Net income	\$ 2,526	\$ (122)	\$ 287	\$ (1,133)	\$ 1,558
Net cash from (used in) operating activities	\$ (1,877)	\$ (247)	\$ 1,379	\$ (241)	\$ (986)
Net cash used in investing activities	\$ (92)	\$ (19)	\$ —	\$ —	\$ (111)
Net cash used in financing activities	\$ —	\$ —	\$ —	\$ (1,783)	\$ (1,783)
Property and equipment expenditures	\$ 92	\$ 19	\$ —	\$ —	\$ 111

(a) includes \$169,000 in non-cash interest expense, based on the imputed interest savings on the customer security deposits, interest revenue on leases on loans is higher by the same amount.

**Directors and Officers**

**Frederick W. Steiner**

Director  
Chairman of Chesswood Group Limited  
Chairman, Audit and Governance Committee  
*C.E.O., Imperial Coffee and Services Inc.*

**Clare Copeland**

Director  
Chairman, Compensation Committee  
*C.E.O., Falls Management Company*  
*Chairman, Toronto Hydro Corporation*

**Jeffrey Wortsman**

Director  
*President & C.E.O., Danier Leather Inc.*

**Barry Shafran**

Director  
*President & C.E.O., Chesswood Group Limited*  
*Chairman and C.E.O., Pawnee Leasing Corporation*

**David Obront**

Director  
*President, Carpool Two Ltd.*

**Robert Day**

Director  
*Former Chairman, Pawnee Leasing Corporation*

**Samuel Leeper**

Director  
*Former C.E.O., Pawnee Leasing Corporation*

**Executive Team**

Barry Shafran  
*President & C.E.O.*  
*Chesswood Group Limited*  
*Chairman and C.E.O.*  
*Pawnee Leasing Corporation*

**Lisa Stevenson**

*Director of Finance*  
*Chief Financial Officer*

**Other Information**

**Auditors**

*BDO Canada LLP*

**Transfer Agent**

*Equity Financial Trust Company*

**Corporate Counsel**

*McCarthy Tetrault LLP*

**Website**

*[www.chesswoodgroup.com](http://www.chesswoodgroup.com)*

**Toronto Stock Exchange Symbol**

*CHW*



**TSX: CHW**

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