

Condensed Consolidated Interim Financial Statements of

DIVERSIFIED ROYALTY CORP.

Three and six months ended June 30, 2022 and 2021

(Unaudited)

DIVERSIFIED ROYALTY CORP.

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

	Note	June 30, 2022	December 31, 2021
Assets			
Current assets:			
Cash		\$ 5,865	\$ 8,939
Royalties and management fees receivable	5	5,474	4,911
Amounts receivable		8	11
Prepaid expenses and other		342	297
		11,689	14,158
Interest rate swap assets	10	2,932	647
Right-of-use asset and other		849	897
Investment in NND LP	6	43,319	44,467
Intangible assets	7	324,872	320,595
		\$ 383,661	\$ 380,764
Liabilities and Shareholders' Equity			
Current liabilities:			
Accounts payable and accrued liabilities		\$ 1,213	\$ 2,544
Interest rate swap liabilities	10	-	984
Income tax payable	12	765	2,121
Convertible debentures	9	4,932	55,968
		6,910	61,617
Long-term bank loans, net of deferred financing charges	8	109,855	109,750
Long-term convertible debentures	9	47,187	-
Promissory note		3,178	3,109
Exchangeable units and other	11	2,778	2,008
Interest rate swap liabilities	10	107	33
Lease obligation		800	829
Deferred income tax liability	12	15,004	11,893
Shareholders' equity:			
Share capital		207,251	201,972
Contributed surplus		39,665	39,450
Equity component of convertible debentures		3,971	2,938
Accumulated deficit		(53,045)	(52,835)
		197,842	191,525
		\$ 383,661	\$ 380,764

Nature of operations (note 1)

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

DIVERSIFIED ROYALTY CORP.

Condensed Consolidated Interim Statements of Net Income and Comprehensive Income

(Unaudited)

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

	Note	Three months ended June 30,			Six months ended June 30,		
		2022	2021	2022	2021	2022	2021
Royalty income	4	\$ 10,963	\$ 9,063	\$ 20,571	\$ 16,562		
Management fees		117	111	251	222		
		11,080	9,174	20,822	16,784		
Expenses:							
Salaries and benefits		552	566	1,098	889		
Share-based compensation	13	301	304	556	449		
General and administration		228	213	394	359		
Professional fees		125	246	204	329		
		1,206	1,329	2,252	2,026		
Income from operations		9,874	7,845	18,570	14,758		
Interest expense on credit facilities		(2,307)	(1,822)	(4,186)	(3,572)		
Other finance costs, net	15	(331)	(449)	(829)	(910)		
Fair value adjustment on financial instruments	6, 10, 11	2,350	1,627	4,619	2,657		
Income before income taxes		9,586	7,201	18,174	12,933		
Income tax expense	12	2,443	1,992	4,835	3,588		
Net income and comprehensive income		\$ 7,143	\$ 5,209	\$ 13,339	\$ 9,345		
Weighted average number of shares outstanding							
Basic		123,701,443	121,745,380	123,184,629	121,532,221		
Diluted		143,212,823	122,590,175	146,374,764	122,373,211		
Income per share							
Basic	14	\$ 0.06	\$ 0.04	\$ 0.11	\$ 0.08		
Diluted	14	\$ 0.06	\$ 0.04	\$ 0.10	\$ 0.08		

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, December 31, 2021		122,559,192 \$	201,972 \$	39,450 \$	2,938 \$	(52,835) \$	191,525
Common shares issued on DRIP		595,002	1,662	-	-	-	1,662
Restricted share units settled		81,582	195	(301)	-	-	(106)
Share-based compensation		-	-	516	-	-	516
Dividends declared		-	-	-	-	(13,549)	(13,549)
Redemption of convertible debentures	9	-	-	-	(1,058)	-	(1,058)
Issuance of convertible debentures	9	-	-	-	2,091	-	2,091
Addition to intangible assets	7	1,083,063	3,422	-	-	-	3,422
Comprehensive income		-	-	-	-	13,339	13,339
Balance as at June 30, 2022		124,318,839 \$	207,251 \$	39,665 \$	3,971 \$	(53,045) \$	197,842

	Note	Common shares	Share capital	Contributed surplus	Equity component of convertible debentures	Accumulated deficit	Total equity
Balance, December 31, 2020		121,187,757 \$	198,570 \$	39,425 \$	2,938 \$	(51,260) \$	189,673
Common shares issued on DRIP		609,793	1,484	-	-	-	1,484
Restricted share units settled		141,579	254	(408)	-	-	(154)
Share-based compensation		-	-	370	-	-	370
Dividends declared		-	-	-	-	(12,158)	(12,158)
Comprehensive income		-	-	-	-	9,345	9,345
Balance as at June 30, 2021		121,939,129 \$	200,308 \$	39,387 \$	2,938 \$	(54,073) \$	188,560

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DIVERSIFIED ROYALTY CORP.

Condensed Consolidated Interim Statements of Cash Flows

(Unaudited)

(Expressed in thousands of Canadian dollars)

	Note	Three months ended June 30,		Six months ended June 30,	
		2022	2021	2022	2021
Operating activities:					
Net income		\$ 7,143	\$ 5,209	\$ 13,339	\$ 9,345
Adjustments for:					
Tax expense	12	2,443	1,992	4,835	3,588
Depreciation expense		24	23	49	41
Share-based compensation		301	304	556	449
Fair value adjustments on financial instruments		(2,350)	(1,627)	(4,619)	(2,657)
Interest expense on credit facilities		2,307	1,822	4,186	3,572
Other finance costs, net		331	449	829	910
Foreign exchange gain (loss)		3	(6)	2	(3)
Interest paid		(3,070)	(2,577)	(4,186)	(3,572)
Interest received		61	6	69	19
Taxes paid		(1,949)	(530)	(3,910)	(1,657)
Distributions received from NND LP		1,240	1,217	2,486	2,440
Changes in non-cash operating items:					
Royalties and management fees receivable		(625)	(512)	(563)	(388)
Amounts receivable		29	(43)	3	(37)
Prepaid expenses and other		54	(38)	95	(58)
Accounts payable and accrued liabilities		(1,322)	(919)	(2,206)	(1,126)
Cash flows generated from operating activities		4,620	4,770	10,965	10,866
Financing activities:					
Proceeds from issuance of convertible debentures, net of fees	9	-	-	50,400	-
Redemption of convertible debentures	9	(52,500)	(269)	(52,500)	(269)
Payment of dividends		(5,955)	(5,360)	(11,887)	(10,674)
Payment of lease obligations		(26)	(8)	(52)	(8)
Proceeds from issuance of debt		-	11,400	-	11,400
Cash flows generated from (used in) financing activities		(58,481)	5,763	(14,039)	449
Investing activities:					
Additions to intangible assets	7	-	(16,051)	-	(16,051)
Purchase of fixed assets		-	(223)	-	(223)
Cash flows used in investing activities		-	(16,274)	-	(16,274)
Net decrease in cash		(53,861)	(5,741)	(3,074)	(4,959)
Cash, beginning of the period		59,726	10,000	8,939	9,218
Cash, end of the period		\$ 5,865	\$ 4,259	\$ 5,865	\$ 4,259

Supplemental cash flow information (note 17)

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

DIVERSIFIED ROYALTY CORP.

Notes to Condensed Consolidated Interim Financial Statements
(Unaudited)
(Tabular amounts expressed in thousands of Canadian dollars)

For the three and six months ended June 30, 2022 and 2021

Diversified Royalty Corp. (“DIV”) is a company domiciled in Canada and governed by the Business Corporations Act (British Columbia). The condensed consolidated interim financial statements of DIV as at and for the three and six months ended June 30, 2022 are composed of DIV and its subsidiaries (together referred to as the “Company”). The head office of the Company is located at 330-609 Granville Street, Vancouver, BC, V7Y 1A1. The registered office of the Company is located at the 25th Floor, 700 West Georgia Street, Vancouver, BC, V7Y 1B3. The Company’s common shares are listed on the Toronto Stock Exchange (“TSX”) and traded under the symbol “DIV”.

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”). The Company’s Royalty Partners and the respective license and royalty arrangements are summarized below.

Sutton Group Realty Services Ltd. (“Sutton”): SGRS Royalties Limited Partnership (“SGRS LP”) (an entity controlled by the Company), owns the trademarks and certain other intellectual property rights utilized by Sutton in its residential real estate franchise business (the “SGRS Rights”). The Company granted Sutton the licence to use the SGRS Rights in exchange for a royalty payment currently equal to \$63.347 per agent per month (the “Sutton Royalty Rate”) for the number of agents included in the royalty pool (the “Sutton Royalty Pool”).

Mr. Lube Canada Limited Partnership (“Mr. Lube”): ML Royalties Limited Partnership (“ML LP”) (an entity controlled by the Company) owns the trademarks and certain other intellectual property rights utilized by Mr. Lube in its business (the “ML Rights”). The Company granted Mr. Lube the licence to use the ML Rights in exchange for a royalty payment currently equal to 7.95% of non-tire system sales and 2.50% of tire system sales of Mr. Lube locations in the royalty pool (the “Mr. Lube Royalty Pool”).

LoyaltyOne Co. (“LoyaltyOne”): AM Royalties Limited Partnership (“AM LP”) (a wholly owned subsidiary of the Company) owns the Canadian AIR MILES® trademarks and certain Canadian intellectual property rights (collectively, the “AIR MILES® Rights”) used by LoyaltyOne in operating the AIR MILES® reward program in Canada (the “AIR MILES® Program”). In accordance with the terms of two license agreements with LoyaltyOne (collectively the “AIR MILES® Licenses”), LoyaltyOne has an exclusive right to use the AIR MILES® Rights in exchange for a royalty payment equal to 1% of gross billings from the AIR MILES® Program.

Mr. Mikes Restaurants Corporation (“Mr. Mikes”): MRM Royalties Limited Partnership (“MRM LP”) (an entity controlled by the Company) owns the trademarks and certain other intellectual property rights utilized by Mr. Mikes in its restaurant business (the “MRM Rights”). The Company granted Mr. Mikes the licence to use the MRM Rights in exchange for a royalty payment currently equal to 4.35% of notional system sales of Mr. Mikes locations in the royalty pool (the “Mr. Mikes Royalty Pool”).

Nurse Next Door Professional Homecare Services Inc. (“Nurse Next Door”): NND Royalties Limited Partnership (“NND LP”) (an entity that is majority-owned by the Company) has legal ownership of 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 6). NND LP granted Nurse Next Door the licence to use the NND Rights. The Company, through its ownership of NND LP Class A units, is currently entitled to receive a cash distribution, currently equal to \$0.42 million per month, which grows at a fixed rate of 2.0% per annum (the “DIV Distribution Entitlement”).

Oxford Learning Centres, Inc. (“Oxford”): OX Royalties Limited Partnership (“OX LP”) (an entity controlled by the Company) owns the trademarks and certain other intellectual property rights utilized by Oxford Learning Centres, Inc. (“Oxford”) in its supplemental education business (the “Oxford Rights”). The Company granted Oxford the licence to use the Oxford Rights in exchange for a royalty payment currently equal to 7.67% of the gross sales of Oxford locations in the royalty pool (the “Oxford Royalty Pool”).

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.

DIVERSIFIED ROYALTY CORP.

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1. Nature of operations (continued):

COVID-19

Since the onset of the COVID-19 pandemic in March 2020, jurisdictions across Canada have had varying levels of COVID-19 related restrictions in place and many of those restrictions have been modified multiple times in response to the fluctuating number of COVID-19 cases, the appearance of new COVID-19 variants, and vaccination levels. The situation remains dynamic and the ultimate duration and magnitude of the impact on the economy, our business and the respective businesses of our Royalty Partners (including their respective franchisees) remains uncertain. Government restrictions, which have included, among others, the temporary closure of non-essential businesses (in most jurisdictions), restrictions on business operations, bans on public gatherings over certain sizes and travel advisories to avoid non-essential travel, may continue or be re-imposed at any time. Accordingly, DIV does not know the full extent of the financial impact of such interruptions going forward. DIV's Royalty Partners (including their respective franchisees) have had, and may continue to have in the months ahead, significant interruptions to their respective businesses, including prolonged periods of low system sales on which certain royalties are based and low revenues on which the Royalty Partner rely to pay royalties to DIV. In addition, the rates of recovery for DIV's Royalty Partners have and will continue to be dependent upon, among other things, the availability, effectiveness and the individual take-up rate of vaccines for the COVID-19 virus, government responses, rates of economic recovery, precautionary measures taken by consumers and the rate at which social restrictions are lifted. Recently experienced improvement trends by certain of DIV's Royalty Partners may not continue and may regress. There is also a risk that certain Royalty Partner franchise locations that temporarily closed may not reopen, and those that are open may be required to close again in the future as a direct or indirect result of the impacts of COVID-19 and related government restrictions. 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, and result in an impairment in the value of the long-lived assets or investments or decreases in revenue or the profitability of DIV's 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, 2021.

These condensed consolidated interim financial statements were authorized and approved for issue by the Company's Board of Directors on August 12, 2022.

(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 consolidated financial statements for the year ended December 31, 2021.

(c) Functional and presentation currency:

These condensed consolidated interim 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 consolidated financial statements for the year ended December 31, 2021.

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4. Royalty income:

	Three months ended June 30,		Six months ended June 30,	
	2022	2021	2022	2021
Mr. Lube	\$ 6,109	\$ 4,698	\$ 10,862	\$ 8,273
AIR MILES®	1,791	1,623	3,321	3,148
Mr. Mikes ¹	912	823	2,191	1,320
Oxford	1,125	913	2,145	1,809
Sutton	1,026	1,006	2,052	2,012
	\$ 10,963	\$ 9,063	\$ 20,571	\$ 16,562

1) For the six months ended June 30, 2022, Mr. Mikes royalty income includes a one-time payment of \$0.55 million representing partial payment of deferred contractual royalty fees and deferred contractual management fees, which has been recognized as revenue upon collection.

For the six months ended June 30, 2022 and 2021, DIV granted royalty relief to Mr. Mikes in connection with the COVID-19 pandemic, collecting 79% of the contractual royalty amounts for the six months ended June 30, 2022 and 65% for the six months ended June 30, 2021. DIV continues to discuss with its lender and Mr. Mikes about whether additional royalty relief is required for subsequent periods.

Effective July 1, 2022, the monthly Sutton Royalty Rate increased from \$63.347 per agent to \$64.614 per agent.

5. Royalties and management fees receivable:

	June 30,	December 31,
	2022	2021
Mr. Lube	\$ 2,136	\$ 1,813
AIR MILES®	2,024	2,003
Mr. Mikes	517	366
Oxford	421	353
Sutton	369	369
Nurse Next Door	7	7
	\$ 5,474	\$ 4,911

6. Investment in NND LP:

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 June 30, 2022, and December 31, 2021. The contractual cash flows receivable from Nurse Next Door were discounted at a rate of 14.4% (December 31, 2021 – 13.9%).

The total fair value of NND LP at June 30, 2022, was \$43.3 million (December 31, 2021 - \$44.5 million) and a fair value gain of \$1.3 million was recorded during the six months ended June 30, 2022 (2021 – \$2.1 million). A one percentage point increase in the discount rate would decrease the fair value by \$3.1 million. A one percentage point decrease in the discount rate would increase the fair value by \$3.6 million.

For the six months ended June 30, 2022, the DIV Distribution Entitlement was \$2.5 million gross and net of expenses incurred by NND LP (June 30, 2021 - \$2.5 million gross and net of expenses incurred by NND LP).

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7. Intangible Assets:

	ML Rights (a)	AIR MILES (b)	SGRS Rights (c)	MRM Rights (d)	Oxford Rights (e)	Total
Balance, December 31, 2021	\$ 170,958	\$ 48,810	\$ 32,273	\$ 29,050	\$ 39,504	\$ 320,595
Additions	4,277	-	-	-	-	4,277
Balance, June 30, 2022	\$ 175,235	\$ 48,810	\$ 32,273	\$ 29,050	\$ 39,504	\$ 324,872

On November 9, 2020, DIV and Mr. Lube entered into an amendment to the amended and restated limited partnership agreement of ML LP (the "LP Amendment") to confirm the terms on which the Mr. Lube Royalty Pool will be adjusted to include royalties from 13 additional Mr. Lube locations effective May 1, 2021.

The initial consideration paid on May 1, 2021, for the addition of the 13 locations to the Mr. Lube Royalty Pool was determined to be \$7.7 million, representing 80% of the total estimated consideration of \$9.6 million. After adjusting to reflect the actual system sales of these locations for the year ending December 31, 2021, DIV paid Mr. Lube the remaining \$1.6 million of cash consideration for the net additional royalty revenue related to 7 of the 13 locations on May 1, 2022. The remaining consideration payable for the net additional royalty revenue related to 6 of the 13 locations will be paid to Mr. Lube on May 1, 2023 and will be adjusted to reflect the actual system sales of these locations for the year ending December 31, 2022. As at June 30, 2022, the remaining consideration payable to Mr. Lube was \$1.0 million, recorded to exchangeable units and other (note 11b) on the statement of financial position.

On May 1, 2022, the Mr. Lube Royalty Pool was adjusted to include the royalties from 6 new Mr. Lube locations and to remove two Mr. Lube locations for which make-whole payments were being made due to the store closures in 2021. The initial consideration for the addition of 6 new stores to the Mr. Lube Royalty Pool was determined to be \$3.4 million, representing 80% of the total consideration of \$4.3 million, based on the forecast system sales of these 6 locations for the 2022 fiscal year. DIV elected to pay the initial consideration in shares and issued 1,083,063 DIV shares to Mr. Lube, valued at \$3.1592 per share based on the weighted average share price of the Company's shares over the 20 trading days ending on April 25, 2022, the fifth trading day before May 1, 2022. In exchange for the 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. The remaining 20% consideration payable for the additional royalty revenue related to the 6 locations will be paid to Mr. Lube on May 1, 2023 and will be adjusted to reflect the actual system sales of these locations for the year ending December 31, 2022. As at June 30, 2022, the remaining consideration payable to Mr. Lube was \$0.8 million, recorded to exchangeable units and other (note 11b) on the statement of financial position.

In addition, on May 1, 2022, Mr. Lube elected to defer the third royalty rate increase until the next adjustment date in respect of which the Mr. Lube royalty rate will be eligible to be increased.

8. Borrowings:

(a) Acquisition facility:

The Company has a \$50.0 million undrawn senior secured credit facility (the "Acquisition Facility") that matures on April 20, 2026. As at June 30, 2022, the Company had \$nil outstanding under the Acquisition Facility.

On April 20, 2022, DIV amended its Acquisition Facility to allow for a one-time advance of up to \$9.0 million to be used to partially fund the repayment of DIV's outstanding convertible debentures due on December 31, 2022 ("2022 Debentures") and to extend the maturity date of the Acquisition Facility to April 20, 2026. In addition, the Company incurred transaction costs of \$0.2 million, which were recorded to prepaid expenses and other on the balance sheet and will be amortized over the term of the Acquisition Facility.

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8. Borrowings (continued):

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

As at June 30, 2022, the Company had the following term loan facilities:

Term loan facilities	Interest rate	Maturity date	Face value	Carrying value
ML LP term loan	BA + 2.50%	May 1, 2025	\$ 53,000	\$ 52,741
AM LP term loan	BA + 1.95%	Sep 30, 2026	17,400	17,268
SGRS LP term loan	BA + 1.95%	Jun 30, 2026	6,300	6,256
MRLP term loan	BA + 1.95%	Jun 24, 2024	10,300	10,244
NNDH LP term loan	BA + 1.90%	Nov 15, 2024	14,500	14,408
OX LP term loan	BA + 1.95%	Apr 27, 2025	9,000	8,938
			\$ 110,500	\$ 109,855

As at June 30, 2022, the Company had the following operating lines of credit:

Operating lines of credit	Interest rate	Maturity date	Maximum available	Available for use
ML LP term loan	Prime + 0.25%	May 1, 2025	\$ 1,000	\$ 1,000
AM LP term loan	BA + 1.95%	Sep 30, 2026	3,000	3,000
SGRS LP term loan	BA + 1.95%	Jun 30, 2026	500	500
MRLP term loan	Prime + 0.25%	Jun 24, 2024	500	500
OX LP term loan	Prime + 0.25%	Apr 27, 2025	500	500
			\$ 5,500	\$ 5,500

As at June 30, 2022, the Company was in compliance with all financial covenants associated with its Acquisition Facility, term loan facilities and operating lines of credit. The AM Credit Agreement was amended and restated in September 2021 in order to, among other things, amend the financial covenants for the last fiscal quarter of 2021 and for the first two quarters of 2022. If AM LP had not received such waivers or entered into such amendment, AM LP would have been in breach of its financial covenants as of June 30, 2022.

9. Convertible Debentures:

On March 30, 2022, the Company issued convertible unsecured subordinated debentures ("2027 Debentures") for an aggregate principal amount of \$52.5 million at a price of \$1,000 per debenture ("the Offering"). The 2027 Debentures mature on June 30, 2027 and bear interest at an annual rate of 6.00% payable semi-annually in arrears on the last day of December and June in each year, commencing June 30, 2022. At the holder's option, the 2027 Debentures may be converted into common shares of the Company at any time prior to the earlier of the last business day immediately preceding June 30, 2027 and the date specified by the Company for redemption. The conversion price will be \$4.05 per common share (the "Conversion Price"), subject to adjustment in certain circumstances.

The 2027 Debentures are not redeemable prior to June 30, 2025, except upon the satisfaction of certain conditions after a change of control has occurred. On and after June 30, 2025 and prior to June 30, 2026, the 2027 Debentures may be redeemed in whole or in part from time to time at DIV's option, provided that the volume weighted average trading price of the common shares on the TSX during the 20 consecutive trading days ending on the fifth trading day preceding the date on which the notice of the redemption is given is not less than 125% of the Conversion Price. On or after June 30, 2026 and prior to the maturity date, DIV may, at its option, redeem the 2027 Debentures, in whole or in part, from time to time at par plus accrued and unpaid interest. On redemption or at maturity, the Company will repay the indebtedness of the 2027 Debentures by paying an amount equal to the principal amount of the outstanding debentures, together with accrued and unpaid interest thereon.

The Company may, at its option, elect to satisfy its obligation to repay the principal amount of the 2027 Debentures, which are to be redeemed or which have matured, by issuing shares to the holders of the convertible debentures. The number of shares to be issued will be determined by dividing \$1,000 of principal amount of the debentures by 95% of the then current market price on the maturity date.

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9. Convertible Debentures (continued):

On initial recognition, the Company valued the liability component of the 2027 Debentures at \$49.4 million and the equity component at \$3.1 million. In addition, the Company incurred transaction costs of \$2.6 million, of which \$2.4 million was allocated to the liability component and \$0.2 million was allocated to the equity component. The net amount recognized as the equity component of the 2027 Debentures, after deferred taxes of \$0.8 million, was \$2.1 million.

On May 4, 2022, ("Redemption Date"), the Company used the net proceeds from the Offering to complete the \$52.5 million partial redemption of the principal amount of the 2022 Debentures outstanding plus accrued and unpaid interest at 5.25% up to, but excluding, the Redemption Date. As a result of the partial redemption, \$1.1 million was removed from the equity component of convertible debentures.

The following table reconciles the principal amount of the 2022 Debentures to the carrying value of the liability component:

		June 30, 2022	December 31, 2021
Principal amount - 2022 Debentures	\$	57,500	\$ 57,500
Partial Redemption - principal amount		(52,500)	-
Partial Redemption - deferred financing fees		(393)	-
Equity component		(4,312)	(4,312)
Partial Redemption - equity component		1,058	-
Unamortized deferred financing fees		(25)	(570)
Accretion on liability component		3,604	3,350
Current portion of convertible debentures	\$	4,932	\$ 55,968

The following table reconciles the principal amount of the 2027 Debentures to the carrying value of the liability component:

		June 30, 2022	December 31, 2021
Principal amount - 2027 Debentures	\$	52,500	\$ -
Equity component		(3,074)	-
Unamortized deferred financing fees		(2,362)	-
Accretion on liability component		123	-
Long-term portion of convertible debentures	\$	47,187	\$ -

10. Interest rate swaps:

The following table summarizes the interest rate swap agreements the Company has entered into as of June 30, 2022. The Company recorded a fair value gain of \$3.2 million related to the interest rate swaps for the six months ended June 30, 2022.

Term loan facilities	Effective date	Maturity date	Fixed interest rate	Notional amount
ML LP	Aug 13, 2018	Jul 31, 2022	4.72% \$	34,600
ML LP	Feb 5, 2020	Jul 31, 2022	4.43%	7,000
ML LP	Jul 29, 2022	May 1, 2025	4.25%	39,750
AM LP	Sep 6, 2017	Aug 19, 2022	4.12%	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
OX LP	Aug 26, 2020	Apr 27, 2025	2.96%	4,500

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11. Exchangeable Units and Other:

(a) MRM Units:

Mr. Mikes is entitled to receive distributions from MRM LP on the retained interest on a pro rata basis with the limited partnership units of MRM LP (the "MRM Units") held by DIV. The MRM Units are recorded as a liability and measured at fair value. The distributions issued by MRM LP to Mr. Mikes are recorded as an expense on the Company's income statement.

The fair value of the MRM Units is determined at the end of each period by multiplying the number of 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 June 30, 2022, the MRM Units were valued at \$0.9 million based on the DIV closing share price of \$2.58 at period end (December 31, 2021 - \$2.82), multiplied by the total number of MRM Units of 355,032.

(b) ML Units:

The balance as at June 30, 2022 of \$1.8 million (December 31, 2021 - \$1.0 million) in exchangeable units and other relates to the consideration payable to Mr. Lube, of which \$1.0 million is related to the remaining consideration payable for the 2021 addition of 6 of the 13 locations to be paid to Mr. Lube on May 1, 2023 and \$0.8 million is related to the remaining 20% consideration payable for the additional royalty revenue related to the 2022 addition of 6 locations to be paid to Mr. Lube on May 1, 2023 (refer to note 7). There have been no fair value adjustments since December 31, 2021.

12. Income Taxes:

	Three months ended June 30,		Six months ended June 30,	
	2022	2021	2022	2021
Deferred income tax expense	\$ 1,010	\$ 1,100	\$ 2,281	\$ 2,021
Current income tax expense	1,433	892	2,554	1,567
	\$ 2,443	\$ 1,992	\$ 4,835	\$ 3,588

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

	June 30,	December 31,
	2022	2021
Intangible assets	\$ 219	\$ 227
Financing and share issuance costs	93	93
Convertible debentures	(841)	(260)
Other	(1,202)	(358)
Intangible assets	(13,273)	(11,595)
Net deferred income tax liability	\$ (15,004)	\$ (11,893)

The deferred tax liability as at June 30, 2022 is largely associated with the temporary differences on the Company's intangible assets, which have an undepreciated capital cost allowance of approximately \$193.0 million (December 31, 2021 - \$199.2 million). In addition, pursuant to NND LP's limited partnership agreement dated November 15, 2019, its undepreciated capital cost allowance of approximately \$45.3 million at June 30, 2022 (December 31, 2021 - \$46.5 million) is allocated to the Company for tax purposes.

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13. Share-based compensation:

(a) Restricted share units ("RSUs"):

The number of RSUs outstanding as at June 30, 2022, is as follows:

	June 30, 2022	
	Number of RSUs	Weighted average grant- date fair value
Balance, beginning of period	452,178	\$ 2.05
Granted	301,807	2.88
Dividends earned	25,548	2.89
Settled	(126,350)	3.12
Balance, end of period	653,183	\$ 2.26
Unvested	653,183	\$ 2.26

(b) Share options:

The following table summarizes the changes in the Company's share options during the six months ended June 30, 2022:

	June 30, 2022	
	Number of options	Weighted average exercise price
Balance, beginning of period	3,041,667	\$ 3.06
Granted	791,667	2.80
Balance, end of period	3,833,334	\$ 3.01

The following table summarizes information relating to outstanding and exercisable options as at June 30, 2022:

Expiry Date	Exercise Price	Weighted average remaining life (years)	Options outstanding	Options exercisable
November 23, 2022	\$ 3.22	0.28	2,000,000	2,000,000
October 11, 2022	3.53	0.40	250,000	250,000
May 6, 2026	2.52	3.85	791,667	263,889
January 1, 2027	2.80	4.51	791,667	-
Balance, end of period		1.90	3,833,334	2,513,889

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14. Income per share:

	Three months ended June 30,		Six months ended June 30,	
	2022	2021	2022	2021
Income for the period - basic	\$ 7,143	\$ 5,209	\$ 13,339	\$ 9,345
Interest expense on convertible debentures, net of tax	991	-	1,823	-
Income for the period - diluted	\$ 8,134	\$ 5,209	\$ 15,162	\$ 9,345
Weighted average number of shares outstanding - basic	123,701,443	121,745,380	123,184,629	121,532,221
Effective impact of dilutive securities:				
Share options	106,009	-	143,225	-
RSUs	677,401	489,763	725,211	485,958
Convertible debentures - current & long term	18,372,938	-	21,966,667	-
Exchangeable MRM units	355,032	355,032	355,032	355,032
Weighted average number of shares outstanding - diluted	143,212,823	122,590,175	146,374,764	122,373,211
Net income per common share				
Basic	\$ 0.06	\$ 0.04	\$ 0.11	\$ 0.08
Diluted	\$ 0.06	\$ 0.04	\$ 0.10	\$ 0.08

15. Other finance costs, net:

	Three months ended June 30,		Six months ended June 30,	
	2022	2021	2022	2021
Finance income	\$ 61	\$ 6	\$ 69	\$ 19
Foreign exchange (loss) gain	3	(6)	2	(3)
Amortization of deferred financing charges	(206)	(179)	(430)	(393)
Accretion expense and other	(189)	(270)	(470)	(533)
	\$ (331)	\$ (449)	\$ (829)	\$ (910)

16. Financial instruments:

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 is measured using Level 1 inputs. The fair value of the MRM Units, ML Units and the interest rate swap liabilities are measured using Level 2 inputs. The fair value of the investment in NND LP (note 6) is measured using Level 3 inputs.

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16. Financial instruments (continued):

The following table represents the fair value hierarchy of financial assets:

As at June 30, 2022	Carrying value		Fair value hierarchy		
	FVTPL	Amortized cost	Level 1	Level 2	Level 3
Financial assets					
Cash and cash equivalents	\$ -	\$ 5,865	\$ -	\$ -	\$ -
Royalties and management fees receivable	-	5,474	-	-	-
Amounts receivable	-	8	-	-	-
Interest rate swap assets	2,932	-	-	2,932	-
Investment in NND LP	43,319	-	-	-	43,319
	\$ 46,251	\$ 11,347	\$ -	\$ 2,932	\$ 43,319

The following table represents the fair value hierarchy of financial liabilities:

As at June 30, 2022	Carrying value		Fair value hierarchy		
	FVTPL	Amortized cost	Level 1	Level 2	Level 3
Financial liabilities					
Accounts payable and accrued liabilities	\$ -	\$ 1,213	\$ -	\$ -	\$ -
Long-term bank loans	-	109,855	-	-	-
Promissory note	-	3,178	-	-	-
Lease obligation	-	800	-	-	-
Convertible debentures - current	-	4,932	4,932	-	-
Convertible debentures - long term	-	47,187	47,187	-	-
Interest rate swap liabilities	107	-	-	107	-
Exchangeable MRM Units	2,778	-	-	2,778	-
	\$ 2,885	\$ 167,165	\$ 52,119	\$ 2,885	\$ -

17. Supplemental cash flow information:

The following table represents significant non-cash transactions:

	Three months ended June 30,		Six months ended June 30,	
	2022	2021	2022	2021
Non-cash transactions:				
Additions to intangible assets, settled in shares	\$ 3,422	\$ -	\$ 3,422	\$ -