# 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, 2019. 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.

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

| | Note | September 30, 2019 (unaudited) | December 31, 2018 (audited) |
|---|---|---|---|
| **ASSETS** | | | |
| Cash | | **$ 7,691** | $ 2,326 |
| Restricted funds | *10(d)* | **11,846** | 13,598 |
| Assets held for sale | *5* | **1,243** | 1,852 |
| Other assets | *6* | **6,245** | 8,786 |
| Finance receivables | *7* | **783,365** | 728,924 |
| Deferred tax assets | | **273** | 375 |
| Interest rate derivatives | | **—** | 896 |
| Right-to-use assets | *8* | **3,240** | — |
| Property and equipment | | **1,548** | 1,628 |
| Intangible assets | | **17,551** | 18,765 |
| Goodwill | | **40,608** | 41,037 |
| **TOTAL ASSETS** | | **$ 873,610** | $ 818,187 |
| **LIABILITIES** | | | |
| Accounts payable and other liabilities | *9* | **$ 14,426** | $ 15,600 |
| Premises leases payable | *8* | **3,399** | — |
| Borrowings | *10* | **663,353** | 601,525 |
| Customer security deposits | | **13,185** | 16,773 |
| Interest rate derivatives | | **337** | — |
| Deferred tax liabilities | | **19,652** | 20,794 |
| | | **714,352** | 654,692 |
| **SHAREHOLDERS' EQUITY** | | | |
| Common shares | *14* | **103,963** | 103,576 |
| Non-controlling interest | | **13,360** | 13,713 |
| Share-based compensation reserve | *15* | **5,322** | 5,414 |
| Accumulated other comprehensive income | | **15,597** | 18,350 |
| Retained earnings | | **21,016** | 22,442 |
| | | **159,258** | 163,495 |
| **TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY** | | **$ 873,610** | $ 818,187 |

*Please see notes to the condensed interim consolidated financial statements.*

**CHESSWOOD GROUP LIMITED**
**CONDENSED INTERIM CONSOLIDATED STATEMENTS OF INCOME**
**FOR THE THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2019 AND 2018**
***(in thousands of dollars, except per share amounts, unaudited)***

| | Note | Three months ended September 30, 2019 | Three months ended September 30, 2018 | Nine months ended September 30, 2019 | Nine months ended September 30, 2018 |
|---|---|---|---|---|---|
| **Finance revenue** | | | | | |
| Interest revenue on finance leases and loans | | **$ 27,708** | $ 25,622 | **$ 82,055** | $ 71,620 |
| Ancillary finance and other fee income | | **4,073** | 3,276 | **12,069** | 9,475 |
| | | **31,781** | 28,898 | **94,124** | 81,095 |
| **Finance expenses** | | | | | |
| Interest expense | | **8,676** | 7,213 | **25,469** | 18,681 |
| Provision for credit losses | *7* | **7,868** | 4,111 | **21,463** | 13,695 |
| | | **16,544** | 11,324 | **46,932** | 32,376 |
| **Finance margin** | | **15,237** | 17,574 | **47,192** | 48,719 |
| **Expenses** | | | | | |
| Personnel expenses | | **5,255** | 4,410 | **15,331** | 12,548 |
| Other expenses | | **4,593** | 3,624 | **13,525** | 10,010 |
| Depreciation - property and equipment | | **299** | 125 | **886** | 361 |
| Amortization - intangible assets | | **333** | 333 | **999** | 1,179 |
| | | **10,480** | 8,492 | **30,741** | 24,098 |
| **Operating income** | | **4,757** | 9,082 | **16,451** | 24,621 |
| Unrealized gain (loss) on investments held | | **(61)** | — | **30** | (151) |
| Financing costs - convertible debentures | | **—** | — | **—** | 29 |
| Unrealized gain (loss) on interest rate derivatives | | **(82)** | 256 | **(1,211)** | 1,575 |
| Unrealized loss on foreign exchange | | **(75)** | (58) | **(220)** | (146) |
| **Income before taxes** | | **4,539** | 9,280 | **15,050** | 25,928 |
| Tax expense | | **(1,521)** | (3,007) | **(4,787)** | (8,108) |
| **Income from continuing operations** | | **3,018** | 6,273 | **10,263** | 17,820 |
| **Loss from discontinued operations** | *5* | **(41)** | (181) | **(321)** | (212) |
| **Net income** | | **$ 2,977** | $ 6,092 | **$ 9,942** | $ 17,608 |
| **Attributable to:** | | | | | |
| Common shareholders | | **$ 2,728** | $ 5,589 | **$ 9,112** | $ 16,158 |
| Non-controlling interest | | **$ 249** | $ 503 | **$ 830** | $ 1,450 |
| **Income from continuing operations per share:** | | | | | |
| Basic | *17* | **$ 0.17** | $ 0.35 | **$ 0.58** | $ 0.99 |
| Diluted | *17* | **$ 0.16** | $ 0.34 | **$ 0.57** | $ 0.97 |

*Please see notes to the condensed interim consolidated financial statements.*

**CHESSWOOD GROUP LIMITED**
**CONDENSED INTERIM CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME**
**FOR THE THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2019 AND 2018**
***(in thousands of dollars, unaudited)***

| | Three months ended September 30, | | Nine months ended September 30, | |
|---|---|---|---|---|
| | **2019** | 2018 | **2019** | 2018 |
| Net income | **$ 2,977** | $ 6,092 | **$ 9,942** | $ 17,608 |
| Other comprehensive income: | | | | |
| Unrealized gain (loss) on translation of foreign operations | **999** | (1,585) | **(3,004)** | 3,113 |
| Comprehensive income | **$ 3,976** | $ 4,507 | **$ 6,938** | $ 20,721 |
| **Attributable to:** | | | | |
| Common shareholders | **$ 3,644** | $ 4,134 | **$ 6,359** | $ 19,014 |
| Non-controlling interest | **$ 332** | $ 373 | **$ 579** | $ 1,707 |

*Please see notes to the condensed interim consolidated financial statements.*

**CHESSWOOD GROUP LIMITED**
**CONDENSED INTERIM CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY**
**FOR THE THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2019 AND 2018**
***(in thousands of dollars, unaudited)***

| | Note | Common shares | Common shares | Non-controlling interest | Share-based compensation reserve | Accumulated other comprehensive income | Retained earnings | 2019 Total |
|---|---|---|---|---|---|---|---|---|
| | | (# '000s) | | | | | | |
| **Shareholders' equity - December 31, 2018** | | **16,229** | **$ 103,576** | **$ 13,713** | **$ 5,414** | **$ 18,350** | **$ 22,442** | **$ 163,495** |
| Net income | | **—** | **—** | **830** | **—** | **—** | **9,112** | **9,942** |
| Dividends declared | 16 | **—** | **—** | **(932)** | **—** | **—** | **(10,228)** | **(11,160)** |
| Share-based compensation | 15 | **—** | **—** | **—** | **508** | **—** | **—** | **508** |
| Exercise of restricted share units | 15 | **44** | **482** | **—** | **(482)** | **—** | **—** | **—** |
| Exercise of options | 15 | **53** | **403** | **—** | **(118)** | **—** | **—** | **285** |
| Repurchase of common shares under issuer bid | 14 | **(78)** | **(498)** | **—** | **—** | **—** | **(310)** | **(808)** |
| Unrealized loss on translation of foreign operations | | | **—** | **(251)** | **—** | **(2,753)** | **—** | **(3,004)** |
| **Shareholders' equity - Sep 30, 2019** | | **16,248** | **$ 103,963** | **$ 13,360** | **$ 5,322** | **$ 15,597** | **$ 21,016** | **$ 159,258** |

| | Note | Common shares | Common shares | Non-controlling interest | Share-based compensation reserve | Accumulated other comprehensive income | Retained earnings | 2018 Total |
|---|---|---|---|---|---|---|---|---|
| | | (# '000s) | | | | | | |
| Shareholders' equity - December 31, 2017 | | 16,575 | $ 105,208 | $ 13,230 | $ 5,295 | $ 10,776 | $ 26,712 | $ 161,221 |
| Impact of adopting IFRS 9 | | — | — | (602) | — | — | (6,753) | (7,355) |
| Net income | | — | — | 1,450 | — | — | 16,158 | 17,608 |
| Dividends declared | 16 | — | — | (931) | — | — | (10,375) | (11,306) |
| Share-based compensation | 15 | — | — | — | 859 | — | — | 859 |
| Exercise of restricted share units | 15 | 70 | 806 | — | (806) | — | — | — |
| Exercise of options | 15 | 83 | 741 | — | (169) | — | — | 572 |
| Repurchase of common shares under issuer bid | 14 | (293) | (1,863) | — | — | — | (1,223) | (3,086) |
| Unrealized gain on translation of foreign operations | | | — | 256 | — | 2,857 | — | 3,113 |
| Shareholders' equity - Sep 30, 2018 | | 16,435 | 104,892 | 13,403 | 5,179 | 13,633 | 24,519 | 161,626 |
| Impact of adopting IFRS 9 & 15 | | — | — | (243) | — | — | (2,691) | (2,934) |
| Net income | | — | — | 439 | — | — | 4,838 | 5,277 |
| Dividends declared | | — | — | (311) | — | — | (3,427) | (3,738) |
| Share-based compensation | | — | — | — | 235 | — | — | 235 |
| Repurchase of common shares under issuer bid | 14 | (206) | (1,316) | — | — | — | (797) | (2,113) |
| Unrealized gain on translation of foreign operations | | | — | 425 | — | 4,717 | — | 5,142 |
| Shareholders' equity - December 31, 2018 | | 16,229 | $ 103,576 | $ 13,713 | $ 5,414 | $ 18,350 | $ 22,442 | $ 163,495 |

*Please see notes to the condensed interim consolidated financial statements.*

**CHESSWOOD GROUP LIMITED**
**CONDENSED INTERIM CONSOLIDATED STATEMENTS OF CASH FLOWS**
**FOR THE THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2019 AND 2018**

| *(in thousands of dollars, unaudited)* | Note | Three months ended September 30, 2019 | Three months ended September 30, 2018 | Nine months ended September 30, 2019 | Nine months ended September 30, 2018 |
|---|---|---|---|---|---|
| **OPERATING ACTIVITIES** | | | | | |
| Income from continuing operations | | **$ 3,018** | $ 6,273 | **$ 10,263** | $ 17,820 |
| Non-cash items included in net income | | | | | |
| Amortization and depreciation | | **632** | 458 | **1,885** | 1,540 |
| Provision for credit losses *(excluding recoveries)* | 7 | **10,644** | 6,385 | **29,648** | 20,460 |
| Amortization of origination costs | | **6,747** | 6,069 | **19,864** | 16,953 |
| Tax expense | | **1,521** | 3,007 | **4,787** | 8,108 |
| Other non-cash items | 19 | **1,340** | 800 | **4,522** | 1,517 |
| | | **20,884** | 16,719 | **60,706** | 48,578 |
| Cash from operating activities before change in net operating assets | | **23,902** | 22,992 | **70,969** | 66,398 |
| Funds advanced on origination of finance receivables | | **(99,813)** | (98,788) | **(306,209)** | (306,163) |
| Origination costs paid on finance receivables | | **(7,948)** | (8,435) | **(25,250)** | (26,268) |
| Principal collections of finance receivables | | **72,678** | 61,522 | **210,863** | 169,548 |
| Change in other net operating assets | 19 | **7,364** | 4,845 | **(258)** | 2,897 |
| Cash used in operating activities before undernoted | | **(3,817)** | (17,864) | **(49,885)** | (93,588) |
| Interest paid on convertible debentures | | **—** | — | **—** | (61) |
| Income taxes paid - net | | **(1,441)** | 3,529 | **(5,460)** | (2,260) |
| Cash used in operating activities - continuing operations | | **(5,258)** | (14,335) | **(55,345)** | (95,909) |
| Cash from operating activities - discontinued operations | 5 | **138** | 352 | **230** | 1,197 |
| **Cash used in operating activities** | | **(5,120)** | (13,983) | **(55,115)** | (94,712) |
| **INVESTING ACTIVITIES** | | | | | |
| Purchase of property and equipment | | **(28)** | (56) | **(312)** | (162) |
| **Cash used in investing activities** | | **(28)** | (56) | **(312)** | (162) |
| **FINANCING ACTIVITIES** | | | | | |
| Borrowings, net | 10 | **12,507** | 22,601 | **75,972** | 133,095 |
| Payment of financing costs | 10 | **(2,213)** | (2,338) | **(2,969)** | (3,518) |
| Payment of lease obligations | 8 | **(168)** | — | **(471)** | — |
| Redemption of convertible debentures | | **—** | — | **—** | (20,000) |
| Proceeds from exercise of options | 15 | **34** | 274 | **285** | 571 |
| Repurchase of common shares under issuer bid | 14 | **(152)** | — | **(808)** | (3,086) |
| Cash dividends paid | 16 | **(3,724)** | (3,757) | **(11,159)** | (11,316) |
| **Cash from financing activities** | | **6,284** | 16,780 | **60,850** | 95,746 |
| Unrealized foreign exchange gain (loss) on cash | | **61** | 2 | **(58)** | 77 |
| Net increase (decrease) in cash | | **1,197** | 2,743 | **5,365** | 949 |
| Cash, beginning of period | | **6,494** | 1,846 | **2,326** | 3,640 |
| **Cash, end of period** | | **$ 7,691** | $ 4,589 | **$ 7,691** | $ 4,589 |

*Please see notes to the condensed interim consolidated financial statements.*

## TABLE OF NOTES



## 1. NATURE OF BUSINESS AND BASIS OF PREPARATION

Chesswood Group Limited (the “Company” or "Chesswood") is incorporated under the laws of the Province of Ontario. The Company’s head office is located at 156 Duncan Mill Road, Unit 16, Toronto, Ontario, M3B 3N2, and its shares trade on the Toronto Stock Exchange under the symbol CHW.

The Company holds a 100% interest in Chesswood Holdings Ltd. Chesswood Holdings Ltd. owns 100% of the shares of the operating companies: Blue Chip Leasing Corporation ("Blue Chip") incorporated in Ontario, Lease-Win Limited, Case Funding Inc. ("Case Funding"), 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 each of the operating subsidiaries Pawnee Leasing Corporation (“Pawnee”), incorporated in Colorado, United States, Tandem Finance Inc. ("Tandem"), incorporated in Colorado, United States and Windset Capital Corporation ("Windset"), incorporated in Delaware, United States. In addition, Pawnee holds, through consolidated, wholly-owned Special Purpose Entities ("SPEs"), a portfolio of leases and loans which are financed through arm's length financial institutions. See Note 7 - *Finance Receivables* and Note 10(b) - *Borrowings*.

Through its subsidiaries, the Company operates in the following businesses:

- Pawnee - micro and small-ticket equipment financing to small and medium-sized businesses in the United States.
- Tandem - small-ticket equipment originations through equipment vendors and distributors in the United States.
- Blue Chip - commercial equipment financing to small and medium-sized businesses in Canada.

Discontinued operations include:

- Case Funding - holds a portfolio of legal finance receivables in the United States.

The consolidated financial statements, including comparatives:

- have been prepared in accordance with 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, 2018, except for the effects of adopting IFRS 16, *Leases*, see Note 2 - *New Accounting Standards*.
- are presented on a consistent basis with prior periods, except for renaming 'income before undernoted items' as 'operating income' and the inclusion of amortization - intangible assets in the calculation of that subtotal. The calculation of this measure has been changed for the current and prior periods to be consistent with the discussion of operating income and adjusted operating income in the Management Discussion & Analysis ("MD&A") for the nine-month period ended September 30, 2019.
- have been prepared on the going concern and historical cost bases, except for derivative financial instruments and hybrid financial liabilities designated as at fair value through net income or loss, which have been measured at fair value.
- 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 IFRS 10, *Consolidated Financial Statements.* All intra-group balances and items of income and expense resulting from intra-group transactions are eliminated in full. Transaction costs in connection with business combinations are expensed as incurred.
- should be read in conjunction with the Company’s most recently issued Annual Report which includes information necessary, or useful, to understanding the Company’s businesses and financial reporting.
- are unaudited (except otherwise noted).
- the results reported in these condensed consolidated interim financial statements should not be regarded as necessarily indicative of results that may be expected for the entire year.

The preparation of condensed interim consolidated financial statements, including the application of accounting policies, requires management to make estimates and assumptions using judgment that affect the reported amounts of assets and liabilities, and income and expenses during the reporting period. Estimates and other judgments are continually evaluated and are based on management's experience and other factors, including expectations about future events that are believed to be reasonable under the circumstances. Actual results may differ from those estimates. Preparation of these condensed interim consolidated financial statements required management to exercise judgment over the likelihood of the extension options included in its premises leases being exercised. The significant estimates and judgments made by management in applying the Company's accounting policies and the key sources of estimation uncertainty were otherwise the same as those that applied to the audited consolidated financial statements for the year ended December 31, 2018.

The reporting currency is the Canadian dollar and the financial statements are presented in thousands of Canadian dollars except per share amounts and as otherwise noted. The functional currency of the Company, Chesswood Holdings Ltd., Blue Chip and Lease-Win Limited is the Canadian dollar. The functional currency of U.S. Acquisitionco, Pawnee, Windset, Tandem, the SPEs, and Case Funding is the United States dollar. Income and expenses of subsidiaries with a different functional currency than the Company’s presentation currency are translated in the Company’s consolidated financial statements at the average U.S. dollar exchange rate for the reporting period (for the nine months ended September 30, 2019 - 1.3292; 2018 - 1.2876), and assets and liabilities are translated at the closing rate (as at September 30, 2019 - 1.3243; December 31, 2018 - 1.3642).

In order to improve clarity, certain items have been combined on the statements of financial position with details provided separately in the Notes to the unaudited condensed consolidated interim financial statements, and certain comparative figures have been reclassified to conform to the presentation adopted in the current year's unaudited condensed consolidated interim financial statements.

The Company’s unaudited condensed consolidated interim financial statements were authorized for issue on November 6, 2019 by the Board of Directors.

## 2. NEW ACCOUNTING STANDARDS

**New accounting standards adopted in 2019**

***IFRS 16 Leases***

The Company adopted IFRS 16, which replaced IAS 17, *Leases*, with effect from January 1, 2019, using the modified retrospective approach, as permitted on transition. Accordingly, the information presented for 2018 has not been restated and remains as previously reported under IAS 17 and related interpretations. The Company's new accounting policy is described in Note 8 - *Right-To-Use Assets and Premises Leases Payable*.

IFRS 16's approach to lessor accounting is substantially unchanged from its predecessor. The Company, as a Lessor, will record property tax income and expense associated with leasing on a gross basis in the consolidated statements of income. The property tax revenue and expense are recorded in the same period as earned and incurred, and the Company recognizes a provision for uncollectible property tax revenue as contra-revenue when a loss is probable and collectability is not reasonably assured.

For lessees, IAS 17 required an entity to identify 'finance' leases, being those leases where in substance the lessee has acquired substantially all the risks and rewards incidental to ownership of the subject asset. For a finance lease, the underlying asset is recognized on the statement of financial position at an amount equal to the fair value of the leased asset, or if lower, the present value of minimum lease payments. Any lease not classified as finance in nature is considered to be an operating lease. The Company's only material leases are for its premises at the Pawnee and Blue Chip locations, which were determined to be operating in nature. Therefore, lease payments were expensed as incurred, straight-line, over the lease term.

IFRS 16 has removed the distinction between finance and operating leases and requires lessees to recognize right-of-use assets and lease liabilities for all leases, subject to certain optional exceptions, on commencement of a lease. Under the new accounting policy, the nature of expenses related to those leases has changed from straight-line operating lease expense to a depreciation charge for the right-to-use assets and interest expense on the lease liabilities.

The Company elected to use the following exemptions on application of the new rules: lease contracts for which the lease ends within 12 months from the date of initial application; lease contracts for which the underlying asset is of low value; and short-term leases that have a lease term of 12 months or less. Leases of certain office equipment are considered of low value and have been excluded. The lease payments associated with these leases are recognized as an expense on a straight-line basis over the lease term.

On initial application, the Company recorded a lease liability of $3.8 million measured as the future lease payments discounted using a weighted average incremental borrowing rate at January 1, 2018 of 4.5%. The Company elected to measure the right-to-use assets at an amount equal to the lease liability. Therefore on adoption there was no net impact on retained earnings.

| | January 1, 2019 |
|---|---|
| | *($ thousands)* |
| Operating lease commitment as at December 31, 2018 as disclosed in Note 17 in 2018 Annual Financial Statements | $ 4,556 |
| Operating lease renewal options reasonably certain to be exercised but not included in operating lease commitments as at December 31, 2018 | 545 |
| Service contracts that do not convey a right-to-use defined asset and low value office equipment leases | (851) |
| Discount, using the incremental borrowing rate as at January 1, 2019 | (591) |
| Foreign exchange (average rate for 2018 vs January 1, 2019 rate) | 178 |
| Lease liabilities recognized as at January 1, 2019 | $ 3,837 |

Ancillary finance and other fee income and other expenses increased by $2.7 million, as certain lessor costs, including property taxes that are paid by the lessee to the lessor are required to be presented gross in the unaudited condensed consolidated interim statements of income, prior year comparatives were not restated. The estimated receivable for property taxes has been reclassified to Finance receivables from Other assets, the prior period balance has not been reclassified.

## 3. FINANCIAL INSTRUMENTS

Financial assets and financial liabilities are recognized when the Company becomes a party to the contractual provisions of the instrument. Financial assets and financial liabilities are recognized initially at fair value plus transaction costs, except for financial assets and financial liabilities carried at fair value through net income or loss, which are measured initially at fair value.

Financial assets are derecognized when the contractual rights to the cash flows from the asset expire or when the asset and substantially all related risks and rewards are transferred. A financial liability is derecognized when it is extinguished, which occurs when it is either discharged, canceled or expires.

**Financial assets**

Financial assets are categorized for subsequent measurement as follows:

*Amortized cost*
Financial assets that are held in a business model with the objective of collecting contractual cash flows where those cash flows represent solely payments of principal and interest ("SPPI") are measured at amortized cost ("AC"). The Company's cash, restricted funds, net investment in leases, and loan receivables are measured at amortized cost. Broker commissions related to the origination of finance leases are deferred and recorded as an adjustment to the yield of the net investment in finance leases as part of the effective interest rate. Gains and losses are recognized in the statement of income when the loans or receivables are derecognized or impaired.

*Financial assets at fair value through net income or loss*
Financial assets that are held for trading and derivative assets are required to be measured at fair value through net income or loss ("FVTP"). Financial assets that meet certain conditions may be designated at fair value through net income or loss upon initial recognition. Upon initial recognition, attributable transaction costs are recognized in net income or loss as incurred.

Assets in this category are subsequently measured at fair value with gains or losses recognized in net income or loss. The fair values of derivative financial instruments are based on changes in observable prices in active markets or by a valuation technique where no market exists.

The Company's investment in Dealnet common shares (included in Other assets on the consolidated statements of financial position) is classified in this category.

*Fair value through other comprehensive income*
Financial assets that are held to both collect contractual cash flows and for sale are required to be measured at fair value through other comprehensive income ("FVOCI"). Other financial assets, provided they are not held for trading and have not been designated as at fair value through net income or loss, can be designated as at fair value through other comprehensive income on initial recognition.

Gains and losses are recognized in other comprehensive income and presented in the available for sale reserve within equity, except for the accretion in value based on the effective interest method, impairment losses and foreign exchange differences on monetary assets, which are recognized in net income or loss. Financial assets measured at fair value through other comprehensive income for which fair value cannot be estimated reliably, are measured at cost and any impairment losses are recognized in net income or loss. Upon initial recognition, attributable transaction costs are recognized in net income or loss as incurred. When the asset is disposed of or is determined to be impaired, the cumulative gain or loss recognized in other comprehensive income is reclassified from equity to net income or loss and presented as a reclassification adjustment within other comprehensive income.

The Company's plaintiff advances are designated as at fair value through other comprehensive income. See Note 5 - *Discontinued Operations*.

**Financial liabilities**

Financial liabilities are categorized as follows for subsequent measurement:

*Amortized cost*
Financial liabilities that are not otherwise measured as at fair value through net income or loss or designated at fair value are measured at amortized cost using the effective interest rate method. Any host contract in a hybrid instrument is also measured at amortized cost. Gains and losses are recognized in net income or loss when the liabilities are derecognized. Transaction costs incurred in connection with the issuance of loans and borrowings are capitalized and recorded as a reduction of the carrying amount of the related financial liabilities and amortized using the effective interest method.

The Company's financial liabilities measured at amortized cost include borrowings, accounts payable, other liabilities and customer security deposits.

*Financial liabilities at fair value through net income or loss*
Financial liabilities that are held for trading and stand-alone derivative liabilities are required to be measured at fair value through net income or loss ("FVTP"). When certain conditions are satisfied, embedded derivatives are required to be separately recognized and measured at fair value with subsequent changes in fair value recognized in net income or loss.

A designation can be made at initial recognition for financial liabilities that include one or more embedded derivatives, provided the host contract is not a financial asset, to measure the entire hybrid instrument at fair value. Where certain criteria are met, for example measurement at amortized cost would create measurement inconsistencies, the financial liability can also be designated at fair value. For such designated financial liabilities, the amount of the change in fair value that relates to changes in the entity's own credit risk is recognized in other comprehensive income and the remaining amount of the change in fair value is recognized in net income or loss. All contingent consideration payable is also included in this category. Derivative financial instruments that are designated as effective hedge instruments are excluded from this category.

The Company's interest rate swap contracts are required to be measured at fair value through net income or loss. The Company has not designated any financial instruments as hedges for accounting purposes.

The fair values of financial liabilities are based on changes in observable prices in active markets or by a valuation technique where no market exists. Transaction costs attributable to the issuance of financial liabilities at fair value through net income or loss are recognized in net income or loss as incurred.

*(a) Categories and measurement hierarchy*

The categories to which the financial instruments are allocated are:

| Financial instrument | Classification |
|---|---|
| **ASSETS** | |
| Cash | Amortized cost |
| Restricted funds | Amortized cost |
| Other assets | Amortized cost |
| Other assets | FVTP |
| Loan receivables | Amortized cost |
| Interest rate derivatives | FVTP |
| **LIABILITIES** | |
| Accounts payable and other liabilities | Amortized cost |
| Borrowings | Amortized cost |
| Customer security deposits | Amortized cost |
| Interest rate derivatives | FVTP |

All financial instruments measured at fair value and for which fair value is disclosed are categorized into one of three hierarchy levels. 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 fair values of financial instruments are classified using the IFRS 13, *Fair Value Measurement,* hierarchy as follows:

| | | | | **September 30, 2019** |
|---|---|---|---|---|
| | Level 1 | Level 2 | Level 3 | Carrying Value |
| **ASSETS** | | | | *($ thousands)* |
| Cash *(iii)* | $ 7,691 | $ — | $ — | $ 7,691 |
| Restricted funds *(iii)* | 11,846 | — | — | 11,846 |
| Other assets - Note 6 | — | 3,229 | — | 3,229 |
| Other assets - Note 6 | 483 | — | — | 483 |
| Loan receivables *(i)* | — | 344,997 | — | 344,997 |
| **LIABILITIES** | | | | |
| Accounts payable and other liabilities *(iii)* | — | (14,426) | — | (14,426) |
| Borrowings *(ii)* | — | (663,353) | — | (663,353) |
| Customer security deposits | — | (13,185) | — | (13,185) |
| Interest rate derivatives *(iv)* | — | (337) | — | (337) |

| | | | | December 31, 2018 |
|---|---|---|---|---|
| | Level 1 | Level 2 | Level 3 | Carrying Value |
| | | | | *($ thousands)* |
| **ASSETS** | | | | |
| Cash *(iii)* | $ 2,326 | $ — | $ — | $ 2,326 |
| Restricted funds *(iii)* | 13,598 | — | — | 13,598 |
| Other assets | — | 4,900 | — | 4,900 |
| Other assets | 453 | — | — | 453 |
| Loan receivables *(i)* | — | 293,131 | — | 293,131 |
| Interest rate derivatives *(iv)* | — | 896 | — | 896 |
| **LIABILITIES** | | | | |
| Accounts payable and other liabilities *(iii)* | — | (15,600) | — | (15,600) |
| Borrowings *(ii)* | — | (601,525) | — | (601,525) |
| Customer security deposits | — | (16,773) | — | (16,773) |

(i) There is no organized market for the finance receivables. The carrying value is the amortized cost using the effective interest rate method which approximates fair value because contractual interest rates approximate current market rates.

(ii) The stated value of the 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, restricted funds and for financial instruments with short maturities, including accounts payable and other liabilities.

(iv) The Company determines the fair value of its interest rate derivatives under the income valuation technique using a discounted cash flow model. Significant inputs to the valuation model include the contracted notional amount, LIBOR rate yield curves and the applicable credit-adjusted risk-free rate yield curve. The Company's interest rate derivative is included in the Level 2 fair value hierarchy because all of the significant inputs are directly or indirectly observable.

Transfers between levels are considered to occur on the date that the fair valuation methodology changes. There were no transfers between levels during the current or comparative periods.

*(b) Gains and losses on financial instruments*

The following table shows the net gains and losses arising for each category of financial instruments:

| | For the three months ended **September 30,** | | For the nine months ended **September 30,** | |
|---|---|---|---|---|
| | **2019** | 2018 | **2019** | 2018 |
| | | *($ thousands)* | | |
| Amortized cost: | | | | |
| Provision for credit losses | **$ (7,868)** | $ (4,111) | **$ (21,463)** | $ (13,695) |
| Designated as at fair value through net income or loss: | | | | |
| Convertible debentures | **—** | — | **—** | 29 |
| Fair value through net income or loss: | | | | |
| Investment in Dealnet common shares | **(61)** | — | **30** | (151) |
| Interest rate derivatives | **(82)** | 256 | **(1,211)** | 1,575 |
| Net loss | **$ (8,011)** | $ (3,855) | **$ (22,644)** | $ (12,242) |

## 4. 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 material changes in the Company's objectives, policies or processes for measuring and managing any of the risks to which it is exposed since the previous year end. Refer to Note 4 - *Financial Risk Management* of the 2018 annual audited consolidated financial statements for further disclosure.

## 5. DISCONTINUED OPERATIONS

On February 3, 2015, Case Funding sold certain assets and operations to a private equity firm. Case Funding retained approximately $9.4 million in finance receivables with a current balance of $1.2 million and pays a servicing fee of 5% of collections to administer the remaining portfolio.

Case Funding's net loss, included in loss from discontinued operations, for the nine months ended September 30, 2019 totaled $321,000 compared to net loss of $212,000 recorded in the same period in the prior year, which represented a basic and diluted loss per share of $0.02 and $0.02 respectively (2018 - $0.00 and $0.00). For the nine months ended September 30, 2019, Case Funding generated cash flows from operations of $230,000 compared to $1.2 million recorded in the prior year. For the three months ended September 30, 2019, Case Funding's net loss totaled $41,000 compared to a $181,000 net loss recorded in the same period in the prior year. For the three months ended September 30, 2019, Case Funding generated cash flows from operations of $138,000 compared to $352,000 recorded in the same period in the prior year.

At Case Funding, management reviews each attorney loan and medical lien receivable on an individual basis for collectability and for reserve requirements, if any. At September 30, 2019, it was determined an allowance of $82,000 (December 31, 2018 - $85,000) was required.

***(a) Assets and liabilities that are classified as held-for-sale***

| Legal finance receivables (Case Funding) consist of: | **September 30, 2019** | December 31, 2018 |
|---|---|---|
| | *($ thousands)* | |
| Attorney loans and medical liens | **$ 52** | $ 52 |
| Plaintiff advances | **1,191** | 1,800 |
| **Legal finance receivables** *(net of allowance)* | **1,243** | 1,852 |
| Current portion *(i)* | 239 | 459 |
| Long-term portion | $ 1,004 | $ 1,393 |

(i) The contracts are due when the underlying cases are settled which cannot be known and is therefore estimated. Plaintiff advances are made on a non-recourse basis, and repayment depends on the success and potential size of respective claims. The current portion of legal finance receivables is subject to estimation.

The fair values are classified using the measurement hierarchy (described in Note 3 - *Financial Instruments)* as follows:

| **ASSETS HELD FOR SALE** | | | | | **September 30, 2019** |
|---|---|---|---|---|---|
| *($ thousands)* | Category | Level 1 | Level 2 | Level 3 | Carrying Value |
| Attorney loans and medical liens *(ii)* | AC | $ — | $ 52 | $ — | $ 52 |
| Plaintiff advances | FVOCI | — | — | 1,191 | 1,191 |

| **ASSETS HELD FOR SALE** | | | | | December 31, 2018 |
|---|---|---|---|---|---|
| *($ thousands)* | Category | Level 1 | Level 2 | Level 3 | Carrying Value |
| Attorney loans and medical liens *(ii)* | AC | $ — | $ 52 | $ — | $ 52 |
| Plaintiff advances | FVOCI | — | — | 1,800 | 1,800 |

(ii) There is no organized market for the legal finance receivables. The carrying value is the amortized cost using the effective interest rate method which approximates fair value because contractual interest rates approximate current market rates.

## 6. OTHER ASSETS

| | | **September 30, 2019** | December 31, 2018 |
|---|---|---|---|
| | | *($ thousands)* | |
| Property tax receivable | | $ — | $ 782 |
| Tax receivable | | **326** | 991 |
| Sales tax receivable | | **202** | 589 |
| Prepaid expenses and other current assets | | **2,005** | 1,071 |
| Loan receivable - EcoHome | *a* | **3,229** | 4,900 |
| Common shares - Dealnet | *b* | **483** | 453 |
| **Other assets** | | **6,245** | 8,786 |
| Current portion | | 5,236 | 6,106 |
| Long-term portion | | $ 1,009 | $ 2,680 |

(a) Loan receivable - EcoHome - On February 18, 2016, the Company sold EcoHome Financial Inc. ("EcoHome") to Dealnet Capital Corp. ("Dealnet"). The loan represented the inter-company warehouse funding to EcoHome of leases and loans that had not yet been securitized with EcoHome funders prior to the sale of EcoHome. The loan receivable is secured by specific EcoHome leases and loans and a general security agreement over all the assets of EcoHome. The loan matures in October 2020, with fixed monthly principal payments, and related interest based on a floating interest rate plus a fixed margin. The loan receivable is carried at amortized cost. At September 30, 2019 and December 31, 2018, it was determined no material allowance for expected credit losses was required.

(b) Common shares - Dealnet - as partial consideration for the sale of EcoHome, the Company received 6,039,689 common shares of Dealnet. The Dealnet shares are measured at fair value through net income or loss. The fair value represents the trading price at each reporting date. Dealnet shares trade on the TSX Venture Exchange under the stock symbol "DLS".

## 7. FINANCE RECEIVABLES

The Company finances its leases and loan receivables by pledging such receivables as security for amounts borrowed from lenders under various facilities, as described in Note 10 - *Borrowings*. The lenders have the right to enforce their security interest in the pledged lease and loan receivables if the Company defaults under these facilities. Therefore, the Company retains ownership (in some cases through consolidated SPE's) and servicing responsibilities of the pledged lease and loan receivables and continues to recognize them on the consolidated statement of financial position.

| | **September 30, 2019** | December 31, 2018 |
|---|---|---|
| | *($ thousands)* | |
| Net investment in leases | **$ 438,368** | $ 435,793 |
| Loan receivables | **344,997** | 293,131 |
| | **$ 783,365** | $ 728,924 |

(a) Net investment in finance receivables includes the following:

| | **September 30, 2019** | December 31, 2018 |
|---|---|---|
| | *($ thousands)* | |
| Total minimum finance receivable payments *(b)* | **$ 954,138** | $ 893,080 |
| Residual values of leased equipment | **27,655** | 25,735 |
| | **981,793** | 918,815 |
| Unearned income, net of initial direct costs of acquisition | **(174,561)** | (168,946) |
| **Net investment in finance receivables before allowance for credit losses** | **807,232** | 749,869 |
| Allowance for credit losses *(c)* | **(27,324)** | (23,929) |
| | **779,908** | 725,940 |
| Reserve receivable on securitized financial contracts | **3,457** | 2,984 |
| Net investment in finance receivables | **783,365** | 728,924 |
| Current portion | 276,961 | 255,906 |
| Long-term portion | $ 506,404 | $ 473,018 |

(b) Minimum scheduled collections of finance receivables at September 30, 2019 are presented in the following table. 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 following minimum scheduled collections are not to be regarded as a forecast of future cash collections.

| | Minimum payments | Present value |
|---|---|---|
| | ($ thousands) | |
| 2019 | $ 96,660 | $ 71,562 |
| 2020 | 339,147 | 263,360 |
| 2021 | 254,736 | 210,453 |
| 2022 | 163,087 | 141,953 |
| 2023 | 80,172 | 73,050 |
| 2024 and thereafter | 20,336 | 19,199 |
| Total minimum payments | $ 954,138 | $ 779,577 |

(c) Allowance for credit losses
The Company measures loss allowances based on an expected credit loss ("ECL") impairment model for all financial instruments except those measured at fair value through profit and loss. Application of the model depends on the following credit stages of the financial assets:

(i) Stage 1 - for new leases and loans recognized and for existing leases or loans that have not experienced a significant increase in credit risk since initial recognition, a loss allowance is recognized equal to the credit losses expected to result from defaults occurring in the next 12 months;
(ii) Stage 2 - for those leases or loans that have experienced a significant increase in credit risk since initial recognition, a loss allowance is recognized equal to the credit losses expected over the remaining life of the lease or loan; and
(iii) Stage 3 - for leases or loans that are considered to be credit-impaired, a loss allowance equal to full life time ECLs is recognized.

Lease and loan receivables are composed of a large number of homogenous leases and loans, with relatively small balances. Thus, the evaluation of the allowance for credit losses is performed collectively for the lease and loan receivable portfolios, segregated into prime and non-prime.

Definitions of default have been selected to eliminate the judgement that may otherwise be necessary, given the diversity within the finance receivable portfolio, the lack of individual drivers of changes in credit risk across assets and over time, and the resulting inability to assess which specific assets will be rectified. For the purposes of measuring ECL, a default is defined as:
- For prime finance receivables: leases and loans that have missed one payment and are not subsequently rectified within 30 days.
- For non-prime finance receivables: leases and loans that have missed one payment.

ECLs are measured as the probability-weighted present value of expected cash shortfalls over the remaining expected life of the financial instrument based on the following defined credit stages:

For Stage 1, the Company utilized recent static pool data applied to recent origination levels and the inclusion of forward-looking macroeconomic assumptions under the ECL methodology. Recent static pool data includes historical loss rates by credit class and by originating quarter and therefore includes all knowable credit and economic conditions up to the reporting date.

For Stage 2, the Company considers prime leases and loans to have experienced a significant increase in credit risk since initial recognition if they are delinquent for over 30 days. Non-prime leases and loans that have experienced a significant increase in credit risk include: those instruments that are delinquent for over 30 days; and an estimate of those assets that will subsequently become delinquent calculated as approximately 15% of non-prime assets that are in default but have been delinquent for less than 30 days at the reporting date.

For Stage 3, the Company considers leases and loans to be credit impaired if they are delinquent for more than 90 days or if the individual leases and loans have otherwise been classified as non-accrual.

Customer security deposits 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 at that time. Past experience suggests that a very high percentage of the customer deposits are applied to the purchase option of the leased equipment at the end of the lease term, or as an offset against outstanding lease receivables.

Pawnee and Blue Chip are entitled to repossess financed equipment if the borrower defaults on their lease or loan contract. When a lease or loan is charged-off, the related equipment no longer has a carrying value on the consolidated financial statements. Any amounts recovered from the sale of equipment after a charge-off, are credited to the allowance for doubtful accounts when received. Repossessed equipment is generally held at various warehouses by the Company's third party contractors to repossess and sell the equipment. As Pawnee and Blue Chip finance a wide range of small equipment, it is difficult to estimate the fair value of the potential collateral when estimating future ECLs.

The process of estimating ECLs uses the following inputs and assumptions, in addition to internal weighted average static pool data, to reflect information about past events, current conditions and forecasts of future conditions that are not already captured in the inputs:

- Security deposits held;
- Recoveries of amounts previously charged off in the last 12 months, as an estimate of recoveries for the next 12 months;
- An estimate of the effects of natural disasters and economic shocks that have occurred on credit losses in the next 12 months;
- The stage of the business cycle for the industry, which considers: the competitive environment, GDP growth, prevailing interest rates and expectations of future rates, fiscal policy and inflation rates; and
- Current delinquency trends of non-accrual and greater than 30 days delinquency rates.

Forecasts of future events and conditions are incorporated by adjusting losses from the static pool data. Determining the inputs listed and ECLs requires significant estimation uncertainty. The estimation and application of forward-looking information requires significant judgement.

The following table shows the gross carrying amount of the finance receivables by credit categories:

| | **As of September 30, 2019** | | | |
|---|---|---|---|---|
| | Stage 1 | Stage 2 | Stage 3 | Total |
| | Performing | Under-Performing | Non-Performing | |
| | *($ thousands)* | | | |
| Prime | $ 535,296 | $ 1,314 | $ 3,422 | $ 540,032 |
| Non-prime | 254,895 | 5,077 | 7,228 | 267,200 |
| Total | $ 790,191 | $ 6,391 | $ 10,650 | $ 807,232 |

| | As of December 31, 2018 | | | |
|---|---|---|---|---|
| | Stage 1 | Stage 2 | Stage 3 | Total |
| | Performing | Under-Performing | Non-Performing | |
| | *($ thousands)* | | | |
| Prime | $ 472,036 | $ 965 | $ 2,442 | $ 475,443 |
| Non-prime | 264,035 | 5,311 | 5,080 | 274,426 |
| Total | $ 736,071 | $ 6,276 | $ 7,522 | $ 749,869 |

The following tables show reconciliations from the opening to the closing balance of the allowance for credit losses:

| | **Nine months ended September 30, 2019** | | | |
|---|---|---|---|---|
| | Stage 1 | Stage 2 | Stage 3 | |
| | Performing | Under-Performing | Non-Performing | **Total** |
| | *($ thousands)* | | | |
| Balance, January 1, 2019 | $ 10,879 | $ 6,141 | $ 6,909 | **$ 23,929** |
| Transfer to Performing (Stage 1) | 1,538 | (962) | (576) | **—** |
| Transfer to Under-Performing (Stage 2) | (23,012) | 23,067 | (55) | **—** |
| Transfer to Non-Performing (Stage 3) | — | (21,003) | 21,003 | **—** |
| Net remeasurement of loss allowance | 14,589 | (715) | 121 | **13,995** |
| New receivables originated | 7,468 | — | — | **7,468** |
| Provision for credit losses | 583 | 387 | 20,493 | **21,463** |
| Charge-offs | — | — | (25,606) | **(25,606)** |
| Recoveries of amounts previously charged off | — | — | 8,185 | **8,185** |
| Net charge-offs | — | — | (17,421) | **(17,421)** |
| Impact of change in foreign exchange rates | (276) | (177) | (194) | **(647)** |
| Balance, end of period | **$ 11,186** | **$ 6,351** | **$ 9,787** | **$ 27,324** |

| | Nine months ended September 30, 2018 | | | |
|---|---|---|---|---|
| | Stage 1 | Stage 2 | Stage 3 | |
| | Performing | Under-Performing | Non-Performing | **Total** |
| | *($ thousands)* | | | |
| Balance, January 1, 2018 | $ 10,608 | $ 4,150 | $ 7,216 | **$ 21,974** |
| Transfer to Performing (Stage 1) | 1,678 | (885) | (793) | **—** |
| Transfer to Under-Performing (Stage 2) | (15,991) | 16,043 | (52) | **—** |
| Transfer to Non-Performing (Stage 3) | — | (14,962) | 14,962 | **—** |
| Net remeasurement of loss allowance | 6,530 | (238) | (804) | **5,488** |
| New receivables originated | 8,207 | — | — | **8,207** |
| Provision for credit losses | 424 | (42) | 13,313 | **13,695** |
| Charge-offs | — | — | (20,478) | **(20,478)** |
| Recoveries of amounts previously charged off | — | — | 6,725 | **6,725** |
| Net charge-offs | — | — | (13,753) | **(13,753)** |
| Impact of change in foreign exchange rates | 297 | 129 | 207 | **633** |
| Balance, end of period | **$ 11,329** | **$ 4,237** | **$ 6,983** | **$ 22,549** |

(d) Finance receivables past due

The following aging represents the total carrying amount of the lease and loan receivables and not just the payments that are past due. The balances presented exclude the $13.2 million (December 31, 2018 - $16.8 million) of security deposits received from lessees/borrowers and the collateral held (including potential proceeds from repossessed equipment, and potential recoveries from personal guarantees) that would offset any charge-offs. An estimate of fair value for the collateral and personal guarantees cannot reasonably be determined.

Pawnee charges off leases and loans 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 recognized before the subject leases/loans reach 154 days contractually past due, due to insolvency or non-responsiveness of the lessee or borrower. Blue Chip charges off leases and loans on an individual basis when there is no realistic prospect of recovery. Loan and lease receivables that are charged-off during the period are all subject to continued collection efforts.

| | | | | | | |
|---|---|---|---|---|---|---|
| | | | | | | **As of September 30, 2019** |
| *($ thousands)* | **Current** | **1-30 days** | **31 - 60 days** | **61 - 90 days** | **Over 90 days** | **Total** |
| Equipment lease receivables | **$ 433,896** | **$ 8,488** | **$ 3,030** | **$ 1,113** | **$ 3,954** | **$ 450,481** |
| Loan receivables | **344,977** | **6,921** | **1,710** | **980** | **2,163** | **356,751** |
| | **$ 778,873** | **$ 15,409** | **$ 4,740** | **$ 2,093** | **$ 6,117** | **$ 807,232** |
| Credit impaired | **$ 356** | **$ 309** | **$ 1,226** | **$ 2,016** | **$ 5,880** | **$ 9,787** |
| Past due but not impaired | **$ —** | **$ 15,100** | **$ 3,514** | **$ 77** | **$ 237** | **$ 18,928** |

| | | | | | | |
|---|---|---|---|---|---|---|
| | | | | | | As of December 31, 2018 |
| *($ thousands)* | Current | 1-30 days | 31 - 60 days | 61 - 90 days | Over 90 days | Total |
| Equipment lease receivables | $ 434,231 | $ 8,757 | $ 2,551 | $ 1,102 | $ 2,653 | $ 449,294 |
| Loan receivables | 296,429 | 3,189 | 200 | 545 | 212 | 300,575 |
| | $ 730,660 | $ 11,946 | $ 2,751 | $ 1,647 | $ 2,865 | $ 749,869 |
| Impaired | $ 544 | $ 273 | $ 1,985 | $ 1,554 | $ 2,553 | $ 6,909 |
| Past due but not impaired | $ — | $ 11,673 | $ 766 | $ 93 | $ 312 | $ 12,844 |

(e) Modifications
In cases where a borrower experiences financial difficulties, Pawnee and Blue Chip may grant certain concessionary modifications to the terms and conditions of a lease or loan. Modifications may include payment deferrals, extension of amortization periods, and other modifications intended to minimize the economic loss and to avoid repossession of collateral. Pawnee and Blue Chip have policies in place to determine the appropriate remediation strategy based on certain conditions. Significant increase in credit risk (Stage 2 categorization) is assessed based on the risk of default at initial recognition of the original asset. Expected cash flows arising from the modified contractual terms are considered when calculating the ECL for the modified asset. For finance receivables that were modified while having a lifetime ECL, the leases and loans can revert to having 12-month ECL after a period of performance and improvement in the borrower's financial condition.

The net investment in finance receivables that have been modified (in 2019 or prior) and are current at September 30, 2019 is $14.2 million (December 31, 2018 - $14.8 million). On average the terms have been modified to extend the contracts by approximately one to three months, depending on the modification. Finance receivables modified during the nine months ended September 30, 2019 had a total net investment in finance receivable balance at the time of modification of $19.6 million (2018 - $18.9 million). These amounts reflect the net investment in finance receivable balances prior to payments collected since modification, or leases that terminated early after modifications or leases charged-off after modification.

## 8. RIGHT-TO-USE ASSETS AND PREMISES LEASES PAYABLE

Under IFRS 16, the Company assesses whether a contract is, or contains, a lease based on whether the contract conveys the right to control the use of an identified asset for a period of time in exchange for consideration. Included in right-to-use assets and premises leases payable are the Company's leased offices at the Pawnee and Blue Chip locations. For such agreements, the Company recognizes a right-of-use asset and a lease liability at the lease commencement date. Measurement requires the lease term to be determined which includes optional extension periods only if they are reasonably certain to be exercised. Determining the lease term is judgmental.

The lease liability is initially measured at the present value of the lease payments that are unpaid at the commencement date, discounted using the Company's incremental borrowing rate because the rate implicit in the lease is not known. The right-to-use asset is measured based on the initial amount of the lease liability adjusted for any lease payments made at or before the commencement date, plus any initial direct costs incurred and an estimate of costs to dismantle and remove the underlying asset or to restore the underlying asset or the site on which it is located, less any lease incentives received.

The right-to-use assets are depreciated over the respective lease term using the straight-line method as this most closely reflects the expected pattern of consumption of the future economic benefits. Lease terms range from 2 to 7 years, and the optional extension periods have been excluded. Right-to-use assets are reduced by impairment losses, if any, and adjusted for certain remeasurments of the lease liability. The lease liability is subsequently accounted for at amortized cost using the effective interest rate method.

The lease liability for the Company's leases will be remeasured in a future period if there is a change in future lease payments arising from a change in the likelihood that extension options are exercised. On remeasuring a lease agreement, a corresponding adjustment is made to the carrying amount of the right-to-use asset.

The following table presents the right-to-use assets for the Company:

| | | For the nine months ended September 30, 2019 |
|---|---|---|
| | | *($ thousands)* |
| Premises: | | |
| Balance, beginning of period | $ | — |
| Adoption of IFRS 16 | | 3,837 |
| Balance, January 1, 2019 | | 3,837 |
| Additions | | — |
| Depreciation | | (510) |
| Effects of movement in exchange rates | | (87) |
| Balance, end of period | $ | 3,240 |

The contractual undiscounted cash flows for the related lease obligations are disclosed in Note 12 - *Minimum payments*. The effective interest expense on these lease obligations for the nine months ended September 30, 2019 was $123,000 and is included in interest expense. Total outflow for leases was $471,000. Expenses for leases of low-dollar value items are not material. Pawnee's two options to extend the premises lease term for two additional periods of 60 month each are not reasonably certain to be exercised and have therefore been excluded from the measurement of lease obligations.

| | | For the nine months ended September 30, 2019 |
|---|---|---|
| | | *($ thousands)* |
| Premises Leases Liability | | |
| Balance, beginning of period | $ | — |
| Adoption of IFRS 16 | | 3,837 |
| Balance, January 1, 2019 | | 3,837 |
| Additions | | — |
| Principal payments | | (347) |
| Effects of movement in exchange rates | | (91) |
| Balance, end of period | $ | 3,399 |

## 9. ACCOUNTS PAYABLE AND OTHER LIABILITIES

Accounts payable and other liabilities comprise:

| | **September 30, 2019** | December 31, 2018 |
|---|---|---|
| | *($ thousands)* | |
| Dividend payable | **$ 1,241** | $ 1,240 |
| Accounts payable | **1,817** | 2,187 |
| Sales tax payable | **827** | 874 |
| Customer deposits and prepayments | **924** | 845 |
| Unfunded finance receivables | **4,987** | 5,984 |
| Taxes payable | — | 742 |
| Payroll related payables and accruals | **2,432** | 1,176 |
| Accrued expenses and other liabilities | **2,198** | 2,552 |
| | **$ 14,426** | $ 15,600 |

## 10. BORROWINGS

| | Chesswood credit facility *(a)* | Chesswood deferred financing costs | Pawnee credit facilities *(b)* | Pawnee deferred financing costs | Blue Chip financing facilities *(c)* | Total |
|---|---|---|---|---|---|---|
| | | | *($ thousands)* | | | |
| Net as of December 31, 2017 | $ 200,405 | $ (2,536) | $ 87,241 | $ (2,142) | $ 129,187 | $ 412,155 |
| Proceeds or draw-downs | 242,806 | — | 172,288 | — | 84,029 | 499,123 |
| Repayments | (227,950) | — | (45,606) | — | (67,054) | (340,610) |
| Payment of financing costs | — | (425) | — | (3,542) | — | (3,967) |
| Amortization of deferred financing costs | — | 1,254 | — | 1,521 | — | 2,775 |
| Foreign currency translation adjustment | 18,017 | — | 14,326 | (294) | — | 32,049 |
| Net as of December 31, 2018 | 233,278 | (1,707) | 228,249 | (4,457) | 146,162 | 601,525 |
| Proceeds or draw-downs | 158,241 | — | 74,873 | — | 52,653 | 285,767 |
| Repayments | (115,042) | — | (38,087) | — | (56,666) | (209,795) |
| Payment of financing costs | — | (1,855) | — | (1,114) | — | (2,969) |
| Amortization of deferred financing costs | — | 1,001 | — | 1,489 | — | 2,490 |
| Foreign currency translation adjustment | (6,982) | — | (6,811) | 128 | — | (13,665) |
| **Net as of September 30, 2019** | **$ 269,495** | **$ (2,561)** | **$ 258,224** | **$ (3,954)** | **$ 142,149** | **$ 663,353** |

(a) The Chesswood revolving credit facility allows borrowings of up to US$250.0 million subject to, among other things, certain percentages of eligible gross finance receivables. This credit facility is secured by substantially all of the Company's assets, contains covenants, including maintaining leverage and interest coverage ratios, and expires on December 8, 2022 (renewed on September 30, 2019 - previously expired on December 8, 2020). At September 30, 2019, the Company was utilizing US$212.3 million (December 31, 2018 - US$178.7 million) of its credit facility and had approximately US$37.7 million in additional borrowings available under the corporate credit facility. At September 30, 2019 and December 31, 2018, and throughout the periods presented, the Company was compliant with all covenants. Based on average debt levels, the effective interest rate during the nine months ended September 30, 2019 was 5.44% (year-ended December 31, 2018 - 5.12%). Subsequent to the quarter-end, the outstanding balance of this facility was reduced by US$105.4 million from the proceeds of a securitization, see Note 21 - *Subsequent Events*.

(b) Pawnee credit facilities:
(i) Pawnee has a US$250 million revolving warehouse loan facility specifically to fund its growing prime portfolio, through its subsidiary Pawnee Portfolio Fund ("PPF"). The warehouse facility will hold Pawnee's prime receivables before they are securitized. This credit facility is secured by PPF's assets, contains covenants, including maintaining leverage and interest coverage ratios, and expires in August 2023. At September 30, 2019, Pawnee was utilizing US$120.0 million of this facility (December 31, 2018 - US$83.0 million). At September 30, 2019 and throughout the period from August 2018, Pawnee was compliant with all covenants. Based on average debt levels, the effective interest rate during the nine months ended September 30, 2019 was 5.60% (December 31, 2018 - 7.54%). Subsequent to the quarter-end, the outstanding balance of this facility was reduced by US$120.0 million from the proceeds of a securitization, see Note 21 - *Subsequent Events*.
(ii) Pawnee has a combined US$125 million non-recourse asset-backed facilities with Capital One (the "CapOne facilities"), through subsidiaries Pawnee Receivable Fund I and II LLC. The CapOne facilities are secured by US$154.2 million in gross receivables from Pawnee's prime portfolio of equipment leases and loans and repayment terms are based on the cash flow of the underlying portfolio. The proceeds were used to pay down Chesswood's existing revolving credit facility. The facilities require Pawnee to mitigate its interest rate risk by entering into interest rate caps for a notional amount not less than 80% of the aggregate outstanding balance. The balance of the facilities at September 30, 2019 was US$57.1 million. Pawnee is to comply with leverage ratio, interest coverage ratio, and tangible net worth covenants. At September 30, 2019 and December 31, 2018, and throughout the periods presented, Pawnee was compliant with all covenants. Based on average debt levels, the effective interest rate during the nine months ended September 30, 2019 was 5.83% (2018 - 5.51%).
(iii) Pawnee has a credit facility, with an US$80 million annual capacity, with a life insurance company that expires in June 2027. The funder makes approved advances to Pawnee on a tranche-by-tranche basis, with each tranche collateralized by a specific group of underlying finance receivables and any related security provided thereunder. The facility has recourse only to the assets financed. The cost of each loan advance is fixed at the time of each tranche. Pawnee maintains certain cash reserves as credit enhancements or provides letters of guarantee in lieu of those same cash reserves. Pawnee retains the servicing of these finance receivables. The balance of this facility at September 30, 2019 was US$17.9 million with an effective interest rate of 4.12% (including amortization of origination costs).

(c) Blue Chip has master purchase and servicing agreements with various financial institutions and life insurance companies (referred to collectively as the "Funders"). The Funders make advances to Blue Chip on a tranche-by-tranche basis, with each tranche collateralized by a specific group of underlying finance receivables and any related security provided thereunder. The facilities have limited recourse to other assets in the event that lessees\borrowers fail to make payments when due. Blue Chip either maintains certain cash reserves as credit enhancements or provides letters of guarantee in return for release of the cash reserves. Blue Chip continues to service these finance receivables on behalf of the Funders.

At September 30, 2019, Blue Chip had access to the following committed lines of funding: (i) $60.0 million annual limit from a life insurance company; (ii) $100.0 million rolling limit from a financial institution; and (iii) approved funding from another financial institution with no annual or rolling limit. As at September 30, 2019, Blue Chip had $142.1 million (December 31, 2018 - $146.2 million) in securitization and bulk lease financing facilities debt outstanding, was utilizing $94.2 million (December 31, 2018 - $76.2 million) of its available financing and had access to at least $95.8 million (December 31, 2018 - $93.8 million) of additional financing from the Funders.

Interest rates are fixed at the time of each advance and are based on Government of Canada Bond yields with maturities comparable to the term of the underlying leases plus a premium. Based on average debt levels, the effective interest rate during the nine months ended September 30, 2019 was 3.60% (2018 - 3.31%). As at September 30, 2019, Blue Chip had provided $10.4 million in outstanding letters of guarantee through Chesswood's revolving credit facility. Blue Chip must meet certain financial covenants, including leverage ratio, interest coverage ratio, and tangible net worth covenants, to support these securitization and bulk lease financing facilities. As at September 30, 2019 and December 31, 2018, and throughout the periods presented, Blue Chip was compliant with all covenants.

(d) Restricted funds
Restricted funds represent cash reserve accounts which are held in trust as security for secured borrowings (Pawnee facilities in *(b)* above) and cash collection accounts required by the lenders of certain financial assets that can only be used to repay these debts on specific dates. The 'cash in collections accounts' will be applied to the outstanding borrowings in the following month.

| | | **September 30, 2019** | | December 31, 2018 |
|---|---|---|---|---|
| | | *($ thousands)* | | |
| Restricted - cash in collection accounts | **$** | **7,332** | $ | 9,063 |
| Restricted - cash reserves | | **4,514** | | 4,535 |
| **Restricted funds** | **$** | **11,846** | $ | 13,598 |

## 11. INTEREST RATE DERIVATIVES

Interest rate derivatives, which comprise interest rate swaps and caps, are not considered trading instruments as the Company intends to hold them until maturity. The instruments do not qualify as hedges for accounting purposes, and are therefore recorded as separate derivative financial instruments. Accordingly, the estimated fair values are recorded on the accompanying consolidated statement of financial position. The fair values are based on the estimated net present value of cash flows and represent the consideration the Company would receive (pay) if a derivative was terminated on the reporting date.

Payments made and received pursuant to the terms of the instruments are recorded as an adjustment to interest expense. Fair value adjustments are recorded separately on the statement of income.

(a) Derivative swaps

The Company enters into interest rate swap agreements that provide for payment of an annual fixed rate, in exchange for a LIBOR based floating rate amount. The interest rate swaps are intended to offset a portion of the variable interest rate risk on Chesswood's revolving credit facility (see Note 10(a) - *Borrowings*). At September 30, 2019, the fair value of the swaps was a liability of $385,000 (December 31, 2018 - an asset of $455,000).

The following swap agreements were outstanding at September 30, 2019:

| **Effective Date** | **Notional Amount US$** | **Annual Fixed Rate** | **Maturity Date** |
|---|---|---|---|
| August 15, 2016 | $20 million | 1.985% | August 13, 2020 |
| August 15, 2016 | $20 million | 2.120% | August 13, 2021 |

(b) Derivative caps

During the third quarter, Pawnee entered into a US$40.0 million interest rate cap agreement that provides for payment of an annual fixed rate, in exchange for a LIBOR based floating rate amount. The interest rate cap is intended to offset a portion of the variable interest rate risk on Pawnee's warehouse facility (see Note 10(b)(*i*) - *Borrowings*). The interest rate cap agreement matures on July 25, 2022. At September 30, 2019, the fair value of the swap was an asset of $35,000 (December 31, 2018 - n/a).

During the third quarter, Pawnee entered into a US$164.5 million interest rate swaption agreement that provides for payment of an annual fixed rate, in exchange for a LIBOR based floating rate amount. The swaption agreement was used to protect the pricing of the marketed securitization entered into subsequent to the quarter end (see Note 10(b)(*i*) - *Borrowings* and Note 21 - *Subsequent Events*). The swaption agreement matured on October 23, 2019. At September 30, 2019, the fair value of the swap was an asset of $2,300 (December 31, 2018 - n/a).

Pawnee's non-recourse asset-backed facilities (see Note 10(b)(*ii*) - *Borrowings*) require Pawnee to mitigate interest rate risk by entering into an interest rate cap for a notional amount of not less than 80% of the aggregate outstanding balance. The interest rate caps are tied to the repayment terms of the underlying finance receivables portfolio supporting the Pawnee facility, through the maturity date, with a floating index rate based on USD-LIBOR-BBA, but subject to a capped fixed rate of 2.25% and 2.75%. At September 30, 2019, the fair value of the interest rate caps was an asset of $11,000 (December 31, 2018 - asset $441,000).

## 12. MINIMUM PAYMENTS

The following are the contractual payments and maturities of financial liabilities and other commitments (including interest):

| *($ thousands)* | | 2019 | 2020 | 2021 | 2022 | 2023 | 2024 + | **Total** |
|---|---|---|---|---|---|---|---|---|
| Accounts payable and other liabilities | | $ 14,426 | $ — | $ — | $ — | $ — | $ — | **$ 14,426** |
| Premises leases payments | *(i)* | 169 | 699 | 721 | 732 | 743 | 813 | **3,877** |
| Borrowings | *(ii)* | 60,404 | 191,162 | 124,219 | 347,257 | 33,514 | 1,520 | **758,076** |
| Customer security deposits | *(iii)* | 1,138 | 3,874 | 4,014 | 3,052 | 2,294 | 146 | **14,518** |
| | | 76,137 | 195,735 | 128,954 | 351,041 | 36,551 | 2,479 | **790,897** |
| Service contracts | | 99 | 283 | 216 | 111 | 2 | — | **711** |
| Total commitments | | $ 76,236 | $ 196,018 | $ 129,170 | $351,152 | $ 36,553 | $ 2,479 | **$ 791,608** |

i. The Company and its subsidiaries are committed to future minimum rental payments under existing leases for premises, excluding occupancy costs and property tax, with expirations up to 2025. See Note 8 - *Right-to-Use Assets and Premises Leases Payable*.
ii. Borrowings are described in Note 10 - *Borrowings*, and include fixed payments for Pawnee and Blue Chip's securitization facilities and Chesswood's corporate credit facility and Pawnee's warehouse facility, which are lines-of-credit and, as such, the balances can fluctuate. The amount above includes fixed interest payments on Pawnee and Blue Chip's credit facilities and estimated interest payments on the Chesswood corporate credit facility, assuming the interest rate, debt balance and foreign exchange rate at September 30, 2019 remain the same until the expiry date of December 2020. The amount owing under Chesswood's corporate credit facility is shown in year of maturity, all other expected borrowings payments are based on the underlying finance receivables supporting the borrowings.
iii. The Company's experience has shown 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.
iv. Please see Note 7(b) - *Finance Receivables* for the expected collections of finance receivables over the same time period. See Note 10(d) - *Borrowings* - for the amount of restricted cash in collections accounts that will be applied to debt in the following month.

The Company has no material "off-balance sheet" financing obligations, except for U.S.$8.8 million in letters of guarantee. For contingent liabilities and other commitments, refer to Note 18 - *Contingent Liabilities and Other Financial Commitments* of the 2018 annual audited consolidated financial statements.

## 13. CAPITAL MANAGEMENT

The Company's capital consists of borrowings and shareholders' equity. The Company's objectives when managing capital are to safeguard the Company's long-term ability to continue as a going concern and to provide adequate returns for shareholders. The Company's share capital is not subject to external restrictions.

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 share repurchases through the normal course issuer bid and the amount of dividends paid to shareholders.

Chesswood's three-year revolving senior secured US$250 million credit facility supports growth in finance receivables, provides the Company's working capital needs and for general corporate purposes. The facility, available in U.S. or Canadian dollars, also improves the Company's financial flexibility by centralizing treasury management and making the provision of capital to individual businesses more efficient. This credit facility is secured by substantially all of the Company's assets, contains covenants including maintaining leverage and interest coverage ratios, and expires on December 8, 2022. At September 30, 2019 and December 31, 2018, and throughout the periods presented, the Company was compliant with all covenants.

Financing facilities of operating subsidiaries are used to provide funding for the respective subsidiary's operations (namely to provide financing for the purchase of assets which are to be the subject of leases and loans or to support working capital). The financing facilities are not intended to directly fund dividends paid by the Company.

## 14. COMMON SHARES

The Company is authorized to issue an unlimited number of common shares, with no par value. Each common share entitles the holder thereof to receive notice of, to attend, and to one vote at all meetings of the shareholders. The holders of common shares will be entitled to receive any dividends, if, as and when declared by the Company's directors. The Shareholders will also be entitled to share equally, share-for-share, in any distribution of the assets of the Company upon the liquidation, dissolution or winding-up of the Company or other distribution of its assets among its Shareholders for the purpose of winding-up its affairs. Additional information relevant to the common shares, the rights of holders thereof and the operation and conduct of the Company can be found in the Company's Articles and by-laws, which have been filed under the Company's profile on SEDAR at www.sedar.com.

| | | Common shares | | Amount |
|---|---|---|---|---|
| | | *(# '000s)* | | *($ thousands)* |
| Balance, December 31, 2017 | | 16,575 | $ | 105,208 |
| Exercise of restricted share units (*Note 15(b)*) | | 70 | | 806 |
| Exercise of options (*Note 15(a)*) | | 83 | | 741 |
| Repurchase of common shares under issuer bid | *(a)* | (499) | $ | (3,179) |
| Balance, December 31, 2018 | | 16,229 | $ | 103,576 |
| Exercise of restricted share units (*Note 15(b)*) | | 44 | | 482 |
| Exercise of options *(Note 15(a))* | | 53 | | 403 |
| Repurchase of common shares under issuer bid | *(a)* | (78) | | (498) |
| **Balance, September 30, 2019** | | **16,248** | **$** | **103,963** |

(a) Normal course issuer bids

In August 2017, the Company's Board of Directors approved the repurchase for cancellation of up to 1,085,981 of the Company's outstanding common shares for the period commencing August 25, 2017 and ending on August 24, 2018. During 2017, no common shares were repurchased under this normal course issuer bid. From January 1, 2018 to August 24, 2018, the Company repurchased 293,096 of its shares under the normal course issuer bid at an average cost of $10.5277 per share. The excess of the purchase price over the average stated value of common shares purchased for cancellation was charged to retained earnings.

In August 2018, the Company's Board of Directors approved the repurchase for cancellation of up to 1,043,895 of the Company's outstanding common shares for the period commencing August 25, 2018 and ending on August 24, 2019. From August 25, 2018 to December 31, 2018, the Company repurchased 206,340 of its shares under the normal course issuer bid at an average cost of $10.2412 per share. From January 1, 2019 to August 24, 2019, the Company repurchased 78,020 of its shares under the normal course issuer bid at an average cost of $10.3583 per share. The excess of the purchase price over the average stated value of common shares purchased for cancellation was charged to retained earnings.

In August 2019, the Company's Board of Directors approved the repurchase for cancellation of up to 1,031,791 of the Company's outstanding common shares for the period commencing August 26, 2019 and ending on August 25, 2020. From August 26, 2019 to September 30, 2019, no common shares were repurchased under this normal course issuer bid. Decisions regarding the timing of purchases are based on market conditions and other factors.

## 15. COMPENSATION PLANS

Share-based compensation reserve represents the accumulated share-based compensation expensed over the vesting term for options and restricted share units unexercised at September 30, 2019. There were 2,553,939 options and 44,000 restricted share units outstanding at September 30, 2019.

*(a) Share options*

The options vest 30% at the end of the first year, another 35% at the end of the second year, and the remaining 35% at the end of the third year and expire on the 10th anniversary of the grant date. The options settle in Common Shares and have an exercise price equal to the 10-day volume weighted average price of the Common Shares prior to the day such options were granted. The cost of options is measured using the Black-Scholes option pricing model and is expensed over the vesting period of each tranche with an increase in share-based compensation reserve.

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

| | For the three months ended **September 30,** | | For the nine months ended **September 30,** | |
|---|---|---|---|---|
| | **2019** | 2018 | **2019** | 2018 |
| Balance, beginning of period | **2,335,939** | 2,474,854 | **2,384,354** | 2,155,989 |
| Granted | **222,500** | — | **222,500** | 405,000 |
| Exercised | **(4,500)** | (27,000) | **(52,915)** | (83,135) |
| Forfeited | **—** | (43,500) | **—** | (73,500) |
| Balance, end of period | **2,553,939** | 2,404,354 | **2,553,939** | 2,404,354 |

An analysis of the options outstanding at September 30, 2019 is as follows:

| Grant date | Number of options outstanding | Vested | Expiry date | Exercise price |
|---|---|---|---|---|
| April 25, 2011 | 197,500 | 197,500 | April 24, 2021 | $ 7.79 |
| June 10, 2011 | 50,000 | 50,000 | June 9, 2021 | $ 7.73 |
| December 6, 2011 | 170,000 | 170,000 | December 6, 2021 | $ 6.14 |
| June 25, 2012 | 153,989 | 153,989 | June 24, 2022 | $ 7.45 |
| December 6, 2012 | 125,000 | 125,000 | December 6, 2022 | $ 8.86 |
| April 29, 2014 | 265,000 | 265,000 | April 29, 2024 | $ 14.12 |
| April 16, 2015 | 160,000 | 160,000 | April 16, 2025 | $ 12.53 |
| April 29, 2015 | 150,000 | 150,000 | April 29, 2025 | $ 12.24 |
| August 15, 2016 | 334,950 | 334,950 | August 15, 2026 | $ 10.17 |
| June 19, 2017 | 355,000 | 230,750 | June 19, 2027 | $ 12.15 |
| March 28, 2018 | 370,000 | 111,000 | March 28, 2028 | $ 10.96 |
| September 6, 2019 | 222,500 | — | September 6, 2029 | $ 8.95 |
| | 2,553,939 | 1,948,189 | | |

During the nine months ended September 30, 2019, personnel expenses and the share-based compensation reserve included $244,700 (2018 - $414,100) relating to option expense. As of September 30, 2019, unrecognized non-cash compensation expense related to the outstanding options was $337,100 (September 30, 2018 - $509,500), which is expected to be recognized over the remaining vesting period.

During the nine months ended September 30, 2019, 52,915 options were exercised (2018 - 83,135) for total cash consideration of $285,000 (2018 - $571,000). On exercise, the accumulated amount in share-based compensation reserve related to the exercised options of $118,000 (2018 - $169,000) was transferred to Common Share capital (Common Share capital was also increased by the cash consideration received upon exercise). For the options exercised during the nine months ended September 30, 2019, the weighted average share price at the date of exercise was $10.56 (2018 - $11.20).

At September 30, 2019, the weighted average exercise price is $10.44 (September 30, 2018 - $10.45) and the weighted average remaining contractual life for all options outstanding is 5.8 years (September 30, 2018 - 6.3 years). The 1,948,189 options exercisable at September 30, 2019 have a weighted average exercise price of $10.39 (September 30, 2018 - 1,669,354 options at $10.10).

The value of the options granted during the period was determined using the Black-Scholes Option Pricing model with the following assumptions:

| | September 6, 2019 | March 28, 2018 |
|---|---|---|
| Number of options granted | 222,500 | 405,000 |
| Weighted average share price at date | $8.95 | $10.96 |
| Expected volatility | 27% - 28% | 30% - 32% |
| Expected life (years) | 7 - 9 | 7 - 9 |
| Expected dividend yield | 7.04% | 7.40% |
| Risk-free interest rates | 1.19% | 2.05% |
| Weighted average fair value of options granted | $0.84 | $1.23 |

The risk-free rate was based on the Government of Canada benchmark bond yield on the date of grant for a term equal to the expected life of the options. Expected volatility was determined by calculating the historical volatility of the Company's share price over a period equal to the expected life of the options. The expected life was based on the contractual life of the awards and adjusted, based on management's best estimate and historical redemption rates.

The Black-Scholes Option Pricing Model was developed for use in estimating the fair value of traded options, which have no black-out or vesting restrictions and are fully transferable. In addition, the Black-Scholes Option Pricing Model requires the use of subjective assumptions, including the expected stock price volatility. As a result of the Company's Stock Option Plan having characteristics different from those of traded options, and because changes in the subjective assumptions can have a material effect on the fair value estimates, the Black-Scholes Option Pricing model does not necessarily provide a single measure of the fair value of options granted.

*(b) Restricted share units*

Restricted share units (RSUs) typically vest one year from the date of issue, are to be settled by the issue of Common Shares and expire in ten years. RSUs granted are in respect of future services and are expensed over the vesting period with an increase in share-based compensation reserve. Compensation cost is measured based on the weighted average market price of the Common Shares for the 10 days prior to the date of the grant of the RSUs, which was $10.14 (2018 - $10.96). Holders of RSUs are not entitled to dividends before the RSUs are exercised.

A summary of the RSUs outstanding is as follows:

| | For the three months ended **September 30,** | | For the nine months ended **September 30,** | |
|---|---|---|---|---|
| | **2019** | 2018 | **2019** | 2018 |
| Balance, beginning of period | **44,000** | 44,000 | **44,000** | 70,000 |
| Granted | **—** | — | **44,000** | 44,000 |
| Exercised | **—** | — | **(44,000)** | (70,000) |
| Balance, end of period | **44,000** | 44,000 | **44,000** | 44,000 |

During the nine months ended September 30, 2019, personnel expenses and share-based compensation reserve included $264,100 (2018 - $444,700) relating to RSUs. During the nine months ended September 30, 2019, an aggregate of 44,000 RSUs were granted (2018 - 44,000) to directors. During the nine months ended September 30, 2019, 44,000 RSUs were exercised (2018 - 70,000). On exercise, the accumulated balance in share-based compensation reserve related to the RSUs of $482,200 (2018 - $806,200) was transferred from reserve to Common Share capital. For the RSUs exercised during the nine months ended September 30, 2019, the weighted average share price at the date of exercise was $11.10 (2018 - $10.48). As of September 30, 2019, unrecognized non-cash compensation expense related to non-vested RSUs was $297,000 (September 30, 2018 - $236,500).

## 16. DIVIDENDS

Under the Chesswood revolving credit facility (see Note 10(a) - *Borrowings*), the maximum amount of cash dividends (and/or cost of any repurchases under normal course issuer bids) that the Company can pay in respect of a month is 1/12 of 90% of Free Cash Flow for the most recently completed four financial quarters in which Chesswood has publicly filed its consolidated financial statements (including its annual consolidated financial statements in respect of a fourth quarter). Free Cash Flow is defined in the MD&A for the nine-month period ended September 30, 2019.

The following dividends were paid to Common Shareholders and Exchangeable Securities holders (included as non-controlling interest) during the nine months ended September 30, 2019:

| Record date | Payment date | Cash dividend per share ($) | Total dividend amount<br>*($ thousands)* |
|---|---|---|---|
| December 31, 2018 | January 15, 2019 | $ 0.070 | $ 1,240 |
| January 31, 2019 | February 15, 2019 | $ 0.070 | 1,236 |
| February 28, 2019 | March 15, 2019 | $ 0.070 | 1,236 |
| March 29, 2019 | April 15, 2019 | $ 0.070 | 1,241 |
| April 30, 2019 | May 15, 2019 | $ 0.070 | 1,241 |
| May 31, 2019 | June 17, 2019 | $ 0.070 | 1,242 |
| June 28, 2019 | July 15, 2019 | $ 0.070 | 1,242 |
| July 31, 2019 | August 15, 2019 | $ 0.070 | 1,241 |
| August 30, 2019 | September 16, 2019 | $ 0.070 | 1,240 |
| | | | $ 11,159 |

The following dividends were paid to Common Shareholders and Exchangeable Securities holders (included as non-controlling interest) during the nine months ended September 30, 2018:

| Record date | Payment date | Cash dividend per share ($) | Total dividend amount<br>*($ thousands)* |
|---|---|---|---|
| December 29, 2017 | January 15, 2018 | $ 0.070 | $ 1,264 |
| January 31, 2018 | February 15, 2018 | $ 0.070 | 1,264 |
| February 28, 2018 | March 15, 2018 | $ 0.070 | 1,260 |
| March 29, 2018 | April 16, 2018 | $ 0.070 | 1,260 |
| April 30, 2018 | May 15, 2018 | $ 0.070 | 1,254 |
| May 31, 2018 | June 15, 2018 | $ 0.070 | 1,257 |
| June 29, 2018 | July 16, 2018 | $ 0.070 | 1,252 |
| July 31, 2018 | August 15, 2018 | $ 0.070 | 1,252 |
| August 31, 2018 | September 17, 2018 | $ 0.070 | 1,253 |
| | | | $ 11,316 |

## 17. EARNINGS PER SHARE

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

| | For the three months ended September 30, | | For the nine months ended September 30, | |
|---|---|---|---|---|
| | **2019** | 2018 | **2019** | 2018 |
| Weighted average number of common shares outstanding | **16,246,753** | 16,412,873 | **16,230,687** | 16,469,099 |
| Dilutive effect of options | **148,630** | 386,748 | **223,652** | 338,892 |
| Dilutive effect of restricted share units | **44,000** | 44,000 | **32,557** | 66,205 |
| Weighted average common shares outstanding for diluted earnings per share | **16,439,383** | 16,843,621 | **16,486,896** | 16,874,196 |
| Options excluded from calculation of diluted shares for the period due to their anti-dilutive effect | **1,634,950** | 950,000 | **1,300,000** | 950,000 |

## 18. RELATED PARTY TRANSACTIONS

a) The Company has no parent or other ultimate controlling party.
b) The Company's key management consists of the President & Chief Executive Officer, Chief Financial Officer and the Board of Directors. Key management compensation is as follows:

| | For the three months ended September 30, | | For the nine months ended September 30, | |
|---|---|---|---|---|
| | **2019** | 2018 | **2019** | 2018 |
| | | *($ thousands)* | | |
| Salaries, fees and other short-term employee benefits | **$ 446** | $ 396 | **$ 1,331** | $ 1,096 |
| Share-based compensation | **130** | 163 | **343** | 599 |
| Compensation expense of key management | **$ 576** | $ 559 | **$ 1,674** | $ 1,695 |

## 19. CASH FLOW SUPPLEMENTARY DISCLOSURE

| | For the three months ended September 30, | | | For the nine months ended September 30, | |
|---|---|---|---|---|---|
| | **2019** | 2018 | *Note* | **2019** | 2018 |
| | | | *($ thousands)* | | |
| **Non-cash transactions** | | | | | |
| Common shares issued on exercise of RSUs | **$ —** | $ — | | **$ 482** | $ 806 |
| **Interest paid** | **$ 7,149** | $ 5,929 | | **$ 20,945** | $ 15,556 |

| | For the three months ended September 30, 2019 | 2018 | Note | For the nine months ended September 30, 2019 | 2018 |
|---|---|---|---|---|---|
| | ($ thousands) | | | | |
| **Other non-cash items included in net income** | | | | | |
| Share-based compensation expense | **$ 172** | $ 233 | *15* | **$ 508** | $ 859 |
| Amortization of deferred financing costs | **911** | 765 | *10* | **2,490** | 1,965 |
| Financing costs - convertible debentures | **—** | — | | **—** | (29) |
| Unrealized (gain) loss on investments | **61** | — | | **(30)** | 151 |
| Interest expense - premises leases payable | **39** | — | *8* | **123** | — |
| Unrealized (gain) loss on interest rate derivatives | **82** | (256) | | **1,211** | (1,575) |
| Unrealized loss on foreign exchange | **75** | 58 | | **220** | 146 |
| | **$ 1,340** | $ 800 | | **$ 4,522** | $ 1,517 |
| **Change in other net operating assets** | | | | | |
| Restricted funds | **$ 6,485** | $ 2,069 | | **$ 1,360** | $ (3,015) |
| Other assets | **350** | 683 | | **1,903** | 4,250 |
| Accounts payable and other liabilities | **1,222** | 1,737 | | **(410)** | 396 |
| Customer security deposits | **(693)** | 356 | | **(3,111)** | 1,266 |
| | **$ 7,364** | $ 4,845 | | **$ (258)** | $ 2,897 |
| **Borrowings – continuing operations** | | | | | |
| Draw-downs or proceeds from borrowings | **$ 75,899** | $ 103,156 | *10* | **$ 285,767** | $ 366,038 |
| Payments - borrowings | **(63,392)** | (80,555) | *10* | **(209,795)** | (232,943) |
| | **$ 12,507** | $ 22,601 | | **$ 75,972** | $ 133,095 |

## 20. SEGMENT INFORMATION

Segments are identified on the same basis that is used internally to manage and to report on performance, taking into account materiality and the products and services of each segment and the organizational structure of the Company. The Company's operations consist of the following reportable segments: Equipment Financing - U.S. and Equipment Financing - Canada.

The Company's U.S. Equipment Financing business is located in the United States and is involved in small-ticket equipment leasing and lending to small and medium-sized businesses. Tandem and Windset's information is aggregated with Chesswood's U.S. Equipment Financing segment as both Pawnee, Tandem and Windset offer lending solutions to small businesses in the United States. Tandem and Windset continues to leverage off Pawnee's experience, processes and "back-office" support for credit adjudication, collections and documentation. The Canadian Equipment Financing segment provides commercial equipment financing to small and medium-sized businesses in Canada and includes Blue Chip.

Segment information is prepared in conformity with the accounting policies adopted for the Company's consolidated 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 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 consolidated 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:

| *($ thousands)* | Nine months ended September 30, 2019 | | | | |
|---|---|---|---|---|---|
| | **Equipment Financing - U.S.** | **Equipment Financing - Canada** | **Discontinued Operations** *(Note 5)* | **Corporate Overhead - Canada** | **Total** |
| Interest revenue on leases and loans | $ 71,711 | $ 10,344 | | $ — | $ 82,055 |
| Ancillary finance and other fee income | 8,496 | 3,399 | | 174 | 12,069 |
| Interest expense | (21,328) | (4,141) | | — | (25,469) |
| Provision for credit losses | (19,891) | (1,572) | | — | (21,463) |
| **Finance margin** | **38,988** | **8,030** | | **174** | **47,192** |
| Personnel expenses | 11,087 | 2,288 | | 1,448 | 14,823 |
| Share-based compensation expense | 137 | 10 | | 361 | 508 |
| Other expenses | 11,007 | 1,376 | | 1,142 | 13,525 |
| Depreciation - property and equipment | 760 | 95 | | 31 | 886 |
| Amortization - intangible assets | — | 999 | | — | 999 |
| **Operating income** | **15,997** | **3,262** | | **(2,808)** | **16,451** |
| Fair value adjustments - investments | — | — | | 30 | 30 |
| Unrealized loss on interest rate derivatives | (380) | — | | (831) | (1,211) |
| Unrealized loss on foreign exchange | — | — | | (220) | (220) |
| **Income before taxes** | **15,617** | **3,262** | | **(3,829)** | **15,050** |
| Tax expense | 3,154 | 845 | | 788 | 4,787 |
| **Income from continuing operations** | **12,463** | **2,417** | | **(4,617)** | **10,263** |
| Loss from discontinued operations | — | — | $ (321) | — | (321) |
| **Net income** | **$ 12,463** | **$ 2,417** | **$ (321)** | **$ (4,617)** | **$ 9,942** |
| Net cash used in operating activities | $ (58,802) | $ 6,021 | $ 230 | $ (2,564) | $ (55,115) |
| Net cash used in investing activities | $ (292) | $ (20) | $ — | $ — | $ (312) |
| Net cash from financing activities | $ 35,330 | $ (4,141) | $ — | $ 29,661 | $ 60,850 |
| Total assets | $ 662,227 | $ 204,527 | $ 1,243 | $ 5,613 | $ 873,610 |
| Total liabilities | $ 297,934 | $ 147,830 | $ — | $ 268,588 | $ 714,352 |
| Finance receivables | $ 617,855 | $ 165,510 | $ — | $ — | $ 783,365 |
| Goodwill and intangible assets | $ 21,394 | $ 36,765 | $ — | $ — | $ 58,159 |
| Property and equipment expenditures | $ 292 | $ 20 | $ — | $ — | $ 312 |

| | Nine Months Ended September 30, 2018 | | | | |
|---|---|---|---|---|---|
| *($ thousands)* | **Equipment Financing - U.S.** | **Equipment Financing - Canada** | **Discontinued Operations** *(Note 5)* | **Corporate Overhead - Canada** | **Total** |
| Interest revenue on leases and loans | $ 61,629 | $ 9,991 | | $ — | $ 71,620 |
| Ancillary finance and other fee income | 5,907 | 3,283 | | 285 | 9,475 |
| Interest expense | (15,018) | (3,663) | | — | (18,681) |
| Provision for credit losses | (12,203) | (1,492) | | — | (13,695) |
| **Finance margin** | **40,315** | **8,119** | | **285** | **48,719** |
| Personnel expenses | 8,453 | 1,945 | | 1,291 | 11,689 |
| Share-based compensation expense | 221 | 15 | | 623 | 859 |
| Other expenses | 7,729 | 1,187 | | 1,094 | 10,010 |
| Depreciation - property and equipment | 346 | 15 | | — | 361 |
| Amortization - intangible assets | — | 1,179 | | — | 1,179 |
| **Operating income** | **23,566** | **3,778** | | **(2,723)** | **24,621** |
| Fair value adjustments - convertible debentures and investments | — | — | | (122) | (122) |
| Unrealized gain on interest rate derivatives | 608 | — | | 967 | 1,575 |
| Unrealized loss on foreign exchange | — | — | | (146) | (146) |
| **Income before taxes** | **24,174** | **3,778** | | **(2,024)** | **25,928** |
| Tax expense | 5,102 | 986 | | 2,020 | 8,108 |
| **Income from continuing operations** | **19,072** | **2,792** | | **(4,044)** | **17,820** |
| Loss from discontinued operations | — | — | $ (212) | — | (212) |
| **Net income** | **$ 19,072** | **$ 2,792** | **$ (212)** | **$ (4,044)** | **$ 17,608** |
| Net cash used in operating activities | $ (78,271) | $ (18,269) | $ 1,197 | $ 631 | $ (94,712) |
| Net cash used in investing activities | $ (162) | $ — | $ — | $ — | $ (162) |
| Net cash from financing activities | $ 59,854 | $ 15,759 | $ — | $ 20,133 | $ 95,746 |
| Total assets | $ 546,357 | $ 209,793 | $ 2,069 | $ 8,091 | $ 766,310 |
| Total liabilities | $ 190,953 | $ 152,281 | $ — | $ 261,450 | $ 604,684 |
| Finance receivables | $ 509,362 | $ 170,422 | $ — | $ — | $ 679,784 |
| Goodwill and intangible assets | $ 20,913 | $ 38,095 | $ — | $ — | $ 59,008 |
| Property and equipment expenditures | $ 162 | $ — | $ — | $ — | $ 162 |

| | Three months ended September 30, 2019 | | | | |
|---|---|---|---|---|---|
| *($ thousands)* | Equipment Financing - U.S. | Equipment Financing - Canada | Discontinued Operations *(Note 5)* | Corporate Overhead - Canada | Total |
| Interest revenue on leases and loans | $ 24,277 | $ 3,431 | | $ — | $ 27,708 |
| Ancillary finance and other fee income | 2,873 | 1,151 | | 49 | 4,073 |
| Interest expense | (7,291) | (1,385) | | — | (8,676) |
| Provision for credit losses | (7,241) | (627) | | — | (7,868) |
| **Finance margin** | **12,618** | **2,570** | | **49** | **15,237** |
| Personnel expenses | 3,813 | 790 | | 480 | 5,083 |
| Share-based compensation expense | 34 | 3 | | 135 | 172 |
| Other expenses | 3,630 | 464 | | 499 | 4,593 |
| Depreciation - property and equipment | 256 | 32 | | 11 | 299 |
| Amortization - intangible assets | — | 333 | | — | 333 |
| **Operating income** | **4,885** | **948** | | **(1,076)** | **4,757** |
| Fair value adjustments - investments | — | — | | (61) | (61) |
| Unrealized loss on interest rate derivatives | (7) | — | | (75) | (82) |
| Unrealized loss on foreign exchange | — | — | | (75) | (75) |
| **Income before taxes** | **4,878** | **948** | | **(1,287)** | **4,539** |
| Tax expense | 995 | 236 | | 290 | 1,521 |
| Income from continuing operations | **3,883** | **712** | | **(1,577)** | **3,018** |
| Loss from discontinued operations | — | — | $ (41) | — | (41) |
| **Net income** | **$ 3,883** | **$ 712** | **$ (41)** | **$ (1,577)** | **$ 2,977** |
| Net cash used in operating activities | $ (11,300) | $ 6,065 | $ 138 | $ (23) | $ (5,120) |
| Net cash used in investing activities | $ (22) | $ (6) | $ — | $ — | $ (28) |
| Net cash from financing activities | $ (1,907) | $ (3,755) | $ — | $ 11,946 | $ 6,284 |
| Property and equipment expenditures | $ 22 | $ 6 | $ — | $ — | $ 28 |

| *($ thousands)* | Three months ended September 30, 2018<br>Equipment Financing - U.S. | Equipment Financing - Canada | Discontinued Operations *(Note 5)* | Corporate Overhead - Canada | Total |
|---|---|---|---|---|---|
| Interest revenue on leases and loans | $ 22,133 | $ 3,489 | | $ — | $ 25,622 |
| Ancillary finance and other fee income | 2,092 | 1,103 | | 81 | 3,276 |
| Interest expense | (5,879) | (1,334) | | — | (7,213) |
| Provision for credit losses | (3,545) | (566) | | — | (4,111) |
| **Finance margin** | **14,801** | **2,692** | | **81** | **17,574** |
| Personnel expenses | 3,065 | 665 | | 447 | 4,177 |
| Share-based compensation expense | 67 | (5) | | 171 | 233 |
| Other expenses | 2,742 | 441 | | 441 | 3,624 |
| Depreciation - property and equipment | 121 | 4 | | — | 125 |
| Amortization - intangible assets | — | 333 | | — | 333 |
| **Operating income** | **8,806** | **1,254** | | **(978)** | **9,082** |
| Unrealized gain on interest rate derivatives | 98 | — | | 158 | 256 |
| Unrealized loss on foreign exchange | — | — | | (58) | (58) |
| **Income before taxes** | **8,904** | **1,254** | | **(878)** | **9,280** |
| Tax expense | 1,960 | 322 | | 725 | 3,007 |
| Income from continuing operations | **6,944** | **932** | | **(1,603)** | **6,273** |
| Loss from discontinued operations | — | — | $ (181) | — | (181) |
| **Net income** | **$ 6,944** | **$ 932** | **$ (181)** | **$ (1,603)** | **$ 6,092** |
| Net cash used in operating activities | $ (14,460) | $ (19) | $ 352 | $ 144 | $ (13,983) |
| Net cash used in investing activities | $ (56) | $ — | $ — | $ — | $ (56) |
| Net cash from financing activities | $ 13,680 | $ (2,211) | $ — | $ 5,311 | $ 16,780 |
| Property and equipment expenditures | $ 56 | $ — | $ — | $ — | $ 56 |

## 21. SUBSEQUENT EVENTS

Subsequent to September 30, 2019, the Company announced the renewals of two US$250 million borrowing facilities. Chesswood revolving credit facility maturity was extended from December 2020 to December 2022 and now includes a US$50 million accordion feature that can increase the overall revolver to US$300 million. The maturity of Pawnee's US$250 million revolving warehouse loan facility was extended from August 2020 to September 2021 and expires on September 2024.

In October 2019, Pawnee completed a US$254 million asset-backed securitization which has fixed term and fixed interest rate, and is collateralized by receivables from Pawnee's portfolio of equipment leases and loans. The securitization has an approximate cost of funds, including fees and legal costs, of 3.65% per annum. Proceeds from the securitization were used to pay down Pawnee's warehouse line and Chesswood's senior revolving credit facility.

# Chesswood Group Limited

## DIRECTORS, OFFICERS AND OTHER INFORMATION

**Directors**

**Frederick W. Steiner**
Director, Chairman of Chesswood Group Limited

**Samuel Leeper**
Director , Chairman, Audit and Governance Committee
*Former C.E.O., Pawnee Leasing Corporation*

**Clare Copeland**
Director, Chairman, Compensation Committee
*C.E.O., Falls Management Company*

**David Obront**
Director
*President, Carpool Two Ltd.*

**Robert Day**
Director
*Former Chairman, Pawnee Leasing Corporation*

**Barry Shafran**
Director
*President & C.E.O., Chesswood Group Limited*

**Executive Team**

**Barry Shafran**
*President & C.E.O.*

**Lisa Stevenson**
*Chief Financial Officer*

**Other Information**
**Auditors**
*BDO Canada LLP*

**Transfer Agent**
*TSX Trust Company*

**Corporate Counsel**
*McCarthy Tétrault LLP*

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