Interim Consolidated

Financial Statements

Second Quarter
June 30, 2020

CANADA'S PREMIER NON-BANK LENDER™

INTERIM CONSOLIDATED STATEMENTS OF FINANCIAL POSITION (UNAUDITED)

(in thousands of Canadian dollars)

	Notes	June 30 2020	December 31 2019
Assets			
Mortgages receivable	5	$ 675,339	$ 727,325
Investment properties	6	16,201	16,201
Prepaid expenses		165	105
Total assets		$ 691,705	$ 743,631
Liabilities			
Borrowings under credit facility	7	$ 97,490	$ 123,449
Accounts payable and accrued liabilities	8, 12	2,333	4,144
Accrued convertible debenture interest		956	956
Dividends payable		3,179	5,652
Convertible debentures	9	124,679	153,910
Total liabilities		228,637	288,111
Shareholders' equity			
Share capital		459,747	452,851
Deferred share incentive plan units		788	716
Equity component of convertible debentures		1,470	1,837
Contributed surplus		1,083	781
Deficit		(20)	(665)
Total shareholders' equity		463,068	455,520
Total liabilities and shareholders' equity		$ 691,705	$ 743,631
Commitments	*7, 14(d)*		

The accompanying notes are an integral part of these interim consolidated financial statements.

Approved on behalf of the board of directors:

"Robert Goodall"	*"Mark Silver"*
Robert Goodall, Director	Mark Silver, Director

INTERIM CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY (UNAUDITED)

(in thousands of Canadian dollars, except for number of common shares)

	Notes	Share capital Number	Share capital Amount	Deferred share incentive plan units	Equity component of convertible debentures	Contributed surplus	Retained earnings (deficit)	Total shareholders' equity
Balance, December 31, 2018		36,561,198	$ 385,261	$ 644	$ 1,675	$ 645	$ (919)	$ 387,306
Shares issued by prospectus	10	2,645,000	34,517	–	–	–	–	34,517
Shares issued under dividend reinvestment plan	10	163,881	2,133	–	–	–	–	2,133
Shares issued under employee share purchase plan	10	5,467	73	–	–	–	–	73
Shares issued on debenture conversion	9	74,659	995	–	(5)	–	–	990
Maturity of convertible debentures	9	–	–	–	(136)	136	–	–
Issue costs		–	(1,589)	–	–	–	–	(1,589)
Share-based payments	11	–	–	158	–	–	–	158
Equity component of convertible debentures issued	9	–	–	–	351	–	–	351
Issue costs attributable to equity component of convertible debentures issued	9	–	–	–	(17)	–	–	(17)
Net income and comprehensive income		–	–	–	–	–	18,902	18,902
Dividends declared		–	–	–	–	–	(17,518)	(17,518)
Balance, June 30, 2019		39,450,205	$ 421,390	$ 802	$ 1,868	$ 781	$ 465	$ 425,306
Shares issued by prospectus	10	2,034,300	27,260	–	–	–	–	27,260
Shares issued under dividend reinvestment plan	10	162,995	2,203	–	–	–	–	2,203
Shares issued under employee share purchase plan	10	5,053	72	–	–	–	–	72
Shares issued under deferred share incentive plan	11	19,669	248	(248)	–	–	–	–
Shares issued on debenture conversion	9	191,554	2,599	–	(31)	–	–	2,568
Issue costs		–	(921)	–	–	–	–	(921)
Share-based payments	11	–	–	162	–	–	–	162
Net income and comprehensive income		–	–	–	–	–	19,666	19,666
Dividends declared		–	–	–	–	–	(20,796)	(20,796)
Balance, December 31, 2019		41,863,776	$ 452,851	$ 716	$ 1,837	$ 781	$ (665)	$ 455,520
Shares issued under dividend reinvestment plan	10	140,436	1,731	–	–	–	–	1,731
Shares issued under employee share purchase plan	10	9,658	93	–	–	–	–	93
Shares issued under deferred share incentive plan	11	7,426	93	(93)	–	–	–	–
Shares issued on debenture conversion	9	365,700	4,979	–	(65)	–	–	4,914
Maturity of convertible debentures	9	–	–	–	(302)	302	–	–
Share-based payments	11	–	–	165	–	–	–	165
Net income and comprehensive income		–	–	–	–	–	19,685	19,685
Dividends declared		–	–	–	–	–	(19,040)	(19,040)
Balance, June 30, 2020		42,386,996	$ 459,747	$ 788	$ 1,470	$ 1,083	$ (20)	$ 463,068

Dividends amounted to $0.45 per share for the six months ended June 30, 2020 (six months ended June 30, 2019 – $0.45; year ended December 31, 2019 – $0.96).

The accompanying notes are an integral part of these interim consolidated financial statements.

INTERIM CONSOLIDATED STATEMENTS OF INCOME AND COMPREHENSIVE INCOME (UNAUDITED)

(in thousands of Canadian dollars, except for per share amounts)

	Notes	Three months ended June 30 2020	Three months ended June 30 2019	Six months ended June 30 2020	Six months ended June 30 2019
Revenues					
Mortgage interest and fees	8	$ 16,098	$ 16,667	$ 32,978	$ 32,463
Rental income (loss)	6	143	(102)	320	(120)
Total revenues		16,241	16,565	33,298	32,343
Operating expenses					
Mortgage servicing and management fees	8	1,700	1,757	3,477	3,437
Transfer agent, regulatory fees and investor relations		71	61	160	130
Share-based payments	8, 11	81	78	165	158
Professional fees		57	50	113	90
Directors' expense	8, 12	63	52	134	101
Administration and general		44	24	93	55
Adjustment to fair value of deferred share units	8, 12	19	–	19	–
Provision for mortgage losses	5(b)	1,000	400	2,000	800
Total operating expenses		3,035	2,422	6,161	4,771
Income before financing costs		13,206	14,143	27,137	27,572
Financing costs					
Interest on convertible debentures	9	2,222	2,565	4,653	5,173
Interest and other financing charges	7	1,163	1,911	2,799	3,497
Total financing costs		3,385	4,476	7,452	8,670
Net income and comprehensive income for the period		$ 9,821	$ 9,667	$ 19,685	$ 18,902
Earnings per common share					
Basic	13	$ 0.23	$ 0.25	$ 0.47	$ 0.49
Diluted	13	$ 0.23	$ 0.24	$ 0.47	$ 0.48

The accompanying notes are an integral part of these interim consolidated financial statements.

INTERIM CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)

(in thousands of Canadian dollars)

	Three months ended June 30		Six months ended June 30	
	2020	**2019**	**2020**	**2019**
Cash provided by (used in):				
Operating activities				
Net income and comprehensive income for the period	$ 9,821	$ 9,667	$ 19,685	$ 18,902
Adjustments to determine net cash flows provided by (used in) operating activities				
Share-based payments	81	78	165	158
Mortgage interest and fees earned	(16,098)	(16,667)	(32,978)	(32,463)
Mortgage interest and fees received	22,846	12,985	38,989	23,944
Interest on convertible debentures expensed	2,222	2,565	4,653	5,173
Interest and other financing charges expensed	1,163	1,911	2,799	3,497
Adjustment to fair value of deferred share units	19	–	19	–
Provision for mortgage losses	1,000	400	2,000	800
Changes in operating assets and liabilities				
Prepaid expenses	58	(81)	(60)	(179)
Accounts payable and accrued liabilities	(73)	(144)	(1,863)	(612)
Additions to mortgage discount	–	–	–	46
Additions to unamortized origination fees	33	251	265	422
Cash provided by operating activities	21,072	10,965	33,674	19,688
Investing activities				
Cash advances of mortgages receivable	(15,950)	(76,616)	(97,103)	(130,335)
Cash repayments of mortgages receivable	75,900	51,893	140,813	86,455
Cash provided by (used in) investing activities	59,950	(24,723)	43,710	(43,880)
Financing activities				
Advances under credit facility	155,247	121,744	289,371	207,970
Repayments under credit facility	(199,175)	(100,950)	(315,615)	(193,540)
Interest and fees on convertible debentures paid	(2,070)	(1,112)	(3,993)	(2,016)
Interest and other bank charges paid	(968)	(1,747)	(2,481)	(3,694)
Issuance of common shares	49	35	93	34,589
Share capital issue costs	–	–	–	(1,589)
Issuance of convertible debentures	–	3,750	–	28,750
Convertible debenture issue costs	–	(164)	–	(1,369)
Repayment of convertible debentures	(24,977)	–	(24,977)	(28,278)
Cash dividends paid	(9,128)	(7,798)	(19,782)	(16,631)
Cash provided by (used in) financing activities	(81,022)	13,758	(77,384)	24,192
Increase (decrease) in cash	–	–	–	–
Cash, beginning of period	–	–	–	–
Cash, end of period	$ –	$ –	$ –	$ –

The accompanying notes are an integral part of these interim consolidated financial statements.

NOTE 1 – NATURE OF OPERATIONS

Atrium Mortgage Investment Corporation (the "company") is a corporation domiciled in Canada, incorporated under the *Ontario Business Corporations Act*. The address of the company's registered head office and principal place of business is Suite 900, 20 Adelaide Street East, Toronto, Ontario M5C 2T6.

The company is a Mortgage Investment Corporation (MIC) as defined in Section 130.1(6) of the Canada *Income Tax Act* (ITA). Accordingly, the company is not taxed on income provided that its taxable income is paid to its shareholders in the form of dividends within 90 days after December 31 each year. Such dividends are generally treated by shareholders as interest income, so that each shareholder is in the same position as if the mortgage investments made by the company had been made directly by the shareholder.

The company's common shares are listed on the Toronto Stock Exchange (TSX) under the symbol AI and its convertible debentures are listed under the symbols AI.DB.B, AI.DB.C, AI.DB.D and AI.DB.E.

NOTE 2 – BASIS OF PRESENTATION

(a) Statement of compliance

These interim consolidated financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS) and follow International Accounting Standard 34 *Interim Financial Reporting* (IAS 34) as issued by the International Accounting Standards Board (IASB) as set out in Part I of the *CPA Canada Handbook – Accounting*. These interim consolidated financial statements should be read in conjunction with the company's audited consolidated financial statements for the year ended December 31, 2019. Significant accounting policies have been consistently applied in the preparation of these interim consolidated financial statements, which were authorized for issuance by the board of directors on July 29, 2020.

(b) Basis of measurement

These interim consolidated financial statements are prepared on the historical cost basis.

(c) Functional and presentation currency

These interim consolidated financial statements are presented in Canadian dollars, which is also the company's functional currency. Dollars are expressed in thousands except for per share amounts or where the context requires otherwise.

(d) Principles of consolidation

These interim consolidated financial statements include the accounts of the company and Canadian Properties LP, which is considered to be a subsidiary for financial reporting purposes. Consolidation commenced the date the company obtained control and continues until control ceases. The company has consolidated the subsidiary from August 5, 2016, the date of its formation. All transactions and balances between the company and the subsidiary have been eliminated, including unrealized gains and losses, if any.

NOTE 2 – BASIS OF PRESENTATION (continued)

(e) Use of estimates and judgements

The preparation of interim consolidated financial statements in accordance with IFRS requires management to make estimates, assumptions and judgements that affect the reported amounts of assets and liabilities and disclosure of contingent assets and contingent liabilities at the reporting date and the reported amounts of revenues and expenses during the reporting period.

The most subjective of these estimates relate to:

(a) determining whether the cash flows from the mortgages receivable represent solely payments of principal and interest (SPPI);

(b) the measurement of impairment losses for mortgages receivable, in particular: measurement of credit risk to determine whether there has been a significant increase in credit risk since initial recognition; the assessment of when mortgages receivable become impaired and the incorporation of forward-looking information to determine expected credit losses;

(c) the measurement of fair value, costs of disposal and the value in use of investment properties; and

(d) the measurement of the liability and equity components of the convertible debentures which depend upon the estimated market interest rates for a comparable debenture without the convertibility feature.

Management believes that its estimates are appropriate; however, actual results could differ from the amounts estimated. Estimates and underlying assumptions are reviewed each quarter. Revisions to accounting estimates are recognized in the period in which the estimate is revised and in any future periods affected.

In March 2020, the World Health Organization characterized the outbreak of a strain of the novel coronavirus (“COVID-19”) as a pandemic which resulted in a series of public health and emergency measures being put in place to combat the spread of the virus. These measures have caused material disruption to businesses in Canada and globally resulting in an economic slowdown. The duration and impact of COVID-19 continues to be unknown and it is not possible to reliably estimate the impact that the length and severity of these developments will have on the financial results and condition of the company in future periods. To date, the company has not experienced material changes in the collection of interest and repayments of principal, however, there is no certainty this will continue going forward.

Accordingly, there is inherently more uncertainty associated with the estimates, judgements and assumptions made by management in the preparation of the interim consolidated financial statements. It is not possible to forecast with certainty the extent to which the economic impact of COVID-19 will affect the company’s operations and financial results in the near term and long-term. Areas of the company’s business that could potentially be adversely impacted include, but are not limited to, mortgage interest rates, mortgage interest and fees revenue, rental income, provision for mortgage losses and valuation of investment properties.

NOTE 3 – SIGNIFICANT ACCOUNTING POLICIES

(a) Financial instrument assets – initial recognition and measurement

Financial instrument assets are initially recognized when the company becomes a party to a contract. On initial recognition, the measurement category is determined, based on: (i) the business model under which the asset is held, and (ii) the contractual cash flow characteristics of the instrument.

Upon initial recognition, financial assets are measured as either:

- Fair value through profit and loss (FVTPL) – which is the required measurement classification for instruments that are held for trading and derivative assets;
- Amortized cost – if the instrument is held within a business model whose objective is to collect contractual cash flows and the cash flows represent SPPI;
- Fair value through other comprehensive income (FVOCI) – which is required for debt instruments held in a dual-purpose business model, to collect contractual cash flows and to sell the instruments and can be irrevocably elected at initial recognition provided they have not been designated as FVTPL and are not held for trading; or
- Designated as FVTPL – available on initial recognition provided certain criteria are met.

NOTE 3 – SIGNIFICANT ACCOUNTING POLICIES (continued)

(a) Financial instrument assets – initial recognition and measurement (continued)

All of the company's mortgages receivable are held in a single business model. The company has concluded that its business model is to hold mortgages receivable to collect contractual cash flows for the following reasons:

- The performance of the mortgage portfolio is assessed on the basis of effective yield, and not on a fair value basis, whether realized or unrealized.
- Neither key management compensation nor remuneration paid to the company's manager is based on the fair values of mortgages receivable.
- Historically the company has not sold, and in the future has no expectations to sell, any of its mortgages receivable. While the company may decrease its interest in a syndicated mortgage receivable by transferring its interest, at its amortized cost carrying amount, to another lender in the syndicate, such transfers are consistent with the business model of holding mortgages receivable to collect contractual cash flows.

The returns earned by the company on its mortgages receivable are interest rates that are set at levels to provide an acceptable profit margin based on the time value of money and credit risk, although other basic lending risks (for example, the location and quality of the underlying collateral) may also be built-in. There are no factors that give rise to variation in the return on the company's mortgages receivable other than the time value of money, credit risk and other basic lending risks. Interest rates, or the credit spread for variable rate mortgages, are set for the full term of the loan, which is considered SPPI because the rate is still based on the time value of money and credit risk. The majority of the mortgages receivable can be prepaid after an initial closed period with no penalty, subject to the borrower providing advance written notice according to the terms of their mortgage so the return therefore represents SPPI.

Mortgages receivable are initially recognized at fair value and are subsequently carried at amortized cost using the effective interest method. See Note 3(d) Financial instruments – revenue recognition.

(b) Financial instrument liabilities – initial recognition and measurement

Financial liabilities are measured as either:

- FVTPL – which is required for any financial instrument liabilities that are held for trading and for derivative liabilities;
- Designated as FVTPL – available on initial recognition if either: the instrument includes one or more embedded derivatives and the host contract is not a financial asset; or if the designation meets certain criteria;
- Designated as at fair value – if the instrument does not meet the criteria and is designated as at FVTPL and is not otherwise required to be measured as FVTPL, it can still be irrevocably designated at initial recognition as at fair value, meaning that changes in fair value related to changes in own credit risk are presented in other comprehensive income and other changes in fair value are presented in net income; or
- Amortized cost – which is the default category and is also used for any host contract that is a financial instrument liability.

The company's borrowings under credit facility, accounts payable and accrued liabilities, except for the liability for the deferred share unit plan, dividends payable, accrued convertible debenture interest and the liability component of convertible debentures are measured at amortized cost. These financial instrument liabilities are initially recognized at fair value and are subsequently measured at amortized cost using the effective interest method. The liability for the deferred share unit plan is measured at FVTPL. This financial instrument liability is initially and subsequently measured at fair value. Gains and losses arising from changes in fair value are recorded in net income and comprehensive income in the period in which they arise.

(c) Financial instruments – impairment of assets

Loan commitments and letters of credit (collectively commitments) and mortgages receivable are assessed for impairment at the end of each reporting period using an expected credit loss (ECL) model. The ECL model uses a three-stage impairment approach based on changes in the credit risk of the commitment or mortgage receivable since initial recognition. The three stages are as follows:

NOTE 3 – SIGNIFICANT ACCOUNTING POLICIES (continued)

(c) Financial instruments – impairment of assets (continued)

Credit stage and financial assets included	Impairment loss recognized
Stage 1 – commitments and mortgages receivable on initial recognition and existing assets that have not shown a significant increase in credit risk since initial recognition	12-month ECL – portion of lifetime ECLs that represent the ECL from possible default events within the next 12 months
Stage 2 – commitments and mortgages receivable that have experienced a significant increase in credit risk since initial recognition and up to the date of approval of the interim consolidated financial statements	Lifetime ECL – expected losses from possible default events over the expected life of the instrument, weighted by the likelihood of loss
Stage 3 – impaired commitments and mortgages receivable for which there is objective evidence of impairment at the date of approval of the interim consolidated financial statements	Lifetime ECL – expected losses from possible default events over the expected life of the instrument, weighted by the likelihood of loss

Credit quality is assessed at each reporting period and results in commitments and mortgages receivable being moved between stages, as necessary. Significant judgement is required when assessing evidence of credit impairment and estimating expected credit losses.

For commitments and mortgages receivable, the company considers a number of past events, current conditions and forward-looking information when assessing if there has been a significant increase or subsequent decrease in credit risk. There is a presumption in IFRS 9 *Financial Instruments* (IFRS 9) that credit risk has increased significantly once payments are 30 days past due. However, for single-family residential mortgages receivable, the company's historical experience is that mortgages receivable can become 30 days past due, but be brought up to date by the borrower, therefore another additional risk factor also needs to be identified for the mortgages receivable to move to Stage 2. For single-family residential mortgages receivable that are not 30 days past due, a significant increase in credit risk may still be evidenced by the presence of one or more additional risk factors. For all other mortgages receivable, a significant increase in credit risk is considered to have occurred if payments are 30 days past due or if one or more additional risk factors is present.

The additional risk factors used in assessing credit risk include:

- changes in the financial condition of the borrower;
- responsiveness of the borrower;
- other borrower specific information that may be available, without consideration of collateral;
- current economic conditions: interest rates, housing prices, real estate market statistics and employment statistics; and
- supportable forward-looking information: macro-economic factors, such as forecast real estate values and interest rate forecasts.

Determining whether there has been a significant increase in credit risk since initial recognition, or a subsequent reduction in credit risk back to the level at initial recognition, requires the exercise of significant judgement.

The company considers a commitment or mortgage receivable to be impaired when there is objective evidence that one or more events have occurred that have an unfavourable impact on estimated future cash flows such that there is no longer reasonable assurance as to the timely collection of the full amount of principal and interest.

The company considers a commitment or mortgage receivable to be in default if payments are greater than 90 days past due for single-family residential mortgages receivable or 30 days past due for all other mortgages receivable, or if an event of default has occurred under the terms of the mortgage commitment, including: non-payment of property taxes, a material adverse change in the financial position of the borrower and/or guarantors or a material adverse change in the property given as security. These definitions are consistent with industry practice.

An ECL represents the difference between the present value of all contractual cash flows that are due under the original terms of the contract and the present value of all cash flows expected to be received. The company's application of the concept uses three inputs to measure ECLs for commitments and mortgages receivable classified as Stage 1: probability of default (PD), loss given default (LGD) and exposure at default (EAD). These inputs are determined at each reporting period using historical data and current conditions.

NOTE 3 – SIGNIFICANT ACCOUNTING POLICIES (continued)

(c) Financial instruments – impairment of assets (continued)

Adjustments may be made to the probability of default if the effects of, for example, forecasts of housing prices, employment and interest rates, are expected to be significantly different over the term of the mortgage. The inputs for Stage 1 mortgages receivable are calculated separately for (i) single-family residential mortgages receivable and (ii) mortgages receivable on all other properties on the basis of differences in the credit risk of each. The ECL is assessed individually for each commitment and mortgage receivable classified as either Stage 2 or Stage 3. For mortgages receivable in these stages, forecast future information specific to the loan (for example, forecasts of real estate prices) is incorporated when assessing the cash flows expected to be received. In response to COVID-19, the ECL methodology was modified to include a post-model overlay adjustment to account for the uncertainty and difficulty in forecasting future economic conditions.

Mortgages receivable are presented on the interim consolidated statements of financial position net of the provision for mortgage losses. A loss on a mortgage receivable is written off against the related provision for mortgage losses when there is no reasonable expectation of further recovery, which is the point at which the underlying real property has been liquidated and claims against guarantors, if any, are unlikely to recover any further losses. For any mortgages receivable that have been written off but where guarantors are still being pursued for collection, no recovery is recognized until virtually certain of collection.

(d) Financial instruments - revenue recognition

Mortgage interest and fees revenues are recognized in the interim consolidated statements of income and comprehensive income using the effective interest method. Mortgage interest and fees revenues include the company's share of any fees received, as well as the effect of any discount or premium on the mortgage. Interest revenue is calculated on the gross carrying amount for mortgages receivable in Stages 1 and 2 and on the net carrying amount for mortgages receivable in Stage 3 (see Note 3(c) Financial instruments – impairment of assets).

The effective interest method derives the interest rate that discounts the estimated future cash receipts during the expected life of the mortgage receivable (which is the contractual life, if a shorter period is not expected) to its carrying amount. When calculating the effective interest rate, future cash flows are estimated considering all contractual terms of the financial instrument, but not future credit losses (see Note 3(c) Financial instruments – impairment of assets). The calculation of the effective interest rate includes all fees and transaction costs paid or received. Fees and transaction costs include incremental revenues and costs that are directly attributable to the acquisition or issuance of the mortgage.

(e) Financial instruments – derecognition

Financial assets are derecognized when the contractual rights to receive cash flows from the asset expire. When the company exercises its security and takes title to the underlying real estate, a mortgage receivable is derecognized on the date of foreclosure.

Financial liabilities are derecognized when the obligation under the liability is discharged, cancelled, or expires.

(f) Investment properties

Investment properties are properties over which the company has taken title through exercise of its security interest. Such properties are accounted for under IAS 40 *Investment Property*. An investment property is recognized on the date of acquisition through foreclosure and is measured initially at cost, which is the book value of the respective mortgage receivable net of any related provision for mortgage losses, plus any directly attributable expenditures and transaction costs. Any costs subsequently incurred to complete the construction or development of a property are capitalized. After initial recognition, investment properties are measured using the cost model. Depreciation commences from the date the property is substantially complete and is recognized when the property's carrying amount exceeds its residual value. The carrying value of investment properties are assessed for impairment whenever events or changes in circumstances indicate that the carrying amount of the investment property may exceed its recoverable amount.

NOTE 3 – SIGNIFICANT ACCOUNTING POLICIES (continued)

(f) Investment properties (continued)

If the higher of the fair value less cost of disposal and the value in use of an investment property (its recoverable amount) is less than its carrying amount, then an impairment loss is recognized for the excess. Any impairment loss, or gain or loss realized on disposal is recognized in the interim consolidated statements of income and comprehensive income.

(g) Convertible debentures

Convertible debentures can be converted into common shares of the company at the option of the investor. They are compound financial instruments with two components: a financial liability, and a call option which is an equity instrument. The fair value of the liability component is measured as of the date that the convertible debentures were issued, and the equity instrument is valued on that date based upon the difference between the fair value of the convertible debenture and the fair value of the liability component. The measurement of the fair value of the liability component is based upon market rates of interest on similar debt instruments without the conversion feature. Expenses of issue are allocated between the two components on a pro-rata basis. The book value of the debt is accreted up to its face value over the life of the financial liability using the effective interest method, which applies a constant interest rate over the term of the debt. The value of the equity component is not remeasured subsequent to its initial measurement date.

(h) Income taxes

The company qualifies as a MIC under the ITA, and as such is not taxed on income provided that its taxable income is distributed to its shareholders in the form of dividends within 90 days after December 31 each year. It is the company's policy to pay such dividends to remain non-taxable. Accordingly, no provision for current or deferred income taxes is required.

(i) Earnings per common share

Basic earnings per common share is calculated by dividing earnings during the period by the weighted average number of common shares outstanding during the period. Diluted earnings per share is calculated by adjusting the income and comprehensive income attributable to common shareholders and the weighted average number of common shares outstanding for the effects of all dilutive items such as convertible debentures and deferred share incentive plans.

(j) Share-based payments

The company has an equity-settled share-based compensation plan for grants to eligible directors, officers, and senior management under its deferred share incentive plan. Grants are measured based upon the fair value of the awards granted, using the volume-weighted average trading share price for the five trading days prior to the date of the grant.

(k) Deferred share unit plan

The company has a cash-settled deferred share unit plan for non-executive directors pursuant to which each non-executive director is required to receive one-half of their director compensation in the form of deferred share units. Each non-executive director can elect to receive the remaining one-half of their director compensation in deferred share units or cash or a combination thereof. The deferred share units represent a financial liability as they can only be settled in cash when the non-executive directors cease to serve in any capacity with the company. As such, the deferred share units are initially recognized at their fair value, using the volume-weighted average trading price of the company's common shares on the TSX for the five trading days prior to the last day of the quarter, as directors' expense with a corresponding amount recorded in accounts payable and accrued liabilities. The liability is subsequently remeasured to its fair value at each quarter end with the change in fair value during the period recognized as an operating expense.

NOTE 4 – RECENT ACCOUNTING PRONOUNCEMENTS

Various pronouncements have been issued by the IASB or IFRS Interpretations Committee (IFRIC) that will be effective for future accounting periods. The company closely monitors new accounting standards as well as amendments to existing standards and assesses what impact, if any, they will have on the interim consolidated financial statements. None of the standards issued to date are expected to have a material effect on the interim consolidated financial statements.

NOTE 5 – MORTGAGES RECEIVABLE

(a) Mortgage portfolio

	June 30, 2020			December 31, 2019		
Property type	**Number**	**Outstanding amount**	**% of Portfolio**	**Number**	**Outstanding amount**	**% of Portfolio**
Low-rise residential	28	$ 190,639	28.0%	32	$ 216,144	29.6%
High-rise residential	17	170,270	25.0%	15	174,544	23.9%
Mid-rise residential	20	142,668	21.0%	21	160,456	22.0%
House and apartment	74	49,618	7.3%	91	66,083	9.1%
Condominium corporation	14	2,461	0.4%	14	2,659	0.4%
Residential portfolio	153	555,656	81.7%	173	619,886	85.0%
Commercial	20	124,299	18.3%	19	109,859	15.0%
Mortgage portfolio	173	679,955	100.0%	192	729,745	100.0%
Accrued interest receivable		3,331			3,780	
Mortgage discount		(202)			(224)	
Unamortized origination fees		(355)			(586)	
Provision for mortgage losses		(7,390)			(5,390)	
Mortgages receivable		$ 675,339			$ 727,325	

The mortgage portfolio has maturity dates between 2020 and 2030 with a weighted average remaining term of 8.3 months at June 30, 2020 (December 31, 2019 – 8.7 months). The portfolio has a weighted average interest rate (which excludes lender fees earned by the company) of 8.55% as at June 30, 2020 (8.81% as at December 31, 2019, 8.81% as at June 30, 2019).

Within the mortgage portfolio, at June 30, 2020 there were 25 mortgages receivable aggregating to $129,618 (19.1% of the mortgage portfolio) in which the company has a subordinate position in a syndicated mortgage receivable (December 31, 2019 – 24 mortgages receivable aggregating $108,055, 14.8% of the mortgage portfolio). Additional analysis of the mortgage portfolio, including by location of underlying property and type of mortgage, is set out in the "Investment Portfolio" section of the Management's Discussion and Analysis for the three and six month period ended June 30, 2020.

A majority of the mortgages receivable have an initial closed period, after which the borrower may repay the principal at any time prior to maturity, without penalty, subject to providing advance written notice according to the terms of their mortgage.

Principal repayments based on contractual maturity dates are as follows:

Six months ending December 31, 2020	333,099	49.0%
Years ending December 31, 2021	260,430	38.3%
2022	67,678	10.0%
2023	16,650	2.4%
2024	811	0.1%
Thereafter	1,287	0.2%
	$ 679,955	100.0%

NOTE 5 – MORTGAGES RECEIVABLE (continued)

(b) Provision for mortgage losses

The gross carrying amounts of mortgages receivable and the provision for mortgage losses by property type are as follows:

As at June 30, 2020

Gross carrying amount	Stage 1	Stage 2	Stage 3	Total
Low-rise residential	$ 169,794	$ 20,845	$ –	$ 190,639
High-rise residential	170,270	–	–	170,270
Mid-rise residential	142,668	–	–	142,668
House and apartment	41,750	7,868	–	49,618
Condominium corporation	2,461	–	–	2,461
Commercial	119,870	–	4,429	124,299
Mortgage portfolio	$ 646,813	$ 28,713	$ 4,429	$ 679,955

Provision for mortgage losses	Stage 1	Stage 2	Stage 3	Total
Low-rise residential	$ 1,767	$ 122	$ –	$ 1,889
High-rise residential	1,801	–	–	1,801
Mid-rise residential	1,993	–	–	1,993
House and apartment	367	36	–	403
Condominium corporation	14	–	–	14
Commercial	944	–	346	1,290
Mortgage portfolio	$ 6,886	$ 158	$ 346	$ 7,390

As at December 31, 2019

Gross carrying amount	Stage 1	Stage 2	Stage 3	Total
Low-rise residential	$ 200,928	$ 15,216	$ –	$ 216,144
High-rise residential	174,544	–	–	174,544
Mid-rise residential	160,456	–	–	160,456
House and apartment	65,154	929	–	66,083
Condominium corporation	2,659	–	–	2,659
Commercial	105,554	4,305	–	109,859
Mortgage portfolio	$ 709,295	$ 20,450	$ –	$ 729,745

Provision for mortgage losses	Stage 1	Stage 2	Stage 3	Total
Low-rise residential	$ 1,398	$ 317	$ –	$ 1,715
High-rise residential	1,214	–	–	1,214
Mid-rise residential	1,116	–	–	1,116
House and apartment	251	–	–	251
Condominium corporation	18	–	–	18
Commercial	734	342	–	1,076
Mortgage portfolio	$ 4,731	$ 659	$ –	$ 5,390

The provision for mortgage losses at June 30, 2020 is $7,390 (December 31, 2019 – $5,390). Of this provision, $6,886 (December 31, 2019 – $4,731) represents management's estimate of the ECLs on mortgages receivable in the company's portfolio that have not experienced a significant increase in credit risk since initial recognition (Stage 1). The ECL was assessed individually for each mortgage receivable and commitment classified as Stages 2 and 3 and management estimated the ECL as $158 for mortgages receivable classified as Stage 2 and $346 for those classified as Stage 3 at June 30, 2020 (December 31, 2019 – $659 and $nil).

NOTE 5 – MORTGAGES RECEIVABLE (continued)

(b) Provision for mortgage losses (continued)

The changes in the provision for mortgage losses are shown in the following table:

	Six months ended June 30, 2020			
	Stage 1	Stage 2	Stage 3	Total
Opening balance, January 1, 2020	$ 4,731	$ 659	$ –	$ 5,390
Provision for mortgage losses				
Transfers to Stage 1 [(1)]	42	(42)	–	–
Transfers to Stage 2 [(1)]	(117)	117	–	–
Transfers to Stage 3 [(1)]	–	(342)	342	–
Net remeasurement [(2)]	2,469	(232)	4	2,241
Mortgage advances	674	–	–	674
Mortgage repayments	(913)	(2)	–	(915)
Balance, June 30, 2020	$ 6,886	$ 158	$ 346	$ 7,390

(1) Transfers between stages which are presumed to occur before any corresponding remeasurement of the provision.
(2) Net remeasurement represents the change in the expected credit loss related to changes in model inputs or assumptions, including changes in macroeconomic conditions, and changes in measurement following a transfer between stages. It also includes post-model overlays and adjustments as a result of the economic uncertainty related to the world-wide COVID-19 pandemic.

During the six month period ended June 30, 2020, the provision for mortgage losses for mortgages classified as Stage 1 increased as a result of a post model adjustment made as a result of the economic uncertainty of the worldwide COVID-19 pandemic. The provision for mortgage losses for mortgages classified as Stage 2 decreased as a result of the transfer of mortgages receivable between Stages 2 and Stage 1 due to changes in credit risk and the transfer of a mortgage receivable from Stage 2 to Stage 3 due to management's estimate of impairment. The ECL is assessed individually for Stage 2 and Stage 3 mortgages.

	Six months ended June 30, 2019			
	Stage 1	Stage 2	Stage 3	Total
Opening balance, January 1, 2019	$ 3,900	$ –	$ –	$ 3,900
Provision for mortgage losses				
Transfers to Stage 1 [(1)]	–	–	–	–
Transfers to Stage 2 [(1)]	(96)	96	–	–
Transfers to Stage 3 [(1)]	–	–	–	–
Net remeasurement [(2)]	540	(96)	–	444
Mortgage advances	879	–	–	879
Mortgage repayments	(523)	–	–	(523)
Balance, June 30, 2019	$ 4,700	$ –	$ –	$ 4,700

(1) Transfers between stages which are presumed to occur before any corresponding remeasurement of the provision.
(2) Net remeasurement represents the change in the expected credit loss related to changes in model inputs or assumptions, including changes in macroeconomic conditions, and changes in measurement following a transfer between stages.

During the six month period ended June 30, 2019, the provision for mortgage losses for mortgages receivable classified as Stage 1 increased as a result of the overall increase in the mortgage portfolio.

NOTE 6 – INVESTMENT PROPERTIES

	June 30 2020	December 31 2019
Gross carrying amount	$ 17,007	$ 17,007
Impairment	(806)	(806)
Net carrying amount	$ 16,201	$ 16,201

NOTE 6 – INVESTMENT PROPERTIES (continued)

Investment properties consist of two residential multi-unit rental properties, a four unit property in Leduc, Alberta and a 90 unit property in Regina, Saskatchewan. At December 31, 2019, as a result of the economic conditions in Saskatchewan affecting vacancy and rental rates, the company estimated that the carrying value of the Regina property exceeded its value in use, resulting in an impairment loss of $806. The value in use was estimated using a net operating income analysis. This analysis included estimates of gross rental income, vacancy rates, operating and management expenses and capitalization rates. Increases (decreases) in gross rental income will result in a higher (lower) value in use of the investment property. Increases (decreases) in the vacancy rates, operating and management expenses or capitalization rates will result in a lower (higher) value in use of the investment property. The recoverable amount of this Regina property is estimated to be its value in use of $15,100.

	Three months ended June 30		Six months ended June 30	
Rental income (loss)	**2020**	**2019**	**2020**	**2019**
Revenue from investment properties	$ 272	$ 163	$ 556	$ 269
Property operating costs	(129)	(265)	(236)	(389)
Rental income (loss)	$ 143	$ (102)	$ 320	$ (120)

NOTE 7 – CREDIT FACILITY

At June 30, 2020, the company had a credit facility from a syndicate of four Canadian financial institutions of $210,000 (December 31, 2019 – $210,000) at a formula rate that varies with bank prime and the market bankers' acceptance rate. At any time during the term of the credit facility, the company has the one-time right to increase the credit facility by up to $30,000 (such that the total maximum availability would be up to $240,000). The annualized weighted average rate for the six month period ended June 30, 2020 was 3.41% (4.07% for the year ended December 31, 2019). Drawings under the credit facility may be by way of a bank loan (including an overdraft facility of up to $500), bankers' acceptances or letters of credit (LCs). LCs represent irrevocable assurances that the company's banks will make payments in the event that a borrower of the company cannot meet its obligations to third parties. LCs carry the same credit risk, recourse and collateral security requirements as mortgages extended to customers. The committed credit facility was effective January 2, 2019, has a term to January 11, 2021, and is subject to certain conditions of drawdown and other covenants.

The credit facility is secured by a lien over all of the company's assets by means of a general security agreement. The amount that may be drawn down under the credit facility is determined by the aggregate value of mortgages receivable that are acceptable to the lender. Under the terms of the credit facility, covenants must be met in respect of shareholders' equity, debt to total assets and interest coverage. At June 30, 2020 and December 31, 2019, the company was in compliance with these covenants.

Credit facility	**June 30 2020**	**December 31 2019**
Bankers' acceptances	$ 85,000	$ 113,000
Bank loan	28,220	10,490
Cash	(15,600)	–
Overdraft facility	73	447
Unamortized finance costs	(203)	(488)
Borrowings under credit facility	97,490	123,449
Letters of credit	6,567	8,428
Total credit facility utilization	$ 104,057	$ 131,877

Cash represents funds received by the company on June 30, 2020 that were used to repay the bank loan but were applied against the bank loan by the financial institutions subsequent to June 30, 2020.

Interest on the credit facility is included in financing costs and calculated using the effective interest method. Included in interest and other bank charges for the six month period ended June 30, 2020 is interest on the credit facility of $2,654 (June 30, 2019 – $3,351) and bank fees and amortization of financing costs of $144 (June 30, 2019 – $146).

NOTE 8 – RELATED PARTY TRANSACTIONS

The company pays management and mortgage servicing fees to Canadian Mortgage Capital Corporation (CMCC), which is the manager of the company, and responsible for its day-to-day management. The majority beneficial owner and Chief Executive Officer (CEO) of the manager is also CEO of the company. The company incurred management and mortgage servicing fees of $3,477 for the six month period ended June 30, 2020 (six month period ended June 30, 2019 – $3,437). The management agreement between the company and CMCC contains provisions for the payment of termination fees to the manager in the event that the management agreement is terminated in certain circumstances. Amounts due to related party of $504 (December 31, 2019 – $565) are included in accounts payable and accrued liabilities and are due to CMCC, are in the normal course of business, are non-interest bearing, due on demand and are paid within 30 days of each period end.

Under an employee share purchase plan (ESPP) for the company's common shares, participants, including employees of CMCC, may contribute up to an annual maximum to the ESPP and CMCC matches 50% of the participants' contributions. The total amount matched by CMCC for the six month period ended June 30, 2020 was $31 (six month period ended June 30, 2019 – $24).

Certain of the company's mortgages receivable are shared with other investors. As at June 30, 2020, companies owned by a director and officer of the company were not co-invested in any syndicated secured mortgage receivable (December 31, 2019 – one syndicated mortgage receivable of $56,186, of which the company's share was $28,093).

As at June 30, 2020, the company had four mortgages receivable from borrowers over which a director and officer of the company has joint control (December 31, 2019 – three).

- A secured mortgage receivable loan with a total gross commitment of $3,490 (December 31, 2019 – $3,490), of which $3,490 had been funded at June 30, 2020 (December 31, 2019 – $3,490). During the six month period ended June 30, 2020, the company recognized net mortgage interest and fees of $153 (six month period ended June 30, 2019 – $159) from this mortgage receivable.
- A secured mortgage receivable loan with a total gross commitment of $8,738 (December 31, 2019 – $8,738). The company's share of the commitment is $2,330 (December 31, 2019 – $2,330), of which $2,330 had been funded at June 30, 2020 (December 31, 2019 – $2,330). During the six month period ended June 30, 2020, the company recognized net mortgage interest and fees of $109 (six month period ended June 30, 2019 – $117) from this mortgage receivable.
- A secured mortgage receivable loan with a total gross commitment of $7,875 (December 31, 2019 – $7,875). The company's share of the commitment is $1,500 (December 31, 2019 – $1,500), of which $1,500 had been funded at June 30, 2020 (December 31, 2019 – $1,500). During the six month period ended June 30, 2020, the company recognized net mortgage interest and fees of $59 (six month period ended June 30, 2019 – $54) from this mortgage receivable.
- A secured mortgage receivable loan with a total gross commitment of $18,450 (December 31, 2019 – $nil). The company's share of the commitment is $6,550 (December 31, 2019 – $nil), of which $2,450 had been funded at June 30, 2020 (December 31, 2019 – $nil). During the six month period ended June 30, 2020, the company recognized net mortgage interest and fees of $115 (six month period ended June 30, 2019 – $nil) from this mortgage receivable.

Key management includes directors and officers of the company. Compensation expenses for key management personnel include:

	Three months ended June 30		Six months ended June 30	
	2020	2019	2020	2019
Directors' fees [1] (Note 12)	$ 63	$ 45	$ 125	$ 90
Share-based payments to directors (Note 11)	30	29	61	58
Share-based payments to officers (Note 11)	18	17	37	34
	$ 111	$ 91	$ 223	$ 182

(1) The cumulative adjustment for the fair value of deferred share units issued under the deferred share unit plan was $19 for the six months ended June 30, 2020 (June 30, 2019 - $nil) (see Note 12 – Deferred Share Unit Plan)

Related party transactions are in the normal course of business and are recorded at the amount of consideration established and agreed to by the related parties.

NOTE 9 – CONVERTIBLE DEBENTURES

	Convertible debenture						
	5.60% AI.DB.E	**5.50% AI.DB.D**	**5.30% AI.DB.C**	**5.50% AI.DB.B**		**5.25% AI.DB**	**Total**
Six month period ended June 30, 2020							
Issued and outstanding face value	$ 28,750	$ 34,500	$ 25,300	$ 40,250		$ –	$ 128,800
Book value –							
Convertible debentures, beginning of period	$ 27,274	$ 32,888	$ 24,334	$ 39,639		$ 29,775	$ 153,910
Conversion to shares	–	–	–	–		(4,914)	(4,914)
Repayment of convertible debenture	–	–	–	–		(24,977)	(24,977)
Accretion for the period	137	131	105	171		116	660
Convertible debentures, end of period	$ 27,411	$ 33,019	$ 24,439	$ 39,810		$ –	$ 124,679

	Convertible debenture						
	5.60% AI.DB.E	**5.50% AI.DB.D**	**5.30% AI.DB.C**	**5.50% AI.DB.B**	**6.25% AI.DB.A**	**5.25% AI.DB**	**Total**
Year ended December 31, 2019							
Issued and outstanding face value	$ 28,750	$ 34,500	$ 25,300	$ 40,250	$ –	$ 29,914	$ 158,714
Book value –							
Convertible debentures, beginning of year	$ –	$ 32,627	$ 24,124	$ 39,299	$ 29,186	$ 32,053	$ 157,289
Conversion to shares	–	–	–	–	(990)	(2,568)	(3,558)
Issued	28,750	–	–	–	–	–	28,750
Equity component	(351)	–	–	–	–	–	(351)
Issue costs	(1,369)	–	–	–	–	–	(1,369)
Issue costs attributed to equity component	17	–	–	–	–	–	17
Repayment of convertible debenture	–	–	–	–	(28,278)	–	(28,278)
Accretion for the year	227	261	210	340	82	290	1,410
Convertible debentures, end of year	$ 27,274	$ 32,888	$ 24,334	$ 39,639	$ –	$ 29,775	$ 153,910

On March 29, 2019, the company completed a public offering of 5.60% convertible debentures for gross proceeds of $25,000. On April 16, 2019, the company received gross proceeds of $3,750 from the exercise in full of the over-allotment option on the 5.60% convertible debentures.

	Convertible debenture					
	5.60% AI.DB.E	**5.50% AI.DB.D**	**5.30% AI.DB.C**	**5.50% AI.DB.B**	**6.25% AI.DB.A**	**5.25% AI.DB**
Maturity date	March 31, 2025	Dec. 31, 2025	June 30, 2024	Sept. 30, 2021	March 31, 2019	June 30, 2020
Initial term	6 years	7 years	7 years	7 years	5 years	7 years
Conversion at option of shareholder at:	$14.75/share	$15.60/share	$14.94/share	$14.65/share	$13.30/share	$13.50/share
Interest payment dates	March 31, Sept. 30	June 30, Dec. 31	June 30, Dec. 31	March 31, Sept. 30	March 31, Sept. 30	June 30, Dec. 31
Redeemable at the company's option at par plus accrued interest, provided the weighted average trading price of common shares is not less than 125% of the conversion price from	March 31, 2022	Dec. 31, 2021	June 30, 2020	Sept. 30, 2017	March 31, 2017	June 30, 2016
to	March 31, 2024	Dec. 31, 2023	June 30, 2022	Sept. 30, 2019	March 31, 2018	June 30, 2018
Redeemable at the company's option at par plus accrued interest and unpaid interest after	March 31, 2024	Dec. 31, 2023	June 30, 2022	Sept. 30, 2019	March 31, 2018	June 30, 2018

NOTE 9 – CONVERTIBLE DEBENTURES (continued)

On May 4, 2020, the company redeemed early all of the outstanding 5.25% convertible debentures for cash. The redemption totalled an aggregate principal amount of $24,977 plus all accrued and unpaid interest.

Interest costs related to the convertible debentures are recorded in financing costs using the effective interest rate method. Interest on the convertible debentures is included in financing costs and consists of the following:

	Three months ended June 30		Six months ended June 30	
	2020	**2019**	**2020**	**2019**
Coupon rate interest on convertible debentures	$ 1,889	$ 2,196	$ 3,990	$ 4,456
Accretion and other costs	333	369	663	717
Interest on convertible debentures	$ 2,222	$ 2,565	$ 4,653	$ 5,173

NOTE 10 – SHARE CAPITAL

The company is authorized to issue an unlimited number of common shares without par value. Common shares rank equally with each other and have no preference, conversion, exchange or redemption rights. Common shares participate pro rata with respect to any dividends paid, including distributions upon termination and dissolution.

The company has an optional dividend reinvestment plan (DRIP) for shareholders, whereby participants may reinvest cash dividends in additional common shares of the company at the volume weighted average price for five days prior to distribution, less a 2% discount. During the three and six month period ended June 30, 2020, 44,877 and 140,436 common shares were issued under the Company's DRIP (three and six month period ended June 30, 2019 – 80,810 and 163,881), using reinvested dividends of $404 and $1,731 (three and six month period ended June 30, 2019 – $1,066 and $2,133). Shares issued under the DRIP are issued by the company from treasury. On April 29, 2020, in response to the market disruption caused by the COVID-19 pandemic, the company announced the suspension of its dividend reinvestment plan (DRIP) commencing with the dividend payable on May 12, 2020 to shareholders of record on April 30, 2020.

On May 5, 2020, the company announced that the TSX had accepted a notice filed by the company of its intention to make a normal course issuer bid ("NCIB") with respect to its common shares. The notice provides that the company may purchase up to 4,000,000 common shares during the twelve month period commencing May 11, 2020 and ending on May 10, 2021. During the six months ended June 30, 2020, the company did not purchase any common shares under the NCIB.

Under the employee share purchase plan (ESPP), each participant may contribute up to an annual maximum to the ESPP, and CMCC matches 50% of the participant's contribution. Thus, the company does not bear any of the cost of the ESPP, as it is reimbursed by CMCC and the participants.

NOTE 11 – SHARE-BASED PAYMENTS

Grants are provided to directors and certain employees of the manager under the company's deferred share incentive plan ("DSIP"). The DSIP units vest annually over three years. Common shares are issued to participants on the vesting date of each tranche of the DSIP units, unless a participant elects to defer the issuance. In addition, income deferred share incentive plan ("IDSIP") units are credited to holders of DSIP units granted before 2017 based upon dividends paid on common shares. The fair value of share-based compensation was based upon the volume weighted average market price of the common shares five days prior to the grant date of September 3, 2019 ($13.72).

	Six months ended June 30, 2020			Year ended December 31, 2019		
	DSIP units	IDSIP units	Total	DSIP units	IDSIP units	Total
Balance, beginning of period	73,000	9,874	82,874	68,667	9,056	77,723
Units granted	–	–	–	22,000	–	22,000
Units earned	–	1,406	1,406	–	2,820	2,820
Common shares issued	(6,167)	(1,259)	(7,426)	(17,667)	(2,002)	(19,669)
Balance, end of period	66,833	10,021	76,854	73,000	9,874	82,874

NOTE 11 – SHARE-BASED PAYMENTS (continued)

Share-based payments expense:	Three months ended June 30		Six months ended June 30	
	2020	2019	2020	2019
September 3, 2019 grant	$ 46	$ –	$ 92	$ –
September 1, 2018 grant	21	46	42	92
September 1, 2017 grant	7	17	14	34
September 1, 2016 grant	2	9	5	19
September 1, 2015 grant	2	3	5	6
September 1, 2014 grant	2	2	5	5
August 30, 2013 grant	1	1	2	2
	$ 81	$ 78	$ 165	$ 158

NOTE 12 – DEFERRED SHARE UNIT PLAN

The board of directors established a deferred share unit plan ("DSUP") effective January 1, 2020 pursuant to which each non-executive director is required to receive one-half of their director compensation in the form of deferred share units ("DSU"). Each non-executive director can elect to receive the remaining one-half of their director compensation in DSUs or cash or a combination thereof. DSUs are credited to the director DSUP accounts quarterly, in arrears, in an amount equal to the non-executive director's remuneration elected to be paid in DSUs divided by the fair market value of the common shares on the last day of the quarter. The fair market value is equal to the volume-weighted average trading price of the company's common shares on the TSX for the five trading days immediately preceding that day. Dividend equivalents are credited to a non-executive director's DSUP account as if dividends were paid on each DSU held by a non-executive director on the dividend record date and reinvested in additional DSUs at the fair market value on the dividend payment date.

DSUs can only be exercised when the non-executive director ceases to serve in any capacity with the company. Payment will be made, at the election of the non-executive director, in either cash or common shares of the company purchased in the market, net of applicable taxes or other amounts required to be withheld or deducted, based on the fair market value of the company's common shares on or about the date of the payment. Amounts owed in relation to this plan of $128 (December 31, 2019 – $nil) are included in accounts payable and accrued liabilities. DSU compensation expense is recognized in directors' expense, dividends earned on outstanding DSUs is recognized in interest and other financing charges and the adjustment to fair value of units issued under the DSUP is recognized as an operating expense.

	Three months ended June 30		Six months ended June 30	
	2020	2019	2020	2019
Directors fees paid in DSUs	54	–	108	–
Dividends on DSUs	1	–	1	–
Adjustment to fair value of DSUs	19	–	19	–
	$ 74	$ –	$ 128	$ –

Number of Units	Six months ended June 30 2020	Year ended December 31 2019
Outstanding DSUs, beginning of period	–	–
Granted	11,232	–
Reinvested	142	–
Balance, end of period	11,374	$ –

NOTE 13 – EARNINGS PER SHARE

	Three months ended June 30		Six months ended June 30	
	2020	2019	2020	2019
Basic earnings per share –				
Numerator				
Net income and comprehensive income for the period	$ 9,821	$ 9,667	$ 19,685	$ 18,902
Denominator				
Weighted average common shares outstanding	42,376,225	39,410,929	42,247,732	38,792,599
Basic earnings per share	$ 0.23	$ 0.25	$ 0.47	$ 0.49
Diluted earnings per share –				
Numerator				
Net income and comprehensive income for the period	$ 9,821	$ 9,667	$ 19,685	$ 18,902
Interest on convertible debentures	2,222	2,565	4,653	5,173
Net income and comprehensive income for diluted earnings per share	12,043	12,232	24,338	24,075
Denominator				
Weighted average common shares outstanding	42,376,225	39,410,929	42,247,732	38,792,599
Convertible debentures	9,290,208	10,964,442	9,948,732	11,088,574
Deferred share incentive plan	66,833	48,667	69,747	48,667
Income deferred share units	9,716	8,068	9,935	7,678
Weighted average common shares outstanding – diluted basis	51,742,982	50,432,106	52,276,146	49,937,518
Diluted earnings per share	$ 0.23	$ 0.24	$ 0.47	$ 0.48

NOTE 14 – FINANCIAL INSTRUMENTS

(a) Classification of financial instruments

Financial assets comprise mortgages receivable and are classified and measured at amortized cost. Financial liabilities comprise borrowings under credit facility, accounts payable and accrued liabilities, dividends payable, accrued convertible debenture interest and the liability component of convertible debentures. The liability for the deferred share unit plan is measured at FVTPL. All other financial liabilities are measured at amortized cost.

(b) Fair value

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between arm's length market participants at the measurement date. The fair value hierarchy establishes three levels to classify the inputs to valuation techniques used to measure fair value:

- Level 1 inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities.
- Level 2 inputs are quoted prices in markets that are not active, quoted prices for similar assets or liabilities in active markets, inputs other than quoted prices that are observable for the asset or liability, or inputs that are derived principally from or corroborated by observable market data or other means.
- Level 3 inputs are unobservable (supported by little or no market activity).

NOTE 14 – FINANCIAL INSTRUMENTS (continued)

(b) Fair value (continued)

The fair value hierarchy gives the highest priority to Level 1 inputs and the lowest priority to Level 3 inputs. All financial assets are classified and measured at amortized cost. Their carrying values approximate their fair values due to their relatively short-term maturities and because market interest rates have not fluctuated significantly since the date at which the loans were entered into. The fair value of borrowings under credit facility approximates book value since it bears interest at floating rates. The accounts payable and accrued liabilities, excluding the liability for the deferred share units, dividends payable and accrued convertible debenture interest carrying values approximates their fair values due to the short-term nature of the items. The liability for the deferred share units is measured at fair value using Level 1 inputs. The deferred share units are measured at fair market value on the day they are credited to the directors' DSUP accounts, with fair value equal to the volume-weighted average trading price of the company's common shares on the TSX for the five trading days immediately preceding that day, and are remeasured using fair market value at each reporting date.

The fair value of convertible debentures at the time of issue is established using Level 2 inputs. The fair value of convertible debentures has been determined based on the closing prices of the convertible debentures on the TSX on the respective dates.

Convertible debentures	**June 30 2020**	**December 31 2019**
Fair value	$ 125,866	$ 161,872
Less book value of equity component	(1,470)	(1,837)
	$ 124,396	$ 160,035
Book value of financial liability component	$ 124,679	$ 153,910

(c) Credit risk

Mortgages receivable and issued letters of credit are exposed to credit risk. Credit risk is the risk that a counterparty to a financial instrument will fail to discharge its obligation or commitment, resulting in a financial loss to the company. The maximum exposure to credit risk related to mortgages receivable, including letters of credit outstanding, at June 30, 2020 is $682,463 (December 31, 2019 – $736,570).

The company mitigates the credit risk by maintaining strict credit policies including due diligence processes, credit limits, documentation requirements, review and approval of new and renewed mortgages receivable by the board of directors or a subgroup thereof, quarterly review of the entire portfolio by the board of directors, and other credit policies approved by the board of directors. Credit risk is approved by the board of directors. These credit policies and processes have been consistently applied throughout the two year period ended June 30, 2020.

All mortgages receivable are secured by the underlying real estate, plus other credit enhancements, which may include guarantees from the borrowers, personal guarantees from the borrower's shareholders and/or cross guarantees from related entities. The quality of the mortgage collateral is primarily driven by the location and type of underlying property and type of mortgage receivable. For further information, refer to Note 5(a) and to the "Investment Portfolio" section of the Management's Discussion and Analysis for the three and six month period ended June 30, 2020. Management continuously monitors real estate values and considers there to have been no significant changes in the quality of the collateral underlying the remaining mortgage portfolio.

At June 30, 2020, the largest borrower group accounted for 12.0% of mortgages receivable (December 31, 2019 – 11.3%). See Note 5(a) and Note 5(b) for a breakdown of mortgages receivable and the provision for mortgage losses by property type.

NOTE 14 – FINANCIAL INSTRUMENTS (continued)

(d) Liquidity risk

Liquidity risk is the risk that the company will not be able to meet its obligations when due. The primary sources of liquidity risk are the requirements to fund commitments for new mortgages, advances on existing mortgages receivable, as well as obligations under the company's credit facility. The company's liquidity risk is managed on an ongoing basis in accordance with the policies and procedures in place that reduce the risk to an acceptable level. Policies and procedures include continuous monitoring of expected cash flows, reviewing credit requirements with the company's bankers, issuing convertible debentures or common shares in the public markets from time to time as required, and staggering the maturities of convertible debentures when they are issued.

From time to time the company has arranged temporary increases in its credit facility with its banks in order to manage liquidity requirements, and expects to be able to continue to do so in the future if required. The company's significant financial liabilities include borrowings under credit facility, accounts payable and accrued liabilities, dividends payable, accrued convertible debenture interest and the liability component of convertible debentures. The borrowings under credit facility are drawn upon as required to discharge accounts payable and accrued liabilities as well as to pay out dividends on a monthly basis. The company's agreement with the lender is that the operating line will not be called provided that all covenants are met and that any significant excess cash is used to pay down the borrowings under credit facility.

June 30, 2020	Carrying value	Contractual cash flow	Within 1 year	1 to 3 years	3 to 5 years	More than 5 years
Borrowings under credit facility[1]	$97,693	$99,687	$99,687	$ –	$ –	$ –
Accounts payable and accrued liabilities	2,333	2,333	2,333	–	–	–
Accrued convertible debenture interest	956	956	956	–	–	–
Dividends payable	3,179	3,179	3,179	–	–	–
Convertible debentures[2]	124,679	144,162	45,099	33,656	65,407	–
Total	228,840	250,317	151,254	33,656	65,407	–
Unadvanced mortgage commitments[3]	–	57,883	57,883	–	–	–
Total contractual liabilities	$228,840	$308,200	$209,137	$33,656	$ 65,407	$ –

Notes:

(1) Includes interest assuming the outstanding balance is not repaid until maturity on January 11, 2021.

(2) The 5.50% 2021 debentures are assumed to be repaid in the third quarter of 2020; 5.30% debentures are assumed to be repaid June 30, 2022; 5.50% 2025 debentures are assumed to be repaid December 31, 2023 and 5.60% debentures are assumed to be repaid March 31, 2024.

(3) Unadvanced mortgage commitments include additional funds on existing mortgages receivable and new mortgage commitments. The experience of the company has been that a portion of the unadvanced amounts on existing mortgages receivable will never be drawn.

As at June 30, 2020, management considers that it has adequate procedures in place to manage liquidity risk.

(e) Interest rate risk

The company is exposed to interest rate risk in that an increase in interest rates will result in increased interest expense due to its borrowings under credit facility being set at a variable rate and mortgages receivable are set at a combination of fixed and variable rates. The financial structure of the company results in relatively moderate interest rate risk because a majority of the company's financing is through common shares and convertible debentures, with a moderate amount of borrowings under the credit facility that bear floating interest rates.

If interest rates on debt had been one percentage point higher (lower) during the six month period ended June 30, 2020, income and comprehensive income would have been reduced (increased) by approximately $1,381 during the period, assuming that no changes had been made to the interest rates at which new mortgage loans were entered into. However, if new mortgage loans had been entered into at higher (lower) interest rates, the resulting reduction of income and comprehensive income would have been less than (greater than) $1,381.

NOTE 14 – FINANCIAL INSTRUMENTS (continued)

(f) Currency risk

Currency risk is the risk that the value of financial assets and financial liabilities will fluctuate due to changes in foreign exchange rates. The company is not exposed to currency risk as all financial assets and financial liabilities are denominated in Canadian funds.

NOTE 15 – CAPITAL MANAGEMENT

The company defines capital as total debt plus shareholders' equity, as shown below:

	June 30 2020	December 31 2019
Borrowings under credit facility	$ 97,490	$ 123,449
Convertible debentures	124,679	153,910
Total debt	222,169	277,359
Shareholders' equity	463,068	455,520
Capital employed	$ 685,237	$ 732,879

The company's objectives for managing capital are to preserve shareholders' equity, provide shareholders with stable dividends, and to use leverage in a conservative manner to improve return to shareholders. The company finances growth of its portfolio by issuing common shares and debt. In addition, a small amount of equity is raised every month through a dividend reinvestment plan for shareholders and the employee share purchase plan.

As bank borrowings increase, the company could expect to raise further funds through public offerings of convertible debentures or common shares, and through private placements of debt. The borrowings under credit facility are subject to external covenants as set out in Note 7 – Credit facility. There has been no change in the company's capital management objectives since the prior period.

NOTE 16 – SUBSEQUENT EVENTS

As at July 28, 2020, the company had collected 96% of the mortgage interest due in July, which is in line with historical collection rates.