Condensed Consolidated Interim Financial Statements of

DIVERSIFIED ROYALTY CORP.

Three months ended March 31, 2020 and 2019

DIVERSIFIED ROYALTY CORP.

Condensed Consolidated Interim Statements of Financial Position
(Unaudited)
(Expressed in thousands of Canadian dollars)

	Note	March 31, 2020	December 31, 2019
Assets			
Current assets:			
Cash and cash equivalents	4	$ 9,532	$ 2,968
Royalties and management fees receivable	6	3,767	4,392
Related party receivable	7	-	3,766
Amounts receivable		2,195	17
Prepaid expenses and other		504	529
		15,998	11,672
Investment in NND LP	7	51,002	51,807
Intangible assets	8	306,278	281,787
		$ 373,278	$ 345,266
Liabilities and Shareholders' Equity			
Current liabilities:			
Accounts payable and accrued liabilities		$ 2,346	$ 1,136
Income tax payable	13	489	1,223
		2,835	2,359
Acquisition facility	9(a)	9,000	-
Long-term bank loans, net of deferred financing charges	9(b)	89,513	82,473
Convertible debentures	10	53,521	53,194
Promissory note		3,442	4,805
Exchangeable Units	12	612	1,115
Interest rate swap liabilities	11	2,837	412
Deferred income tax liability	13	6,747	12,213
Shareholders' equity:			
Share capital	14	197,233	163,174
Contributed surplus		40,613	40,293
Equity component of convertible debentures		2,938	2,938
Accumulated deficit		(36,013)	(17,710)
		204,771	188,695
		$ 373,278	$ 345,266

Nature of operations (note 1)
Subsequent event (note 20)

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

DIVERSIFIED ROYALTY CORP.
Condensed Consolidated Interim Statements of Net (Loss) Income and Comprehensive (Loss) Income
(Unaudited)
(Expressed in thousands of Canadian dollars, except per share amounts)

		Three months ended March 31, 2020	2019
	Note	2020	2019
Royalty income	5	$ 7,160	$ 6,325
Management fees		104	78
		7,264	6,403
Expenses			
Salaries and benefits		395	409
Share-based compensation	15	320	391
General and administration		128	125
Professional fees		143	53
Impairment of intangible asset	8	19,841	-
		20,827	978
(Loss) Income from operations		(13,563)	5,425
Interest expense on credit facilities		(1,809)	(1,446)
Other finance income, net	17	967	105
Fair value adjustment on financial instruments	7, 11, 12	(1,732)	(536)
(Loss) Income before income taxes		(16,137)	3,548
Income tax (recovery) expense	13	(4,406)	1,064
Net (loss) income and comprehensive (loss) income		$ (11,731)	$ 2,484
Weighted average number of shares outstanding			
Basic		112,699,189	107,840,033
Diluted		112,699,189	108,773,613
(Loss) Income per share			
Basic	16	$ (0.10)	$ 0.02
Diluted	16	$ (0.10)	$ 0.02

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

DIVERSIFIED ROYALTY CORP.
Condensed Consolidated Interim Statements of Changes in Equity
(Unaudited)
(Expressed in thousands of Canadian dollars, except for share amounts)

	Note	Common shares	Share capital	Contributed surplus	Equity component of convertible debentures	Accumulated deficit	Total equity
Balance, January 1, 2020		109,501,916	$ 163,174	$ 40,293	$ 2,938	$ (17,710)	$188,695
Common shares issued on public offering	14	10,810,000	33,047	-	-	-	33,047
Common shares issued on DRIP	14	465,780	1,012	-	-	-	1,012
Share-based compensation		-	-	320	-	-	320
Dividends declared		-	-	-	-	(6,572)	(6,572)
Comprehensive loss		-	-	-	-	(11,731)	(11,731)
Balance, March 31, 2020		120,777,696	$ 197,233	$ 40,613	$ 2,938	$ (36,013)	$204,771

	Note	Common shares	Share capital	Contributed surplus	Equity component of convertible debentures	Accumulated deficit	Total equity
Balance, January 1, 2019		107,768,300	$ 184,528	$ 25,974	$ 2,938	$ (20,720)	$192,720
Common shares issued on DRIP		291,720	869	-	-	-	869
Share-based compensation		-	-	391	-	-	391
Dividends declared		-	-	-	-	(6,000)	(6,000)
Comprehensive income		-	-	-	-	2,484	2,484
Balance, March 31, 2019		108,060,020	$ 185,397	$ 26,365	$ 2,938	$ (24,236)	$190,464

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

DIVERSIFIED ROYALTY CORP.
Condensed Consolidated Interim Statements of Cash Flows
(Unaudited)
(Expressed in thousands of Canadian dollars)

	Three months ended March 31, 2020	2019
Cash flows from (used in) operating activities:		
Net (loss) income	$ (11,731)	$ 2,484
Adjustments for:		
Deferred income taxes	(4,895)	1,064
Impairment of intangible asset	19,841	-
Share-based compensation	320	391
Fair value adjustments on financial instruments	1,732	536
Interest expense on credit facilities	1,809	1,446
Other finance costs (income), net	(967)	(105)
Foreign exchange (loss) gain	14	(4)
Interest paid	(1,087)	(691)
Interest received	22	443
Distributions received from NND LP	962	-
Changes in non-cash operating items:		
Royalties and management fees receivable	625	238
Amounts receivable	(2,178)	-
Prepaid expenses and other	(7)	(22)
Accounts payable and accrued liabilities	455	(71)
Income tax payable	(734)	-
Net cash from operating activities	4,181	5,709
Cash flows from (used in) financing activities:		
Proceeds from issuance of equity	34,592	-
Equity issuance costs	(2,116)	-
Proceeds from issuance of debt	46,700	-
Repayment of debt	(30,700)	-
Related party receivable	3,766	-
Payment of dividends	(5,560)	(5,131)
Net cash from (used in) financing activities	46,682	(5,131)
Cash flows used in investing activities:		
Addition to intangible assets	(44,299)	-
Net cash used in investing activities	(44,299)	-
Net increase in cash and cash equivalents	6,564	578
Cash and cash equivalents, beginning of period	2,968	78,342
Cash and cash equivalents, end of period	9,532	$ 78,920

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

Diversified Royalty Corp. (“DIV”), formerly BENEV Capital Inc. and prior to that Bennett Environmental Inc., is a company domiciled in Canada and incorporated on July 29, 1992 under the Canada Business Corporation Act. The condensed consolidated interim financial statements of DIV as at and for the three months ended March 31, 2020 are composed of DIV and its subsidiaries (together referred to as the “Company”). The Company’s common shares are listed on the Toronto Stock Exchange (“TSX”) and traded under the symbol “DIV”. The registered office of the Company is located at 902-510 Burrard Street, Vancouver, BC, V6C 3A8.

1. Nature of operations:

The current business of DIV is to acquire royalties from well-managed multi-location businesses and franchisors in North America (“Royalty Partners”).

On June 19, 2015, the Company indirectly acquired, through SGRS Royalties Limited Partnership (“SGRS LP”) (an entity controlled by the Company), all of the Canadian and U.S. trademarks and certain other intellectual property rights utilized by Sutton Group Realty Services Ltd. (“Sutton”) in its residential real estate franchise business (the “SGRS Rights”). The Company granted Sutton the licence to use the SGRS Rights for a term ending on December 31, 2114 in exchange for a royalty payment initially equal to $56.25 per agent per month (the “Sutton Royalty Rate”) for the number of agents included in the royalty pool (the “Sutton Royalty Pool”). Effective July 1, 2019, the Sutton Royalty Rate was increased to $60.887 per agent per month.

On August 19, 2015, the Company indirectly acquired through ML Royalties Limited Partnership (“ML LP”) (an entity controlled by the Company), the trademarks and certain other intellectual property rights (the “ML Rights”) from Mr. Lube Canada Limited Partnership (“Mr. Lube”). The Company granted Mr. Lube the licence to use the ML Rights for a term ending on August 19, 2114 in exchange for a royalty payment initially equal to 6.95% of system sales of Mr. Lube locations in the royalty pool (the “Mr. Lube Royalty Pool”). On May 1, 2018, the Mr. Lube royalty rate on non-tire sales was increased by 0.5% from 6.95% to 7.45%

On August 25, 2017, the Company indirectly acquired through AM Royalties Limited Partnership (“AM LP”) (a wholly owned subsidiary of the Company), the Canadian AIR MILES trademarks and certain Canadian intellectual property rights (collectively, the “AIR MILES Rights”) from a subsidiary of Aimia Inc. (“Aimia”). In accordance with the terms of two license agreements with LoyaltyOne Co. (collectively the “AIR MILES Licenses”) acquired by AM LP as part of acquisition of the AIR MILES Rights, LoyaltyOne Co. has an exclusive right to use the AIR MILES Rights for the purposes of operating the AIR MILES reward program in Canada (the “AIR MILES Program”) for an indefinite term in exchange for a royalty payment equal to 1% of gross billings from the AIR MILES Program.

On May 20, 2019, the Company indirectly acquired through MRM Royalties Limited Partnership (“MRM LP”) (an entity controlled by the Company), the trademarks and certain other intellectual property rights utilized by Mr. Mikes Restaurants Corporation (“Mr. Mikes”) in its restaurant business (the “MRM Rights”). The Company granted Mr. Mikes the licence to use the MRM Rights for a term ending on May 19, 2118 in exchange for a royalty payment initially equal to 4.35% of notional system sales of Mr. Mikes locations in the royalty pool (the “Mr. Mikes Royalty Pool”).

On November 15, 2019, the Company indirectly acquired through NND Royalties Limited Partnership (“NND LP”) (an entity that is majority-owned by the Company), the trademarks and certain other intellectual property rights utilized by Nurse Next Door Professional Homecare Services Inc. (“Nurse Next Door”) in its premium home care business (the “NND Rights”) (note 7). NND LP granted Nurse Next Door the licence to use the NND Rights for a term ending on November 15, 2118 in exchange for a gross royalty payment (the “Gross Royalty”) equal to the greater of: (i) 6% of gross sales from Nurse Next Door’s franchises and corporate stores in Canada and the United States and (ii) $4.8 million per year, which grows at a fixed rate of 2.0% per annum. The Company, through its ownership of NND LP Class A units, is entitled to receive a cash distribution of $4.8 million per year, which grows at a fixed rate of 2.0% per annum (the “DIV Distribution Entitlement”). To the extent the Gross Royalty is greater than the DIV Distribution Entitlement, Nurse Next Door is entitled to receive the excess amount in the form of a cash distribution through its ownership of NND LP Class B units.

On February 20, 2020, the Company indirectly acquired through OX Royalties Limited Partnership (“OX LP”) (an entity that is majority-owned by the Company), the trademarks and certain other intellectual property rights utilized by Oxford Learning Centres, Inc. (“Oxford”) in its pre-school, elementary and secondary school and post-secondary supplemental education business (the “Oxford Rights”). The Company granted Oxford the licence to use the Oxford Rights for a term ending on February 19, 2119 in exchange for a royalty payment initially equal to 7.67% of the gross sales of Oxford locations in the royalty pool (the “Oxford Royalty Pool”).

1. Nature of operations (continued):

Substantially all of the Company's operating revenues are earned from the receipt of royalties and management fees from its Royalty Partners. Accordingly, the revenues of the Company and its ability to pay dividends to shareholders are dependent on the ongoing ability of its Royalty Partners to generate cash and pay royalties and management fees to the Company.

COVID-19

On March 11, 2020, the COVID-19 outbreak was declared a pandemic by the World Health Organization. The situation is dynamic and the ultimate duration and magnitude of the impact on the economy, our business and the respective businesses of our Royalty Partners are not known at this time. Governments worldwide, including the Canadian federal and provincial governments, enacted emergency measures to combat the spread of the virus, which have included, among others, the closure of all non-essential businesses (in most jurisdictions), bans on public gatherings and travel advisories to avoid non-essential travel. These measures have triggered significant disruptions to businesses worldwide, resulting in a sharp and extended global economic downturn.

DIV's Royalty Partners have had, and are generally expected to continue to have, significant interruptions to their respective businesses in the months ahead. In response to the financial difficulty that Mr. Mikes and Sutton are experiencing, DIV has agreed to waive certain royalty and management fee payment obligations (note 5). At this time, DIV does not know the full extent of the financial impact of such interruptions going forward or what the timeline will be for restoring normal operations for its Royalty Partners. The ongoing effects of COVID-19 could impact DIV and its Royalty Partners' (as well as their respective franchisees') ability to obtain debt and equity financing, impairment of investments, and result in an impairment in the value of the long-lived assets, or decreases in revenue or the profitability of our ongoing operations.

2. Basis of preparation:

(a) Statement of compliance:

These condensed consolidated interim financial statements have been prepared in accordance with IAS 34, *Interim Financial Reporting*. Certain information and note disclosures normally included in the annual consolidated financial statements prepared in accordance with International Financial Reporting Standards ("IFRS") have been omitted or condensed. Accordingly, these condensed consolidated interim financial statements should be read in conjunction with the Company's annual consolidated financial statements for the year ended December 31, 2019.

These condensed consolidated interim financial statements were authorized and approved for issue by the Company's Board of Directors on May 14, 2020.

(b) Basis of measurement:

The preparation of financial statements requires management to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates. The critical judgments and key estimates and assumptions are the same as described in the Company's annual financial statements for the year ended December 31, 2019.

(c) Functional and presentation currency:

These consolidated financial statements are presented in Canadian dollars, which is the Company's functional currency.

3. Significant accounting policies:

These condensed consolidated interim financial statements have been prepared using the same accounting policies as the annual financial statements for the year ended December 31, 2019.

(Tabular amounts expressed in thousands of Canadian dollars)

4. Cash and cash equivalents:

		March 31, 2020		December 31, 2019
Cash	$	9,175	$	2,961
Cash equivalents		357		7
	$	9,532	$	2,968

5. Royalty income:

		March 31, 2020		March 31, 2019
Mr. Lube	$	3,463	$	3,663
AIR MILES		1,829		1,695
Sutton		822		967
Oxford		461		-
Mr. Mikes		585		-
	$	7,160	$	6,325

Pursuant to the terms of the licence and royalty agreement between Oxford and OX LP dated February 20, 2020 (the “OX Licence and Royalty Agreement”), the royalty paid by Oxford to OX LP is calculated by multiplying the gross sales of the locations in the Oxford Royalty Pool by a royalty equal to 7.67%.

On March 18, 2020, in response to the evolving circumstances relating to the COVID-19 pandemic, all of Mr. Mikes restaurants were temporarily closed for in-restaurant dining. DIV has waived the Mr. Mikes fixed royalty and management fee payment for the February 24, 2020 to March 22, 2020 period as well as the March 23, 2020 to April 19, 2020 period. DIV is continuing its discussions with its lender and Mr. Mikes about whether additional royalty relief is required for subsequent periods, given that Mr. Mikes is generating minimal revenue. As a result, the Company recognized royalty income from Mr. Mikes for the period from January 1, 2020 to February 23, 2020.

With the dramatic slow-down of residential real estate activity due to COVID-19, DIV waived 50% of Sutton’s March 2020 royalty and management fees that were due in April. In addition, DIV has waived 75% of Sutton’s April and May 2020 royalty and management fees that are due in May and June 2020, respectively.

6. Royalties and management fees receivable:

		March 31, 2020		December 31, 2019
Mr. Lube	$	1,128	$	1,266
AIR MILES		2,066		2,419
Sutton		177		354
Oxford		389		-
Mr. Mikes		-		343
Nurse Next Door		7		10
	$	3,767	$	4,392

The Company has collected the total royalties and management fees receivable at March 31, 2020 from its royalty partners in April 2020.

(Tabular amounts expressed in thousands of Canadian dollars)

7. Investment in NND LP:

The Company, through its ownership of NND LP Class A units, is entitled to receive a cash distribution of $4.8 million per year, which grows at a fixed rate of 2.0% per annum (the "DIV Distribution Entitlement"). To the extent the Gross Royalty is greater than the DIV Distribution Entitlement, Nurse Next Door is entitled to receive the excess amount in the form of a cash distribution through its ownership of NND LP Class B units. NND LP's Gross Royalty for the three months ended March 31, 2020 was $1.6 million, of which the DIV Distribution Entitlement was $1.2 million. The cash distributions received by the Company from NND LP were recorded as a reduction in its investment in NND LP.

Nurse Next Door has the ability to purchase the NND Rights from NND LP (the "NND Buy-Out Option") at any time after November 15, 2026. Due to the NND Buy-Out Option, NND LP does not have control (per IFRS 15) over the NND Rights and cannot recognize the NND Rights as an intangible asset on its books. Instead, the transaction is accounted for as a financing arrangement, and the Company's investment in NND LP is a financial instrument measured at fair value. The valuation of the financial instrument includes an estimate of the discounted cash flow receivable from Nurse Next Door and takes into consideration the likelihood of Nurse Next Door exercising the NND Buy-Out Option and the NND Exchange Mechanism. The NND Buy-Out Option and NND Exchange Mechanism are embedded derivatives with a negligible value at March 31, 2020 and December 31, 2019. The contractual cash flows receivable from Nurse Next Door were discounted at a rate of 12.0% (December 31, 2019 - 11.9%). The total fair value of the investment in NND LP was $51.0 million (December 31, 2019 - $51.8 million) and a fair value increase of $0.2 million was recorded during the three months ended March 31, 2020. A one percentage point increase in the interest rate would decrease the fair value by $4.4 million. A one percentage point decrease in the interest rate would increase the fair value by $5.4 million.

At December 31, 2019, DIV had a promissory note receivable of $3.8 million from NND LP, which was repaid during the three months ended March 31, 2020 upon receipt of the GST refund from the CRA.

8. Intangible assets:

	ML Rights	AIR MILES	SGRS Rights	MRM Rights	Oxford Rights	Total
Balance, December 31, 2019	$ 152,327	$ 53,977	$ 32,273	$ 43,210	$ -	$ 281,787
Additions	-	-	-	-	44,332	44,332
Impairment	-	-	-	(19,841)	-	(19,841)
Balance, March 31, 2020	$ 152,327	$ 53,977	$ 32,273	$ 23,369	$ 44,332	$ 306,278

(a) Mr. Lube Rights

On May 1, 2019, the Mr. Lube Royalty Pool was adjusted to include four new Mr. Lube locations. The initial consideration paid to Mr. Lube for the estimated net additional royalty revenue was $2.7 million, representing 80% of the total estimated consideration of $3.4 million. In exchange for the net addition to the Mr. Lube Royalty Pool, Mr. Lube received the right to exchange Class B LP units of ML LP for common shares of DIV. DIV elected to pay for the initial consideration to Mr. Lube in cash. The remaining consideration payable for the additional royalty revenue was originally payable on May 1, 2020 based on the actual system sales of the four new locations added to the Mr. Lube Royalty Pool for the year ended December 31, 2019.

Based on the actual system sales for the year ended December 31, 2019 of the four new locations added to the Mr. Lube Royalty Pool, Mr. Lube is entitled to exchange 357,716 Class B units of ML LP (the "Exchangeable ML Units") for DIV shares (or cash at DIV's option). On April 28, 2020, Mr. Lube and DIV entered into an agreement to defer the settlement of the Exchangeable ML Units to a subsequent adjustment date being no earlier than May 1, 2021.

8. Intangible assets (continued):

(b) Oxford Rights:

On February 20, 2020, the Company indirectly acquired, through OX LP, the Oxford Rights for a purchase price of $44.0 million (the "Purchase Price"), plus a retained interest provided to Oxford through the issuance of 10,493 Ordinary LP units, 100,000,000 Class B, 100,000,000 Class C, 100,000,000 Class D, 100,000,000 Class E, 100,000,000 Class F, 100,000,000 Class G, and 100,000,000 Class H limited partner units of OX LP having an agreed value of approximately $33,000.

The cash Purchase Price of $44.0 million was funded with $37.0 million drawn from DIV's Acquisition Facility and DIV's cash on hand following DIV's drawdown of the remaining $7.0 million of available capacity under the NNDH LP term loan facility (note 9(b)). The refundable Goods and Services Tax of $2.2 million payable by OX LP on the Purchase Price and estimated transaction costs were funded with a further $2.7 million drawn from the available capacity under the Acquisition Facility. The Acquisition Facility was subsequently partially repaid in cash using funds received from the issuance of equity (note 9(a)) and the issuance of $9.0 million of debt (note 20).

The Class B, Class C, Class D, Class E, Class F, Class G and Class H units are exchangeable into common shares of the Company through the exchange agreement dated February 20, 2020 among Oxford, OX Royalties GP Inc. and the Company (the "Oxford Exchange Agreement") upon the satisfaction of certain performance criteria.

Annually on May 1, the Oxford Royalty Pool may be adjusted, subject to meeting certain criteria, to include gross sales from new Oxford locations less gross sales from Oxford locations that were permanently closed during the preceding calendar year. In return for adding these net sales to the Oxford Royalty Pool, Oxford receives the right to indirectly acquire common shares of the Company through the exchange of Class B LP Units of OX LP (the "OX Additional Entitlement"). The OX Additional Entitlement is determined based on the estimated net tax-adjusted royalty revenue added to the Oxford Royalty Pool (adjusted by a 10% discount for locations that were open for business prior to December 31, 2023, or a 7.5% discount for all other additions), divided by the yield of the Company's. Oxford receives 80% of the estimated OX Additional Entitlement initially, with the balance received on May 1 of the subsequent year when the actual full year performance of the new locations is known with certainty. The OX Additional Entitlement is automatically exchanged by Oxford into common shares of DIV, or settled in cash at DIV's option, pursuant to the Oxford Exchange Agreement.

The Class C, Class D, Class E, Class F, Class G and Class H units become exchangeable into common shares of the Company on increases in the Oxford Royalty rate of 0.25% increments six times during the term of the OX Licence and Royalty Agreement.

In addition to the royalty payable to OX LP, Oxford will pay DIV a management fee of $40,000 per annum for strategic advice and other services. The management fee will increase by $5,000 every five years over the term of the OX License and Royalty Agreement.

(b) Impairment assessment:

In light of COVID-19, the Company has performed an impairment assessment on its intangible assets. Impairment exists if the carrying value of the cash-generating unit ("CGU") is greater than its recoverable amount. The Company has used the value in use method to determine recoverable amount. The estimates of future cash flows require a number of key assumptions about future business performance. These assumptions and estimates are based on the relevant business' historical experience, economic trends, as well as past and ongoing communications with relevant stakeholders of the Company. However, these forecasted cash flows are based on current and anticipated market conditions, which are inherently uncertain due to the recent and evolving impact of the COVID-19 pandemic. The COVID-19 pandemic and its impact on the economy is constantly evolving in an unpredictable manner and presents many variables and contingencies for modeling. In future periods, the effects of the pandemic may have a material impact on the recoverable amount of the Company's CGUs.

The expected future cash flows, with the exception of the MRM Rights, are based on the most recent two-year forecasts prepared by management and extrapolated over five years, with a terminal capitalization rate applied on the expected cash flows thereafter to reflect the indefinite life of the intangible assets. Subsequent to the most recent two-year forecast, revenue is projected to grow at a rate ranging from 0.5% to 2.75% (December 31, 2019 – 0.5% to 2.75%).

(Tabular amounts expressed in thousands of Canadian dollars)

8. Intangible assets (continued):

(b) Impairment assessment:

Although DIV is entitled to a fixed royalty payment from Mr. Mikes, the estimated future cash flows used to determine the recoverable amount reflect management's best estimates of what the Company can expect to collect from Mr. Mikes in light of the current COVID-19 pandemic. With all Mr. Mikes restaurants temporarily closed for in-restaurant dining, Mr. Mikes is generating minimal revenue and has advised DIV that they will likely be unable to pay its fixed royalty payments to DIV commencing with the February 24, 2020 to March 22, 2020 period. DIV is in discussions with its lenders and Mr. Mikes about whether additional royalty relief is required for subsequent periods, given that Mr. Mikes is generating minimal revenue. In addition, when in-restaurant dining resumes, a slow recovery and constrained cash flow is likely. It is possible that underperformance to these projections could occur if in-restaurant dining remains closed for a longer duration than currently anticipated.

The expected future cash flows are discounted at pre-tax rates, based on the risks associated with the assets, which range from 10.9% to 14.8% (December 31, 2019 - 10.7% to 14.7%). As at March 31, 2020, based on the assessment performed, the Company recorded an impairment loss of $19.8 million during the three months ended March 31, 2020 in connection with the MRM Rights.

The Company also considers other reasonably possible scenarios where forecasted revenue is less than budget, along with other reasonably possible higher discount rates to determine whether the intangible assets would be impaired under those scenarios. As the carrying values of the SGRS Rights and MRM Rights at March 31, 2020 approximate the estimated recoverable amounts, a subsequent change in any key assumption utilized in the estimate of future cash flows for the MRM Rights may result in an additional impairment loss.

9. Borrowings:

(a) Acquisition facility:

The Company has a $50.0 million undrawn senior secured credit facility (the "Acquisition Facility") that matures on November 30, 2022. As at March 31, 2020, the Company had $9.0 million outstanding under the Acquisition Facility, which was fully repaid on April 27, 2020.

(b) Term loan facilities and operating lines of credit:

As at March 31, 2020, the Company had the following term loan facilities and operating lines of credit:

Term loan facilities	Interest rate	Maturity date	Face value	Carrying value
ML LP term loan	BA + 1.95%	Jul 31, 2022	$ 41,600	$ 41,441
AM LP term loan	BA + 2.25%	Sep 6, 2022	17,400	17,299
SGRS LP term loan	BA + 2.00%	Jun 30, 2022	6,300	6,263
MRM LP term loan	BA + 1.95%	Jun 24, 2024	10,300	10,184
NNDH LP term loan	BA + 1.90%	Nov 15, 2024	14,500	14,326
			$ 90,100	$ 89,513

Operating lines of credit	Interest rate	Maturity date	Maximum available	Available for use
ML LP line of credit	Prime + 0.25%	Jul 31, 2022	$ 1,000	$ 1,000
AM LP line of credit	BA + 2.25%	Sep 6, 2022	3,000	3,000
SGRS LP line of credit	BA + 2.00%	Jun 30, 2022	500	500
MRM LP line of credit	Prime + 0.25%	Jun 24, 2024	500	500
			$ 5,000	$ 5,000

(Tabular amounts expressed in thousands of Canadian dollars)

9. Borrowings (continued):

(b) Term loan facilities and operating lines of credit (continued):

NND Holdings Limited Partnership ("NNDH LP"), a wholly-owned subsidiary of DIV, has a non-amortizing $14.5 million term loan, of which $7.5 million was drawn at December 31, 2019. The NNDH LP term loan was fully drawn at March 31, 2020.

As at March 31, 2020, the Company was in compliance with all financial covenants associated with its Acquisition Facility, term loan facilities and operating lines of credit. DIV is in regular discussions with its lending partners about the impact of COVID-19 on its business including covenant relief, which may be required in the months ahead dependent on the second quarter results of several of DIV's royalty partners.

10. Convertible debentures:

The following table reconciles the principal amount of the convertible debentures to the carrying value of the liability component.

	March 31, 2020	December 31, 2019
Principal amount	$ 57,500	$ 57,500
Equity component of debentures	(4,312)	(4,312)
Unamortized deferred financing fees	(1,485)	(1,608)
Accretion on liability component of debentures	1,818	1,614
	$ 53,521	$ 53,194

11. Interest rate swaps:

The following table summarizes the interest rate swap agreements the Company has entered into as of March 31, 2020:

	Effective date	Maturity date	Fixed interest rate	Notional amount
SGRS LP	Jun 19, 2018	Jun 21, 2021	4.64%	$ 6,300
ML LP	Aug 13, 2018	Jul 31, 2022	4.17%	34,600
ML LP	Feb 5, 2020	Jul 31, 2022	3.88%	7,000
AM LP	Sep 6, 2017	Aug 19, 2022	4.42%	8,700
MRM LP	Jul 25, 2019	Jun 24, 2024	4.05%	10,300
NNDH LP	Feb 12, 2020	Nov 15, 2024	3.98%	7,500

12. Exchangeable Units:

The fair value of the Exchangeable MRM Units is determined at the end of each period by multiplying the number of Exchangeable MRM Units held by Mr. Mikes at the end of the period by the closing price of DIV shares on the last business day of the period. As at March 31, 2020, the Exchangeable MRM Units were valued at $0.6 million (December 31, 2019 - $1.1 million) based on the DIV closing share price of $1.63 (December 31, 2019 - $3.14) at period end, multiplied by the total number of Exchangeable MRM Units of 355,032.

During the three months ended March 31, 2020, MRM LP issued distributions of $0.03 million to Mr. Mikes.

(Tabular amounts expressed in thousands of Canadian dollars)

13. Income taxes:

	Three months ended March 31, 2020		2019
Deferred income tax (recovery) expense	$ (4,895)	$	1,064
Current income tax expense	489		-
	$ (4,406)	$	1,064

The tax effect of temporary differences that gives rise to the net deferred tax liability are as follows:

	March 31, 2020	December 31, 2019
Intangible assets	$ 258	$ 263
Other	358	71
Financing and share issuance costs	311	(228)
Convertible debentures	(673)	(728)
Intangible assets	(7,001)	(11,591)
Net deferred tax liability	$ (6,747)	$ (12,213)

The deferred tax liability as at March 31, 2020 is largely associated with the temporary differences on the Company's intangible assets, which have an undepreciated capital cost allowance of approximately $222.1 million (December 31, 2019 - $181.0 million). In addition, pursuant to NND LP's limited partnership agreement, its undepreciated capital cost allowance of approximately $50.9 million at March 31, 2020 (December 31, 2019 – 51.5 million) is allocated to the Company for tax purposes.

14. Share capital:

On March 5, 2020, the Company completed a public offering of 10,810,000 common shares, including 1,410,000 common shares pursuant to the full exercise of the over-allotment option, at a price of $3.20 per common share, for gross proceeds of $34.6 million. After deducting issuance costs of $2.1 million, net proceeds were $32.5 million. The deferred tax impact of $0.6 million on the share issue costs was recognized within share capital.

The Company has a dividend reinvestment plan ("DRIP") that allows eligible holders of the Company's common shares to reinvest some or all cash dividends paid in respect of their common shares in additional common shares of the Company. The Company has temporarily suspended the DRIP, starting with the dividend payable to shareholders in respect of the month of April 2020.

(Tabular amounts expressed in thousands of Canadian dollars)

15. Share-based compensation:

(a) Restricted share units:

The number of RSUs outstanding is as follows:

	March 31, 2020		
	Number of RSUs		Weighted average grant-date fair value
Balance, beginning of period	941,762	$	3.31
Granted	5,779		3.13
Dividends earned	24,636		2.24
Balance, end of period	972,177	$	3.28
Unvested	917,221	$	3.29
Vested	54,956	$	3.05

(b) Share options:

The following table summarizes information relating to outstanding and exercisable options as at March 31, 2020:

	Options outstanding				Options exercisable		
Exercise prices	Number of options	Weighted average remaining life (years)		Weighted average exercise price per share	Number exercisable		Weighted average exercise price per share
$ 3.22 - $ 3.53	2,300,000	2.55	$	3.26	-	$	-
	2,300,000	2.55	$	3.26	-	$	-

16. (Loss) Income per share:

	Three months ended March 31,			
		2020		2019
(Loss) Income for the year	$	(11,731)	$	2,484
Weighted average number of shares outstanding – basic		112,699,189		107,840,033
Dilutive adjustment for RSUs		-		933,580
Weighted average number of shares outstanding – diluted		112,699,189		108,773,613
Net (loss) income per common share:				
Basic	$	(0.10)	$	0.02
Diluted	$	(0.10)	$	0.02

(Tabular amounts expressed in thousands of Canadian dollars)

17. Other finance income, net:

	Three months ended March 31, 2020	2019
Finance income	$ 22	$ 443
Foreign exchange (loss) gain	14	(4)
Distributions paid on Exchangeable MRM Units	(33)	-
Amortization of deferred financing charges	(195)	(144)
Accretion expense and other	1,159	(190)
	$ 967	$ 105

18. Financial instruments and financial risk management:

The Company must classify fair value measurements according to a hierarchy that reflects the significance of the inputs used in performing such measurements. The Company's fair value hierarchy comprises the following levels:

- Level 1 – quoted prices are available in active markets for identical assets or liabilities as of the reporting date. Active markets are those in which transactions occur in sufficient frequency and volume to provide pricing information on an ongoing basis.
- Level 2 – pricing inputs are other than quoted in active markets included in Level 1. Prices in Level 2 are either directly or indirectly observable as of the reporting date.
- Level 3 – valuations in this level are those with inputs for the asset or liability that are not based on observable data.

The carrying value of current financial assets and liabilities approximate their fair value due to their short-term nature. The carrying value of the long-term bank loans approximates their fair value as these facilities bear interest at floating market interest rates. The fair value of the convertible debentures of $54.1 million is measured using Level 1 inputs. The fair value of the Exchangeable MRM Units and the interest rate swap liabilities are measured using Level 2 inputs. The fair value of the investment in NND LP is measured using Level 3 inputs (note 7).

The Company monitors its consolidated cash flow to ensure that there will always be sufficient liquidity to meet liabilities when due. In addition, the Company manages its liquidity risk by preparing rolling cash flow forecasts, taking into consideration various scenarios and assumptions, monitoring the business operations of its royalty partners, and monitoring compliance with the terms of financing arrangements. Given the economic uncertainty facing DIV and its royalty partners as a result of the COVID-19 pandemic, the Company decreased the monthly dividend from $0.01958 per share to $0.01667 per share. The Board believes the reduction of the monthly dividend is a prudent measure to preserve capital and maintain liquidity in the current market environment.

As at March 31, 2020, the Company had a cash and cash equivalents balance of $9.5 million (December 31, 2019 - $3.0 million) and working capital of $13.2 million (December 31, 2019 - $9.3 million). The Company expects to have sufficient liquidity to meet liabilities when due,

(Tabular amounts expressed in thousands of Canadian dollars)

19. Supplemental cash flow information:

The following table reconciles the movements in liabilities to cash flows arising from financing activities:

	Promissory note	Acquisition facility (note 9(a))	Long-term debt (note 9(b))	Debentures (note 10)	Total
Balance, December 31, 2019	$ 4,805	$ (374)	$ 82,473	$ 53,194	$ 140,098
Changes from financing cash flows:					
Proceeds from issuance of debt	-	39,700	7,000	-	46,700
Repayment of debt	-	(30,700)	-	-	(30,700)
Liability-related other changes:					
Amortization of deferred financing charges	-	32	40	123	195
Accretion expense	(1,363)	-	-	204	(1,159)
Balance, March 31, 2020	$ 3,442	$ 8,658	$ 89,513	$ 53,521	$ 155,134

20. Subsequent event:

On April 27, 2020, OX LP entered into a credit agreement with a Canadian chartered bank for a senior credit facility (the “OX Credit Facility”) that comprises of a term loan facility of $9.0 million and a revolving facility of $0.5 million. The non-amortizing OX Credit Facility has a term of 60 months and has a floating interest rate equal to the Bankers’ Acceptance Rate plus 1.95%. The proceeds from the term loan facility were used to partially refinance the acquisition of the Oxford Rights, which closed on February 20, 2020 and was originally funded as a drawdown on DIV’s Acquisition Facility. In connection with receiving the proceeds from OX LP’s Credit Facility, the remaining balance that was outstanding under DIV’s acquisition facility of $9.0 million was repaid in full.