IOU Financial

Business Lending. Simplified.

IOU Financial Inc.

Annual Report 2019

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IOU FINANCIAL INC.

Management's Discussion and Analysis of Financial Condition and Results of Operations

INTRODUCTION

The following management's discussion and analysis ("MD&A") of IOU Financial Inc. ("IOU Financial" or the "Company"), prepared as of April 29, 2020, should be read in conjunction with, and is qualified in its entirety by reference to the condensed consolidated financial statements as at and for the years ended December 31, 2019 and 2018 and related notes which have been prepared in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB").

All amounts are expressed in Canadian dollars unless otherwise indicated.

OVERVIEW

IOU Financial provides small businesses throughout the US and Canada access to the capital they need to seize growth opportunities quickly. In a unique approach to lending, IOU Financial's advanced, automated application and approval system accurately assesses applicants' financial realities, with an emphasis on day-to-day cash flow trends. IOU Financial allows these businesses to apply for six, nine, twelve, fifteen and eighteen-month term loans of up to US$500,000 to qualified US applicants ($150,000 in Canada) within a few business days, with affordable charges favorable to cash-flow management. Its speed and transparency make IOU Financial a trusted alternative to banks. To lean more visit: IOUFinancial.com.

As at December 31, 2019, IOU Financial's customers had been in business an average 11.6 years (based on their incorporation date) at the time of application. These businesses borrowed on average US$74,279 for a weighted average term of 12.0 months and generally used the funds for working capital purposes, to purchase new equipment, invest in an increased workforce, attend to repairs, expand their business, purchase more inventory or increase marketing efforts**.**

IOU Financial finances its lending activities in part by selling some of its commercial loans receivable to third party purchasers on a non-recourse basis and retaining the servicing rights for these loans in exchange for a service fee.

As a lender, IOU Financial earns revenue from fees it charges to its borrowers, interest payments it receives on loans it has funded, gains on the sale of loans it has sold as well as servicing fees it charges third-party purchasers for servicing the loans. A referral fee is earned on loans that are referred to and funded by other third-party lenders.

IOU Financial's common shares trade on the TSX Venture Exchange ("TSX-V") under the symbol "IOU". Since commencing commercial lending operations in December of 2009 until December 31, 2019, the Company has originated approximately US$789.0 million. IOU Financial had 51 full-time employees as at December 31, 2019.

CORPORATE HISTORY

IOU Financial is the continuation of Matco Ravary Inc. (“Matco Ravary”), a Company founded in 1977, which specialized for over 40 years in the retailing of home improvement and building materials. On November 1, 2002, Matco Ravary sold its operating assets to a company involved in the same sector, thereby ceasing all operations in the home improvement and building materials retailing sector. On May 14, 2004, substantially all of its issued and paid-up capital was distributed to its shareholders.

On April 29, 2005, Matco Ravary changed its corporate name to MCO Capital Inc. (“MCO”). During the following fiscal years, the main business and objective of MCO was to identify and evaluate businesses and assets with a view to a potential acquisition.

On February 28, 2011, MCO completed a reverse acquisition and acquired all of the issued and outstanding shares of IOU Central Inc. (“IOU Central”), a Canadian corporation incorporated in August 2006. On the same day, MCO also acquired all of the issued and outstanding shares of IOU USA, other than the shares of IOU USA already held by IOU Central. IOU USA was incorporated in Delaware in August 2006. In connection with the completion of the reverse acquisition, MCO effected a share consolidation and changed its name from “MCO Capital Inc.” to “IOU Financial Inc.”

FORWARD-LOOKING STATEMENTS

Statements made in this MD&A that describe IOU Financial’s or management’s budgets, estimates, expectations, forecasts, objectives, predictions or projections of the future may be “forward-looking statements”. Forward-looking statements are statements, other than statements of historical fact, that address or discuss activities, events or developments that IOU Financial expects or anticipates may occur in the future. The forward-looking statements can be identified by the use of the conditional or forward-looking terminology such as “anticipates”, “believes”, “estimates”, “expects”, “may”, “plans”, “projects”, “should”, “will”, or the negative thereof or other variations thereon.

IOU Financial cautions that, by their nature, forward-looking statements involve risks and uncertainties. A number of factors could cause actual results, performance or developments to differ materially from those expressed or implied by such forward-looking statements, including but not limited to, risks inherent in growing a new business, dependence on third-party service providers, competition, regulatory risk, dependence on key personnel, risks related to rapid growth of the Company, security and confidentiality risk, risk related to inability to attract borrowers and lenders, technological development risk, IT disruptions, maintenance of client relationships, litigation risk, volatility of stock price, and other factors that are beyond its control. IOU Financial cautions that the foregoing list of factors is not exhaustive. For more information on risks and uncertainties and assumptions that would cause the company’s actual results to differ from current expectations, please refer to the section “Risks and Uncertainties” of this MD&A.

The forward-looking statements in this MD&A reflect IOU Financial’s views as at the date of this MD&A and are based on certain assumptions including assumptions as to future economic conditions and courses of action, as well as other factors management believes are appropriate in the circumstances. IOU Financial does not undertake any obligation to update publicly or to revise any such forward-looking statements, unless required by applicable legislation or regulation.

OVERALL PERFORMANCE AND SELECTED FINANCIAL INFORMATION

The following table summarizes key financial data for each of the respective periods. The financial information presented below has been presented in Canadian dollars (except where otherwise noted) and has been prepared in accordance with International Financial Reporting Standards (IFRS).

Summarized Financial Data

For the year ended December 31	**2019** **$**	2018 $
Loan originations ($US)	**154,221,080**	124,966,233
Principal balance of loan portfolio	**56,871,350**	34,504,755
Principal balance of servicing portfolio	**53,900,047**	61,431,330
Total loans under management	**110,771,397**	95,936,085
Adjusted gross revenue (1)	**23,699,254**	18,444,266
Interest expense	**3,998,673**	3,355,496
Provision for loan losses	**7,951,635**	5,004,324
Adjusted operating expenses (2)	**10,117,365**	8,369,410
Adjusted net earnings(3)	**1,758,254**	2,152,712
Adjusted net earnings per share(4)	**0.02**	0.02
Net earnings	**1,523,309**	2,710,218
Net earnings per share(4)	**0.02**	0.03
Total assets	**63,832,810**	43,731,098
Total liabilities	**50,682,432**	31,875,324

(1) IOU Financial's adjusted gross revenue is defined as gross revenue prepared in accordance with IFRS for the period, plus amortization of servicing assets less gain on sale of loans. The Company uses adjusted gross revenue as it eliminates items that do not necessarily reflect how the Company is performing. Specifically, it eliminates the non-cash gain on sale of loans and the non-cash amortization of servicing assets which influence operating results depending on the timing and amount of the loan sales.

(2) IOU Financial's adjusted operating expenses is defined as total operating expenses prepared in accordance with IFRS for the period less: non-cash stock-based compensation which is given at different times and prices, and non-recurring costs, plus non-recurring gains which affects operating results only periodically. The Company uses adjusted operating expenses as it eliminates items that do not necessarily reflect how the Company is performing.

(3) Beginning in the first quarter of 2019, the calculation of adjusted net earnings was revised and is defined as net earnings for the period prepared in accordance with IFRS less: gain on sale of loans and non-recurring gains, plus: amortization of servicing assets, stock-based compensation and non-recurring costs. Prior to the first quarter of 2019, the calculation of adjusted net earnings (net loss) was defined as net earnings (net loss) for the period prepared in accordance with IFRS less: gain on sale of loans and income tax recovery, plus: amortization of servicing assets, stock-based compensation, amortization of transactions costs-financing credit facilities, depreciation and amortization, income tax expense and non-recurring costs. As a result, the prior comparative periods have been calculated to reflect the revised definition. The Company uses adjusted net earnings as a measure of financial performance.

(4) Basic and diluted. The adjusted net earnings and net earnings per share has been calculated using the weighted average number of shares outstanding during each period.

IOU Financial's innovative lending platform continues to be a viable solution to the challenges small businesses face when trying to obtain financing. IOU Financial believes that a large opportunity exists to expand its presence in what it believes is a significantly underserved market.

In 2019, the Company funded US$154.2 million in loans (2018: US $125.0 million), representing an increase of 23.4% over 2018. This was driven by identifying, recruiting, partnering and promoting existing relationships with business loan brokers, continued geographic expansion into Canada and investing in direct marketing and sales. This was in line with the Company's long-term outlook for annual loan origination growth of 25% to 30%. However, it should be noted the Company retracted in March 2020 its previously disclosed long-term outlook for loan origination growth of 25% to 30% due to the Covid-19 pandemic and its unknown consequences on the economy.

For the year ended December 31, 2019, loans originated through our wholesale channel, where borrowers are sourced via relationships with third-party business loan brokers, increased 24.9% year over year to US$141.1 million. The Company will continue to develop this channel by servicing existing broker relationships and forming new relationships. Loans originated through the retail channel, where borrowers are sourced directly, increased 9.5%, year over year, to US$13.1 million. The Company intends to grow this channel through investments in direct marketing and sales. In addition, as part of its wholesale and retail efforts, the Company is currently investing in providing brokers and merchants with a best-in-class user experience.

As at December 31, 2019, total loans under management amounted to $110.8 million (2018: $95.9 million), representing an increase of 15.5% year over year and is attributable to the growth in loan originations of 23.4% compared to the same period in 2018. The principal balance of the loan portfolio amounted to $56.9 million (2018: $34.5 million), representing an increase of 64.8% and consistent with the Company's strategy to retain more loans on its balance sheet. The principal balance of IOU Financial's servicing portfolio (loans being serviced on behalf of third parties) amounted to $53.9 million (2018: $61.4 million), representing a decrease of 12.3%.

Adjusted gross revenue increased 28.5% to $23.7 million for the year ended December 31, 2019 compared to 2018 ($18.4 million) due to an increase in interest revenue and servicing income.

Interest revenue increased 32.7% to $17.9 million in 2019 compared to the same period in 2018 as a result of the increase in the average commercial loans receivable balance of 44.5% in 2019 compared to 2018. The increase in the interest revenue will lag behind the increase in the average commercial loans receivable balance as loans originated in the latter part of the year do not contribute interest revenue for the full year.

Servicing income increased 25.0% to $4.5 million in 2019 compared to 2018 as a result of the increase in the average servicing portfolio of 27.8% in 2019 compared to 2018. The servicing portfolio yield decreased slightly from 8.2% in 2018 to 8.0% in 2019.

Interest expense during the year ended December 31, 2019 increased 19.2% to $4.0 million (2018: $3.4 million). The increase is attributable to an increase in average borrowings of 30.3% in 2019 compared to 2018 and offset by a 1.0 percentage point decrease in the Cost of Borrowing Rate to 10.4%. In an effort to lower its Cost of Borrowing Rate, the Company closed a new credit facility in the first quarter of 2019 at a rate which is substantially lower than the current Cost of Borrowing Rate. Specifically, the rate on the new credit facility was 6.41% at December 31, 2019 or approximately 4.0 percentage points less than the current Cost of Borrowing Rate. Also, in December 2019, the Company modified and extended its 2016 Credit Facility until December 31, 2022. The modified interest rate of the Credit Facility is LIBOR plus 5.5%, down from LIBOR plus 8.5%. The new rate came into effect in January 2020. However, due to the Covid-19 pandemic, the Company effected modification agreements in March and April 2020 with certain borrowers in excess of allowable limits resulting in the 2016 Credit Facility charging additional default interest of 3% for a total interest rate of LIBOR plus 8.5% effective April 1, 2020.

Provision for loan losses during the year ended December 31, 2019 increased to $8.0 million (2018: $5.0 million). The increase is attributable to an increase in the average commercial loans receivable balance in 2019 of 44.5% compared to last year and an increase in the Provisional Credit Loss Rate to 16.7% in 2019 compared to 15.2% in 2018 due to a slight increase in delinquencies related to loans originated in Q2 and Q3 2019. The Provisional Credit Loss Rate in 2019 of 16.7% was in line with the Company's expected average of approximately 16.5%. However, due to the Covid-19 pandemic and because the unprecedented economic situation due to the pandemic remains unknown, the Company is retracting its previous expectation for the Provisional Credit Loss Rate to average approximately 16.5%.The Provisional Credit Loss Rate is a representation of the expected credit loss within the lifetime of the loan and includes a provision to all current loans (Stage 1 provision). The growth in the principal balance of the loan portfolio contributed approximately 1.0% to 2.0% to the Provisional Credit Loss Rate compared to the Net Credit Loss Rate.

The Net Credit Loss Rate decreased from 13.4% in 2018 to 12.5% in 2019. The Net Credit Loss Rate in 2019 of 12.5% was below the Company's expected average Net credit Loss Rate of approximately 15%. However, due to the Covid-19 pandemic and because the unprecedented economic situation due to the pandemic remains unknown, the Company is retracting its previous expectation for the Net Credit Loss Rate to average approximately 15%. The Company uses the Net Credit Loss Rate as an alternative measure to the Provisional Credit Loss Rate as it excludes the effect of provisions (reductions) in the allowance for expected credit losses during the period which may not coincide with the actual timing of charge-offs and recoveries.

Adjusted operating expenses increased 21.0% or $1.7 million to $10.1 million in 2019 (2018: $8.4 million) due primarily to reinvestments in staff, technology and advertising and promotion expenses. However, the Adjusted Operating Expense Ratio, which is a measure of the Company's operating efficiency, decreased to 9.9% in 2019 (2018: 11.0%) as the Company increased its loans under management at a greater rate than operating expenses. Operating expenses increased to $9.9 million for the year ended December 31, 2019 compared to $8.5 million in the same period in 2018. The reinvestments in staff, technology and advertising and promotion expenses were partly offset by the non-recurring gain relating to the revaluation of convertible debentures of $0.5 million in Q3 2019 following the extension of the convertible debentures from December 31, 2020 to December 31, 2023.

IOU closed on the year ended December 31, 2019 with adjusted net earnings of $1,758,254, or $0.02 per share compared to adjusted net earnings of $2,152,712 or $0.02 per share for the same period last year.

IOU closed on its year ended December 31, 2019 with IFRS net earnings of $1,523,309, or $0.02 per share, compared to IFRS net earnings of $2,710,218 or $0.03 per share for the same period in 2018.

ADJUSTED AND IFRS NET EARNINGS FOR THE PERIOD ENDED DECEMBER 31, 2019

The following table presents IOU Financial's adjusted and IFRS net earnings for the years ended December 31, 2019 and 2018. The financial information is presented in Canadian dollars (except where otherwise noted) and was prepared in accordance with IFRS.

Adjusted and IFRS net earnings

For the year ended December 31	**2019** **$**	2018 $
Interest revenue	**17,861,394**	13,464,475
Servicing & other income	**5,837,860**	4,979,791
Adjusted Gross Revenue	**23,699,254**	18,444,266
Interest expense	**3,998,673**	3,355,496
Provision for loan losses	**7,951,635**	5,004,324
Recoveries	**(248,043)**	(322,000)
Cost of Revenue	**11,702,265**	8,037,820
Adjusted Net Revenue	**11,996,989**	10,406,446
Adjusted operating expense	**10,117,365**	8,369,410
Income tax expense/(recovery)	**121,370**	(115,676)
Adjusted Net Earnings	**1,758,254**	2,152,712
Adjusted Net Earnings per Share	**0.02**	0.02

Adjusted Net Earnings	**1,758,254**	2,152,712
Non-cash gain on sales of loans	**3,273,642**	3,466,884
Non-cash amortization of servicing asset	**(3,706,180)**	(2,743,101)
Non-cash stock-based compensation	**(287,986)**	(166,277)
Non-recurring gain	**485,579**	-
Net Earnings per IFRS	**1,523,309**	2,710,218
Net Earnings per Share	**0.02**	0.03

Adjusted Gross Revenue

IOU Financial's adjusted gross revenue is defined as gross revenue prepared in accordance with IFRS, plus amortization of servicing assets less gain on sale of loans. The Company uses adjusted gross revenue as it eliminates items that do not necessarily reflect how the Company is performing. Specifically, it eliminates the non-cash gain on sale of loans and the non-cash amortization of servicing assets which influence operating results depending on the timing and amount of the loan sales.

The following table summarizes revenues by category.

Adjusted Gross Revenue

For the year ended December 31	**2019** **$**	2018 $
Gross Revenue		
Interest revenue	**17,861,394**	13,464,475
Servicing & other income	**5,837,860**	4,979,791
Non-cash amortization of servicing assets	**(3,706,180)**	(2,743,101)
Non-cash gain on sale of loans	**3,273,642**	3,466,884
Gross Revenue	**23,266,716**	**19,168,049**
Non-cash amortization of servicing assets	**3,706,180**	2,743,101
Non-cash gain on sale of loans	**(3,273,642)**	(3,466,884)
Adjusted Gross Revenue	**23,699,254**	**18,444,266**
Ratios		
Portfolio Yield (1)	**37.5%**	40.8%
Servicing Portfolio Yield (2)	**8.0%**	8.2%

(1) Portfolio Yield is calculated as follows: interest revenue divided by the average commercial loans receivable for the period presented on an annualized basis. The ratios are calculated on a five-point basis, using December, March, June, September and period end balances, presented on an annualized basis.
(2) Servicing Portfolio Yield is calculated as follows: servicing income divided by the average servicing portfolio for the period presented on an annualized basis. The ratios are calculated on a five-point basis, using December, March, June, September and period end balances, presented on an annualized basis.

Adjusted gross revenue increased 28.5% to $23.7 million for the year ended December 31, 2019 compared to 2018 ($18.4 million) due to an increase in interest revenue and servicing income.

Interest revenue increased 32.7% to $17.9 million in 2019 compared to the same period in 2018 as a result of the increase in the average commercial loans receivable balance of 44.5% in 2019 compared to 2018. The increase in the interest revenue will lag behind the increase in the average commercial loans receivable balance as loans originated in the latter part of the year do not contribute interest revenue for the full year.

Servicing income increased 25.0% to $4.5 million in 2019 compared to 2018 as a result of the increase in the average servicing portfolio of 27.8% in 2019 compared to 2018. The servicing portfolio yield decreased slightly from 8.2% in 2018 to 8.0% in 2019.

Gross revenue increased to $23.3 million for the year ended December 31, 2019 (2018: $19.2 million), representing an increase of 21.4% over 2018. The increase is due to an increase in interest revenue as a result of an increase in the average commercial loans receivable balance in 2019 of 44.5% compared to 2018 as well as an increase in servicing income due to an increase in the average servicing portfolio.

As per the debt assignment agreements, The Company retains the servicing rights (payment collections) to the loans it has sold, and the purchaser agrees to be charged a servicing fee over the term of the loans. Under IFRS, the Company recognizes a non-cash gain on sale along with servicing assets that are amortized to the consolidated statements of comprehensive income over the term of the assignment agreements. The Company recognizes a non-cash gain on sale of loans and related servicing asset since the actual expected cash flows to be received are higher than the fair value of providing such services.

Cost of revenue

IOU Financial's cost of revenue consists primarily of interest costs incurred in connection with the financing of its lending activities and provisions for loan losses (net of recoveries). The following table summarizes cost of revenue by category.

Cost of Revenue

For the year ended December 31	**2019** **$**	2018 $
Cost of revenue		
Interest expense	**3,998,673**	3,355,496
Provision for loan losses	**7,951,635**	5,004,324
Recoveries	**(248,043)**	(322,000)
Cost of Revenue	**11,702,265**	**8,037,820**
Ratios		
Cost of Borrowing Rate [(1)]	**10.4%**	11.4%
Provisional Credit Loss (PCL) Rate [(2)]	**16.7%**	15.2%
Net Credit Loss (NCL) Rate [(3)]	**12.5%**	13.4%

[(1)] The Cost of Borrowing Rate is calculated as follows: interest expense divided by the average borrowings for the year, presented on an annualized basis. The ratios are calculated on a five-point basis, using December, March, June, September and period end balances, presented on an annualized basis.
[(2)] The Provisional Credit Loss rate is calculated as follows: provision for loan losses divided by the average commercial loans receivable for the year, presented on an annualized basis. The ratios are calculated on a five-point basis, using December, March, June, September and period end balances, presented on an annualized basis.
[(3)] The Net Credit Loss rate is calculated as follows: charge offs net of recoveries divided by the average commercial loans receivable for the year, presented on an annualized basis. The ratios are calculated on a five-point basis, using December, March, June, September and period end balances, presented on an annualized basis.

The cost of revenue for the year ended December 31, 2019 increased from $8.0 million in 2018 to $11.7 million in 2019. The increase is primarily a result of the increase in the provision for loan losses due to the increase in the average commercial loans receivable balance in 2019 of 44.5% compared to last year.

Interest expense during the year ended December 31, 2019 increased 19.2% to $4.0 million (2018: $3.4 million). The increase is attributable to an increase in average borrowings of 30.3% in 2019 compared to 2018 and offset by a 1.0 percentage point decrease in the Cost of Borrowing Rate to 10.4%. In an effort to lower its Cost of Borrowing Rate, the Company closed a new credit facility in the first quarter of 2019 at a rate which is substantially lower than the current Cost of Borrowing Rate. Specifically, the rate on the new credit facility was 6.41% at December 31, 2019 or approximately 4.0 percentage points less than the current Cost of Borrowing Rate. Also, in December 2019, the Company modified and extended its 2016 Credit Facility until December 31, 2022. The modified interest rate of the Credit Facility is LIBOR plus 5.5%, down from LIBOR plus 8.5%. The new rate came into effect in January 2020. However, due to the Covid-19 pandemic, the Company effected modification agreements in March and April 2020 with certain borrowers in excess of allowable limits resulting in the 2016 Credit Facility charging additional default interest of 3% for a total interest rate of LIBOR plus 8.5% effective April 1, 2020.

Provision for loan losses during the year ended December 31, 2019 increased to $8.0 million (2018: $5.0 million). The increase is attributable to an increase in the average commercial loans receivable balance in 2019 of 44.5% compared to last year and an increase in the Provisional Credit Loss Rate to 16.7% in 2019 compared to 15.2% in 2018 due to a slight increase in delinquencies related to loans originated in Q2 and Q3 2019. The Provisional Credit Loss Rate in 2019 of 16.7% was in line with the Company's expected average of approximately 16.5%. However, due to the Covid-19 pandemic and because the unprecedented economic situation due to the pandemic remains unknown, the Company is retracting its previous expectation for the Provisional Credit Loss Rate to average approximately 16.5%.The Provisional Credit Loss Rate is a representation of the expected credit loss within the lifetime of the loan and includes a provision to all current loans (Stage 1 provision). The growth in the principal balance of the loan portfolio contributed approximately 1.0% to 2.0% to the Provisional Credit Loss Rate compared to the Net Credit Loss Rate.

The Net Credit Loss Rate decreased from 13.4% in 2018 to 12.5% in 2019. The Net Credit Loss Rate in 2019 of 12.5% was below the Company's expected average Net credit Loss Rate of approximately 15%. However, due to the Covid-19 pandemic and because the unprecedented economic situation due to the pandemic remains unknown, the Company is retracting its previous expectation for the Net Credit Loss Rate to average approximately 15%. The Company uses the Net Credit Loss Rate as an alternative measure to the Provisional Credit Loss Rate as it excludes the effect of provisions (reductions) in the allowance for expected credit losses during the period which may not coincide with the actual timing of charge-offs and recoveries.

Adjusted Operating Expenses

IOU Financial's adjusted operating expenses is defined as total operating expenses prepared in accordance with IFRS for the period, less: non-cash stock-based compensation, which is given at different times and prices, non-recurring costs, plus non-recurring gains which affects operating results only periodically. The Company uses adjusted operating expenses as it eliminates items that do not necessarily reflect how the Company is performing. Operating expenses consist of day to day operating expenses such as wages and salaries, professional fees, including consulting services, legal, audit and accounting fees, data services and IT costs.

Adjusted Operating Expenses

For the year ended December 31	2019 $	2018 $
Operating Expenses	**9,919,772**	8,535,687
Stock Based Compensation	**(287,986)**	(166,277)
Non-Recurring Gain	**485,579**	-
Adjusted Operating Expenses	**10,117,365**	8,369,410
Ratio		
Adjusted Operating Expense Ratio (1)	**9.9%**	11.0%

(1) The Adjusted Operating Expense Ratio is calculated as follows: adjusted operating expenses divided by the average loans under management for the year, presented on an annualized basis. The nine-month ratios are calculated on a four-point basis, using December, March, June and September period end balances, presented on an annualized basis.

The Adjusted Operating Expense Ratio, which is a measure of the Company's operating efficiency, decreased to 9.9% in 2019 (2018: 11.0%) as the Company increased its loans under management at a greater rate than operating expenses. Operating expenses increased to $9.9 million for the year ended December 31, 2019 compared to $8.5 million in the same period in 2018. The reinvestments in staff, technology and advertising and promotion expenses were partly offset by the non-recurring gain relating to the revaluation of convertible debentures of $0.5 million in Q3 2019 following the extension of the convertible debentures from December 31, 2020 to December 31, 2023.

Adjusted operating expenses increased by $1.8 million to $10.1 million in 2019 compared to $8.4 million in 2018. This increase can be primarily attributed to the following:

- an increase of $0.9 million in wages and salaries as a result of an increase in the number of full-time employees;
- an increase of $0.6 million in data services and IT costs;
- an increase of $0.2 million in advertising and promotion.

Operating expenses increased by $1.4 million to $9.9 million in 2019 compared to $8.5 million in 2018. The reinvestments in staff, technology and advertising and promotion expenses were partly offset by the non-recurring gain relating to the revaluation of convertible debentures of $0.5 million in Q3 2019 following the extension of the convertible debentures from December 31, 2020 to December 31, 2023.

Adjusted Net Earnings

IOU Financial's adjusted earnings is defined as net earnings for the period prepared in accordance with IFRS less: gain on sale of loans and non-recurring gains, plus: amortization of servicing assets, stock-based compensation and non-recurring costs. The Company uses adjusted net earnings as a measure of financial performance.

Adjusted Net Earnings

For the period ended December 31	**2019**	2018
	$	$
Net Earnings	**1,523,309**	2,710,218
Gain on Sale of Loans	**(3,273,642)**	(3,466,884)
Amortization of Servicing Assets	**3,706,180**	2,743,101
Stock-Based Compensation	**287,986**	166,277
Non-Recurring Gain	**(485,579)**	-
Adjusted net earnings (1)	**1,758,254**	2,152,712

(1) Beginning in the first quarter of 2019, the calculation of adjusted net earnings was revised and is defined as net earnings for the period prepared in accordance with IFRS less: gain on sale of loans and non-recurring gains, plus: amortization of servicing assets, stock-based compensation and non-recurring costs. Prior to the first quarter of 2019, the calculation of adjusted net earnings was defined as net earnings for the period prepared in accordance with IFRS less: gain on sale of loans and income tax recovery, plus: amortization of servicing assets, stock-based compensation, amortization of transaction costs-financing credit facilities, depreciation and amortization, income tax expense and non-recurring costs. As a result, the prior comparative periods have been calculated to reflect the revised definition.

IOU closed on the year ended December 31, 2019 with adjusted net earnings of $1,758,254, or $0.02 per share compared to adjusted net earnings of $2,152,712 or $0.02 per share for the same period last year.

IOU closed on its year ended December 31, 2019 with IFRS net earnings of $1,523,309, or $0.02 per share, compared to IFRS net earnings of $2,710,218 or $0.03 per share for the same period in 2018.

CONSOLIDATED FINANCIAL POSITION

The following table presents IOU Financial's consolidated statement of financial position as at December 31, 2019 and December 31, 2018. The financial information is presented in Canadian dollars (except where noted) and was prepared in accordance with IFRS.

Condensed Consolidated Statement of Financial Position

	As at December 31, 2019	As at December 31, 2018
	$	$
Assets		
Commercial loans receivable	**58,964,204**	35,656,294
Allowance for expected credit losses	**(4,515,175)**	(3,324,114)
Commercial loans receivable – net	**54,449,029**	32,332,180
Non-portfolio assets	**9,383,781**	11,398,918
Total assets	**63,832,810**	43,731,098
Liabilities		
Financing credit facilities	**37,954,729**	19,758,556
Convertible debentures – liability component	**9,931,181**	10,407,017
Other liabilities	**2,796,522**	1,709,751
Total liabilities	**50,682,432**	31,875,324
Shareholders' equity	**13,150,378**	11,855,774
Ratios		
Allowance for Expected Credit Losses (ACL) Ratio (1)	7.7%	9.3%
Stage 3 Delinquency Ratio (2)	10.7%	6.6%

(1) The Allowance for Expected Credit Losses Ratio is calculated as follows: allowance for expected credit losses divided by the commercial loans receivable at year end.
(2) The Stage 3 Delinquency Ratio is calculated as follows: amount of commercial loans receivable included in stage 3 divided by the commercial loans receivable at year end.

Total Assets

Total assets increased by $20.1 million (46.0%) from $43.7 million at December 31, 2018 to $63.8 million at December 31, 2019. This increase is mainly attributable to an increase of $22.1 million in commercial loans receivable-net and the recognition of the new right-of-use asset of 0.7 million, offset by a decrease in cash and restricted cash of $2.0 million.

As at December 31, 2019, the allowance for Expected Credit Losses Ratio decreased from 9.3% to 7.7% compared to December 31, 2018. The Stage 3 Delinquency Ratio increased from 6.6% to 10.7% compared to December 31, 2018.

Total Liabilities

IOU Financial's total liabilities increased by $18.8 million (59.0%) from $31.9 million at December 31, 2018 to $50.7 million at December 31, 2019. The increase is mainly due to the increase in financing credit facilities of $18.2 million and an increase of $1.1 million in other liabilities due to the recognition of lease liabilities of $0.8 million and an increase in accounts payable and accrued liabilities of $0.3 million, offset by a decrease in convertible debentures – liability component of $0.5 million primarily due to the extension of convertible debentures from December 31, 2020 to December 31,2023.

Shareholders' Equity

Shareholders' Equity increased by $1.3 million (10.9%) from $11.9 million at December 31, 2018 to $13.2 million at December 31, 2019. This increase is attributable to current period comprehensive income, the exercise of warrants and stock-based compensation.

LIQUIDITY AND CAPITAL RESOURCES

IOU Financial's primary sources of liquidity and capital resources are cash-on-hand, cash provided by operations and cash provided by financing through the issuance of equity and/or debt securities as well as the sale of loans.

On March 5, 2019, the Company entered into a US$50 million credit facility ("2019 Credit Facility"). The facility has an initial commitment amount of US$50 million and is expandable to US$100 million at the Company's request and the lender's acceptance. The interest rate on the facility is 90-day LIBOR plus 4.50%, which represents 6.64% as at December 31, 2019. The term of the facility is three years with a revolving period ending on March 5, 2021 and an amortization period beginning after the revolving period and ending on March 5, 2022. The amount outstanding as at December 31, 2019 is US$14.0 million. In December 2019, IOU modified and extended its US $22 million secured credit facility ("2016 Credit Facility") until December 31, 2022. The modified interest rate of the Credit Facility is LIBOR plus 5.5%, down from LIBOR plus 8.5%. The new rate came into effect in 2020. However, due to the Covid-19 pandemic, the Company effected modification agreements in March and April 2020 with certain borrowers in excess of allowable limits resulting in the 2016 Credit Facility charging additional default interest of 3% for a total interest rate of LIBOR plus 8.5% effective April 1, 2020.

Flow of funds

The following table presents a summary of cash flows for the years ended December 31, 2019 and 2018.

Consolidated Statement of Cash Flows

For the year ended December 31	**2019** **$**	2018 $
Cash (used) generated in operating activities	**(21,222,645)**	4,221,761
Cash used in investing activities	**548,757**	(150,963)
Cash generated (used) in financing activities	**19,487,561**	(1,746,471)
(Decrease) increase in cash	**(1,186,327)**	2,324,327
Exchange rate (loss) gain on cash	**(242,311)**	460,848
Net (decrease) increase in cash	**(1,428,638)**	2,785,175

Cash used in operating activities

The $25.4 million increase in cash used in operating activities for the year ended December 31, 2019, compared to the same period in 2018, was primarily related to an increase of $22.4 million in the cash outflow from the net change in non-cash working capital items (2019: $115.0 million compared to 2018: $92.6 million) and a decrease of $2.4 million in the cash inflow from the sale of commercial loans (2019: $93.3 million compared to 2018: $95.7 million).

Cash used in investing activities

The $0.7 million increase in cash used by investing activities for the year ended December 31, 2019, compared to the same period in 2018, is primarily due to a decrease of $0.6 million in restricted cash.

Cash generated from financing activities

The $21.2 million increase in cash generated in financing activities for year ended December 31, 2019, compared to the same period in 2018, is primarily due to the proceeds of $19.9 million from the financing credit facilities in 2019 and repayment of $1.3 million to the financing credit facilities in 2018.

SUMMARY OF QUARTERLY RESULTS

Quarterly Results

For the quarters ended	Dec 31/19 $	Sept 30/19 $	Jun 30/19 $	Mar 31/19 $
Gross revenue	**6,339,300**	6,595,598	5,486,327	4,845,491
Net revenue	**3,079,405**	3,208,098	2,737,863	2,539,085
Net earnings	**217,569**	1,000,614	219,256	85,870
Net earnings per share [(1)]	**0.00**	0.01	0.00	0.00
For the quarters ended	Dec 31/18 $	Sept 30/18 $	Jun 30/18 $	Mar 31/18 $
Gross revenue	5,220,144	4,871,322	4,638,606	4,437,977
Net revenue	2,740,101	2,819,265	2,899,750	2,671,113
Net earnings	459,638	600,593	852,789	797,198
Net earnings (loss) per share [(1)]	0.01	0.01	0.01	0.01

[(1)] Basic and diluted. Net earnings (loss) per share has been calculated using the weighted average number of shares outstanding during each period. Rounded to the nearest cent.

OFF-BALANCE SHEET ARRANGEMENTS

IOU Financial does not engage in any off-balance sheet financing activities. IOU Financial does not have any interest in non-consolidated entities referred to as variable interest entities, which include special purpose entities and other structured finance entities.

PROPOSED TRANSACTIONS

There were no proposed transactions as at the date of the Company's financial statements.

TRANSACTIONS BETWEEN RELATED PARTIES

i) The CEO and director of IOUF Canada is a shareholder in a company that owns a significant stake in Palos Capital Corporation ("Palos"), the parent company of Palos Management Inc. No servicing fees have been earned by the Company on outstanding servicing portfolio balances of loans that had previously been sold to Palos (2018: $12,453). Palos also received no agency fees during the year (2018: $973) relating to the outstanding servicing portfolio balance related to a third- party purchaser.

ii) The Company rents its Canadian office space from Palos. The lease may be cancelled after October 2021 upon the payment of a termination fee. The terms of this operating lease are similar to those that would have been present for an arm's-length transaction. The amount of $122,018 is expensed as rental expense for the period (2018: rent expense of $200,925). That amount does not include the amortization of right-of-use assets and the interest on the lease liabilities. Future non-cancellable lease liabilities under this agreement amount to $853,193.

iii) Key Management Compensation

Key management includes directors (executive and non-executive), the Chief Operating Officer and the Chief Financial Officer who is also the Company Secretary. The compensation paid or payable to key management for employee services for periods ended December 31, 2019 and 2018 is shown below:

Key Management Compensation

For the year ended December 31	**2019**	2018
Salaries and other short-term employee benefits	**885,529**	771,082
Share-based payments	**169,496**	107,400
	1,055,025	878,482

COMMERCIAL LOANS RECEIVABLE

IOU Financial's commercial loan receivable portfolio is composed of a large number of loans, and as such, no individual loan comprises a significant portion of the portfolio. As at December 31, 2019, the average loan balance in the portfolio was approximately US$91,223 (2018: US$81,863). In addition to limiting its exposure to any single loan, IOU Financial maintains a geographically and industry diversified loan portfolio which reduces the risk of loss arising from adverse regional or industrial economic conditions.

The following tables present the portfolio by geography and industry as at December 31, 2019.

Industry Category	**Portfolio %**
Specialty trade contractors and home building renovation	17%
Casual, fine dining and full- service restaurants	11%
Other store or online retailers and wholesalers	6%
Manufacturing	5%
Automotive garage	4%
Medical services	2%
Other professional services	2%
Retail stores	3%
Gas stations	2%
Dentists	1%
Landscaping Services	2%
Other	45%
Total	100%

State	**Portfolio %**
Texas	14%
California	11%
Florida	10%
New York	6%
Georgia	5%
New Jersey	4%
North Carolina	4%
Illinois	4%
Colorado	3%
Ohio	2%
Maryland	2%
Arizona	2%
Washington	2%
Other	31%
Total	100%

OUTSTANDING SHARE DATA

The following table presents IOU Financial's outstanding share data as at April 29, 2020

Outstanding Share data

Ordinary shares issued and outstanding:	**Number of shares issued**
December 31, 2018	87,825,309
Shares issued between January 1, 2019 and December 31, 2019	548,313
Shares cancelled between January 1, 2019 and December 31,2019	(1,665,500)
Shares cancelled after December 31, 2019	(279,000)
Shares outstanding on April 29, 2020	**86,429,122**
Warrants issued and Outstanding:	**Number of warrants issued**
December 31, 2018	479,125
Warrants exercised during the period	(348,313)
Warrants expired during the period	(130,812)
Warrants outstanding on April 29, 2020	**-**
Options issued and outstanding:	**Number of Options issued**
December 31, 2018	6,201,000
Options granted between January 1, 2019 and December 31, 2019	2,385,000
Options forfeited between January 1, 2019 and December 31, 2019	(1,724,500)
Options granted after December 31, 2019	200,000
Options forfeited after December 31, 2019	-
Options outstanding on April 29, 2020	**7,061,500**

NORMAL COURSE ISSUER BID

IOU Financial has commenced a Normal Course Issuer Bid ("NCIB") pursuant to which IOU Financial may purchase for cancellation, from time to time, as it considers advisable, up to 2,000,000 of its common shares ("Shares") over a 12-month period. The NCIB commenced on May 1st, 2019 and will terminate on April 30, 2020, or on such earlier date on which purchases under the NCIB have been completed or at the option of IOU Financial. Purchases of Shares under the NCIB will be made through the facilities of the TSX Venture Exchange at the market price of the Shares at the time of acquisition. Leede Jones Gable Inc. conducts the NCIB on behalf of IOU and Shares will be purchased at the discretion of senior management of IOU. As of April 29, 2020, 1,944,500 Shares were repurchased and cancelled.

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CONVERTIBLE DEBENTURES

On August 2, 2019, IOU amended its convertible debentures according to the terms below.

- extended the maturity date of the convertible debentures from December 31, 2020 to December 31, 2023;
- eliminated the condition that the convertible debentures be redeemable by IOU only when the current market price is 125% of the conversion price;
- modified the conversion price of the convertible debentures from \$0.75 per share to \$0.50;
- eliminated IOU's right to carry out a forced conversion of the convertible debentures; and
- eliminated IOU's right to redeem or repay the principal amount of the convertible debentures with freely tradeable shares.

The conversion period for the convertible debentures remains unchanged and is set to expire at 5:00 p.m. on the last business day prior to December 31, 2020.

IOU issued the Debentures by way of a private placement pursuant to a trust indenture dated November 2, 2015 and entered into a supplemental trust indenture with Computershare Trust Company of Canada, the debenture trustee.

Following the amendment, the liability component of the convertible debentures was determined to be $10,012,175, resulting in a gain of $485,579.

On October 21st, 2019, $100,000 of convertible debentures was converted to 200,000 common shares at $0.50 per share.

BUSINESS OUTLOOK

The Company's principal balance of its loan and servicing portfolios is diversified both across industry type and location within North America, mostly in the United States. Due to the Covid-19 pandemic, IOU has modified its underwriting standards to cease lending to industries and geographical areas which are strongly impacted by Covid-19. The company continues to originate loans and support businesses deemed essential by various governments.

The duration of the current situation with the pandemic is unknown and considering the uncertainty faced by the North American economy over the coming months, the Company retracted in March 2020 its previously disclosed long-term outlook for loan origination growth of 25% to 30%. However, the Company also sees potential for a greater than expected need for small business loans as significant working capital will be required once the situation normalizes. Furthermore, the Company is working closely with various government agencies to assist some of its merchants who may encounter hardships as a result of the Covid-19 pandemic.

Due to the uncertainty surrounding the current situation, the Company furloughed approximately 40% of its full-time employees and implemented a temporary 20% reduction in salary for all remaining employees commencing on April 1, 2020. IOU also announced, in April 2020, that more than two-thirds of the value of the Company's convertible debenture holders have agreed to defer the payment of interest from the April 30, 2020 payment period to the June 30, 2020 payment period ("reprieve period") and capitalizing the accrued interest over the reprieve period to the principal amount of the debentures at the end of the reprieve period, in accordance to the terms of the trust indenture under which such debentures were issued.

While the current unprecedented economic situation due to the pandemic remains uncertain, the Company is prepared to react quickly as the situation may require and looks forward to emerging as a stronger business coming out of this downturn.

CRITICAL ACCOUNTING ESTIMATES

The Company makes estimates and assumptions concerning the future. The resulting accounting estimates will, by definition, seldom equal the related actual results. The estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are addressed below.

1. Valuation of commercial loans
   Management exercises judgment to determine the expected credit losses (ECL) based on all available reasonable and supportable information about past events, current conditions and forecasts of future events and economic conditions. At the end of each reporting period, the Company applies a three-stage forward looking impairment approach to measure the expected credit losses (ECL) on its Originated to hold (OTH) loans. The stages are based on the change in the credit quality of the OTH loan since initial recognition. Measurement of ECLs at each reporting period reflects reasonable and supportable information about past events, current conditions, and forecasts of future events and economic conditions. Further details on the estimates used to determine any allowance for impaired commercial loans are provided in the accounting policy of the consolidated Financial Statement “Impairment of OTH loans”.

2. Servicing assets
   The initial recognition of servicing assets requires the Company to make estimates of the fair value of the service to be provided which is based on market expectations at the time of the loan sale and may vary from the actual cash flows serviced.

3. Deferred Tax Estimation
   Deferred tax assets and liabilities recognition involves making a series of assumptions. For instance, the Company must estimate the timing of the reversal of temporary differences or if it is probable that temporary differences will not reverse in the foreseeable future or the tax rates expected to apply to the period when the asset is realized or the liability is settled.

   With respect to deferred tax assets, their realization ultimately depends on taxable profits being available in the future. Deferred tax assets should be recognized when it is probable that taxable profits will be available against which the deferred tax asset can be utilized, and it is probable that the entity will earn sufficient taxable profit in future periods to benefit from a reduction in tax payments. This involves the Company making assumptions within its overall tax-planning activities and periodically reassessing them in order to reflect changed circumstances as well as tax regulations. Moreover, the measurement of a deferred tax asset or liability reflects the manner in which the entity expects to recover the asset’s carrying value or settle the liability.

CURRENT CHANGES IN ACCOUNTING POLICIES

The Company has adopted the following new and revised standards, along with any consequential amendments, effective January 1, 2019.

IFRS 16, Leases

On January 1, 2019, the Company adopted IFRS 16, *Leases*, which supersedes IAS 17, *Leases*, and the related interpretations on leases: IFRIC 4, *Determining Whether an Arrangement Contains a Lease*; SIC 15, *Operating Leases – Incentives* and SIC 27, *Evaluating the Substance of Transactions Involving the Legal Form of a Lease*. The Company has adopted the new standard for its annual periods beginning on January 1, 2019, on a modified retrospective basis whereby comparative information has not been adjusted. That new standard affects mostly the Company's operating lease commitments presented in Note 8 to the annual consolidated financial statements. Following the adoption of the new standard, the operating lease commitments are recognized in the Company's consolidated statements of financial position with an increase in assets due to the recognition of the right to use the leased assets (right-of-use assets) and an increase in liabilities due to recognition of the obligation to make lease payments (lease liabilities). Furthermore, given that the previous linear operating lease expense, which approximates the amount of the contractual lease payments, has been replaced by an amortization of the right-of-use asset separately from an interest expense on the lease liability, the nature of the operating expenses of the Company differs.

For more information related to the initial impact of IFRS 16, see note 4 of the December 31, 2018 consolidated financial statements (Significant Accounting Policies). Additional information can be found in the notes to the consolidated financial statements for the year ended December 31, 2019.

IFRIC 23, Uncertainty over Income Tax Treatments

On January 1, 2019, the Company adopted IFRIC 23 which provides guidance on when the recognition of a current tax asset is appropriate if tax laws require an entity to make an immediate payment in respect of a disputed amount. The Company has evaluated that there is no impact on Consolidated Financial Statements.

FINANCIAL INSTRUMENTS AND OTHER INSTRUMENTS

The carrying values of cash, accounts receivable, loans receivable, financing credit facilities and accounts payable approximate their fair values due to the relatively short period to maturity of these items.

The majority of commercial loan receivables are due from customers in the United States. The maximum credit risk associated with the company's financial assets is the carrying value of those assets.

Foreign exchange risk

The Company operates internationally and is exposed to foreign exchange risk arising from currency exposure with respect to the US dollar. Foreign exchange risk arises from future commercial transactions, recognized assets and liabilities.

The Company does not use derivative financial instruments to reduce its foreign exchange exposure. Fluctuations in foreign exchange rates could cause unanticipated fluctuations in the Company's operating results.

Listed below are the relevant instruments and the amount of foreign currencies included in their balances (in US dollars) As at December 31, 2019:

Cash	3 652 021
Restricted cash	287 811
Certain other assets	1 632 749
Net commercial loan receivables	40 620 064
Accounts payable and accrued liabilities	(1 135 831)
Financing credit facilities	(29 406 732)

The exchange rate applied as at December 31, 2019 was 1.2988 (December 31, 2018: 1.3642).

Based on the Company's foreign currency exposure noted above, varying the above foreign exchange rates to reflect a ten (10) percent strengthening of the Canadian dollar would have increased the net earnings by approximately $473,765 (2018: $618,016), assuming that all other variables remained constant. An assumed ten (10) percent weakening of the Canadian dollar would have had an equal but opposite effect on the above currencies to the amounts shown above, on the basis that all other variables remain constant.

Liquidity risk

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they become due. The Company's approach in managing liquidity is to ensure, as much as possible, that it will have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Company's reputation.

The Company manages liquidity risk through the management of its capital structure.

Credit risk

Credit risk is managed on a Company basis and results from the possibility that a loss may occur from the failure of another party to perform according to the terms of the contract. The Company regularly monitors the credit risk exposure and takes steps to mitigate the likelihood of these exposures from resulting in actual loss.

The Company, in the normal course of business, monitors the financial condition of its customers and reviews the credit risk history of each customer. These policies cover the approval of credit applications, attribution of risk ratings, management of impaired loans, establishment of provisions and risk-based pricing. The Company does not believe it is exposed to an unusual level of customer credit risk. The Company’s maximum credit risk is the carrying value of the cash, restricted cash and commercial loans receivable. The allowance for loan losses is maintained at a level considered sufficient to cover all potential losses.

In addition, financial instruments that potentially subject the Company to significant concentrations of credit risk consist of deposits in the form of cash and restricted cash. The Company invests with major North American financial institutions. The Company has investment policies that are designed to provide for the safety and preservation of principal, the Company's liquidity needs and appropriate yields. The Company has no exposure to any asset-backed securities.

Interest rate risk

The Company is subject to interest rate risk on its cash and restricted cash and secured loan facility. Sensitivity to a 10% increase in interest rates over a 12 months horizon based on the balances as at December 31, 2019 decrease net earnings by approximatively $285,601 (2018: $217,909).

None of the Company’s current commercial lending is based on variable interest rates. The Company is also exposed to changes in the value of a loan when that loan’s interest rate is at a rate other than current market rate. The Company mitigates this risk by lending for short terms, with terms at the inception of the loan generally varying from six to eighteen months.

The Company is exposed to cash flow interest rate risk on its financing credit facilities issued at a variable rate. During 2018 and 2019, the borrowings at a variable rate were denominated in USD. The Company mitigates this risk by borrowing in the short term and therefore the Company does not believe that its exposure to interest rate risk is significant.

Interest revenue presented in the consolidated statement of comprehensive loss represents interest revenue on financial assets that are classified as loans and receivables.

RISKS AND UNCERTAINTIES

In addition to the risks mentioned above, IOU Financial is subject to a number of risks and uncertainties in carrying out its activities.

IOU Financial is Subject to the Risks Inherent in Growing a New Business.

IOU Financial's operations are subject to the general risks inherent in growing a new business, including, among others, hiring and retaining experienced and qualified employees. If IOU Financial cannot hire or retain qualified employees, or cannot effectively implement its business planned strategy, it will be hampered in its ability to grow its current market and to develop new markets, which would in turn have an adverse effect on its financial performance. Even if IOU Financial successfully implements its planned strategy, it may not achieve the favorable impact on its operations that it anticipates.

Compliance with debt covenants

IOU Financial entered into loan agreements with lenders in 2016 and in 2019. The loan agreements impose covenants and obligations on the part of the Company. In particular, the agreements contain certain covenants and representations, the breach of which could result in a default and the acceleration of the maturity of the term of the financing credit facilities. IOU Financial plans to address the risk of default by endeavoring to meet the financial covenants and other obligations in the loan agreement. There is no assurance, however, that IOU Financial will be in compliance with covenants in the future due to unforeseen events or circumstances and if IOU Financial was to default there is no assurance that an amendment or waiver will be granted by the lender. Please refer to note 2 of the Consolidated Financial Statements for the Years Ended December 31, 2019 and 2018.

Dependence on Third Party Service Providers

IOU Financial's service to its clients depends, in part, on its ability to attract and retain the services that are provided to it, by third party service providers. If some or all of IOU Financial's current third-party service providers were to interrupt or cancel their current services to IOU Financial, the company might be forced to curtail or cease its operations.

Competition

IOU Financial operates in an increasingly competitive environment. Both large and small competitors compete with IOU Financial. Some of these competitors may have longer operating histories, greater name recognition and greater financial and marketing resources than IOU Financial. IOU Financial believes that its ability to compete effectively is dependent upon the quality of its product and client service. There can be no assurance that IOU Financial will be able to compete effectively and retain its existing clients or attract and retain new clients. IOU Financial's current and potential competitors may develop and market new products or services that render IOU Financial's existing and future products and services less marketable or competitive.

Regulatory Risk

IOU Financial is subject to strict regulatory and licensing compliance standards, non-conformity with which may expose IOU Financial to adverse consequences. IOU Financial's business is dependent to a large extent on its ability to remain in good standing with all regulators. Some of these regulators impose minimum working capital or net equity requirements, amongst other, which in certain cases and under certain circumstances, IOU Financial may not be able to satisfy. Under such cases, the Company may not be able to operate its regular business until all such financial or regulatory requirements have been satisfied.

Dependence on Key Personnel

IOU Financial's future depends, in part, on its ability to attract and retain key personnel. IOU Financial's future also depends on the continued contributions of its executive officers and other key technical personnel, each of whom would be difficult to replace. The loss of the services of executive officers or key personnel, and the process to replace any of its key personnel could involve significant time and expense and may significantly delay or prevent the achievement of its business objectives.

IOU Financial's growth could strain its personnel, resources and infrastructure

IOU Financial's growth in headcount and operations may place a significant strain on its management and its administrative, operational and financial reporting infrastructure. Accordingly, IOU Financial's success will depend, in part, on the ability of its senior management to manage the growth it achieves effectively. To do so, it must continue to hire, train and manage new employees as needed. The addition of new employees and the system development that it anticipates will be necessary to manage its growth will increase its cost base, which will make it more difficult for it to offset any future revenue shortfalls by reducing expenses in the short term. If IOU Financial fails to successfully manage its growth, it will be unable to execute its business plan. If its new hires perform poorly, or if it is unsuccessful in hiring, training, managing and integrating these new employees, or if it is not successful in retaining its existing employees, IOU Financial's business may be harmed. To manage the growth of IOU Financial's operations and personnel, it will need to continue to improve its operational and financial controls and update its reporting procedures and systems. Given the complex nature of the accounting of the Company's operations and the limited number of staff resources, IOU Financial may not be able to address all accounting and reporting impacts of new transactions or agreements on a timely basis.

Security and Confidentiality Risk

IOU Financial stores users' bank information and other personally-identifiable sensitive data. Any accidental or willful security breaches or other unauthorized access could cause users' secure information to be stolen and used for criminal purposes. Security breaches or unauthorized access to secure information could also expose IOU Financial to liability related to the loss of the information, time-consuming and expensive litigation, and negative publicity. If security measures are breached because of third-party action, employee error, malfeasance or otherwise, or if design flaws in its software is exposed and exploited, and, as a result, a third party or disaffected employee obtains unauthorized access to any of its users' data, IOU Financial's relationships with its users will be severely damaged and it could incur significant liability. Because techniques used to obtain unauthorized access or to sabotage systems change frequently and generally are not recognized until they are launched against a target, IOU Financial and its third-party hosting facilities may be unable to anticipate these techniques or to implement adequate preventative measures. In addition, many states have enacted laws requiring companies to notify individuals of data security breaches involving their personal data. These mandatory disclosures regarding a security breach are costly to implement and often lead to widespread negative publicity, which may cause IOU Financial's users to lose confidence in the effectiveness of its data security measures. Any security breach, whether actual or perceived, could harm IOU Financial's reputation and could result in the loss of users and future business.

If IOU Financial is unable to increase transaction volumes, its business and results of operations will be affected adversely.

To succeed, IOU Financial must increase transaction volumes on its lending platform by raising additional capital and attracting a large number of qualified borrowers in a cost-effective manner. The general tightening and other developments in the broader credit markets may impact IOU Financial's ability to attract capital to lend which, in turn, could limit its ability to increase transaction volumes. If IOU Financial is not able to attract qualified borrowers, IOU Financial will not be able to increase its transaction volumes. In addition, IOU Financial will rely on a variety of methods to drive traffic to its website and lending platform. If IOU Financial is unable to use any of its planned marketing initiatives or the cost of these initiatives was to significantly increase, IOU Financial may not be able to attract new qualified borrowers in a cost-effective manner. As a result, its revenue and results of operations could be affected adversely and could impair its ability to maintain its lending platform.

As an online company constantly involved in the development of its online lending platform, IOU Financial faces increased risks, uncertainties, expenses and difficulties.

If IOU Financial is successful, the volume of loans originated through its lending platform may increase beyond its current capacity, which will require IOU Financial to increase its facilities, personnel and infrastructure in order to accommodate the greater servicing requirements and demands of its lending platform. IOU Financial's lending platform is dependent upon its website.

IOU Financial will likely be required to constantly add new hardware and update its software and website, expand its customer support services and add new employees to maintain the operation of its lending platform, as well as satisfy its servicing requirements. If IOU Financial is unable to increase the capacity of its lending platform and maintain the necessary infrastructure, it might then suffer from a negatively impact on its revenue stream.

Any significant disruption in service on IOU Financial's website or in its computer systems could reduce the attractiveness of its lending platform and result in a loss of users.

If a catastrophic event resulted in a lending platform outage and physical data loss, IOU Financial's ability to service its loans would be materially and adversely affected. The satisfactory performance, reliability and availability of its technology and its underlying network infrastructure are critical to its operations, level of customer service, reputation and ability to attract and retain users. IOU Financial's system hardware is hosted in multiple hosting facilities. All of the data is stored in multiple geographic locations to ensure data availability in the event a particular data center fails. IOU Financial's service provider does not guarantee that access to IOU Financial's website will be uninterrupted, error-free or secure. IOU Financial's operations depend on its supplier's ability to protect their and its systems in their facilities against damage or interruption from natural disasters, power or telecommunications failures, air quality, temperature, humidity and other environmental concerns, computer viruses or other attempts to harm its systems, criminal acts and similar events. If its arrangement with this supplier is terminated, or there is a lapse of service or damage to the supplier's facilities, IOU Financial could experience interruptions in its service, as well as delays and additional expense in arranging new facilities. Any interruptions or delays in its service, whether as a result of its supplier or other third-party error, its own error, natural disasters or security breaches, whether accidental or willful, could harm its relationships with its users and its reputation. In addition, in the event of damage or interruption, IOU Financial's insurance policies may not adequately compensate it for any losses that it may incur. IOU Financial's disaster recovery plan has not been tested under actual disaster conditions, and it may not have sufficient capacity to recover all data and services in the event of an outage at a supplier facility. These factors could prevent it from processing or posting payments on the loans, damage its brand and reputation, divert its employees' attention, reduce its revenue, subject it to liability and cause users to abandon its lending platform, any of which could adversely affect its business, financial condition and results of operations.

IOU Financial's ability to service loans or maintain accurate accounts may be adversely affected by computer viruses, physical or electronic break-ins and similar disruptions.

The highly-automated nature of IOU Financial's lending platform may make it an attractive target and potentially vulnerable to computer viruses, physical or electronic break-ins and similar disruptions. If a computer "hacker" were able to infiltrate IOU Financial's lending platform, users would be subject to an increased risk of fraud or identity theft, and IOU Financial may not receive the principal or interest payments that it expects to receive on any loans that it was fraudulently induced to make. Hackers might also disrupt the accurate processing and posting of payments to IOU Financial's accounts on its lending platform, or cause the destruction of data and thereby undermine IOU Financial's rights to repayment of the loans it has made. While IOU Financial has taken steps to prevent hackers from accessing its lending platform, if it is unable to prevent hacker access, its ability to receive the principal and interest payments that it expects to receive on loans it made and its ability to service its loans and to maintain its lending platform could be adversely affected.

Maintenance of Client Relationships

The ability of IOU Financial to attract and maintain clients requires that it provide a competitive offering of products and services that meet the needs and expectations of its clients. IOU Financial's ability to satisfy the needs or demands of its clients may be adversely affected by factors such as the inability or failure to identify changing client needs or expectations or the inability to adapt in a timely and cost-effective manner to innovative products and services offered by competitors.

Litigation Risk

IOU Financial's business may become susceptible from time to time to various legal claims, including class action claims, in the course of its operations or with respect to the interpretation of existing agreements. Any future claims or litigation could have a material adverse effect on IOU Financial's business and its profitability.

Possible Volatility of Stock Price

The market price of the common Shares could be subject to wide fluctuations in response to factors such as actual or anticipated variations in IOU Financial's results of operations, changes in financial estimates by securities analysts or by management, general market conditions and other factors. Market fluctuations, as well as general economic, political and market conditions such as recessions, interest rate changes or international currency fluctuations may adversely affect the market price of the common shares.

GENERAL

The Company also discloses information related to its activities on SEDAR at www.sedar.com and on its website www.ioufinancial.com

IOU Financial

Business Lending. Simplified.

IOU Financial Inc.

Consolidated Financial Statements

For the Years Ended
December 31, 2019 and 2018

IOU FINANCIAL INC.

Consolidated Financial Statements

For the Years Ended
December 31, 2019 and 2018

Independent auditor's report

To the Shareholders of
IOU Financial Inc.

Our opinion

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the financial position of IOU Financial Inc. and its subsidiary (together, the Company) as at December 31, 2019 and 2018 and their financial performance and their cash flows for the years then ended in accordance with International Financial Reporting Standards as issued by the International Accounting Standards Board (IFRS).

What we have audited
The Company's consolidated financial statements comprise:

- the consolidated statements of financial position as at December 31, 2019 and 2018;
- the consolidated statements of comprehensive income for the years then ended;
- the consolidated statements of changes in shareholders' equity for the years then ended;
- the consolidated statements of cash flows for the years then ended; and
- the notes to consolidated financial statements, which include a summary of significant accounting policies.

Basis for opinion

We conducted our audit in accordance with Canadian generally accepted auditing standards. Our responsibilities under those standards are further described in the *Auditor's responsibilities for the audit of the consolidated financial statements* section of our report.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Independence
We are independent of the Company in accordance with the ethical requirements that are relevant to our audit of the consolidated financial statements in Canada. We have fulfilled our other ethical responsibilities in accordance with these requirements.

Material uncertainty related to going concern

We draw attention to note 2 to the consolidated financial statements, which describes events or conditions that indicate the existence of a material uncertainty that may cast significant doubt about the Company's ability to continue as a going concern. Our opinion is not modified in respect of this matter.

Other information

Management is responsible for the other information. The other information comprises the Management's Discussion and Analysis.

Our opinion on the consolidated financial statements does not cover the other information, and we do not express any form of assurance conclusion thereon.

In connection with our audit of the consolidated financial statements, our responsibility is to read the other information identified above and, in doing so, consider whether the other information is materially inconsistent with the consolidated financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated.

If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

Responsibilities of management and those charged with governance for the consolidated financial statements

Management is responsible for the preparation and fair presentation of the consolidated financial statements in accordance with IFRS, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the consolidated financial statements, management is responsible for assessing the Company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Company or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Company's financial reporting process.

Auditor’s responsibilities for the audit of the consolidated financial statements

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor’s report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with Canadian generally accepted auditing standards will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated financial statements.

As part of an audit in accordance with Canadian generally accepted auditing standards, we exercise professional judgment and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company’s internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management’s use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Company’s ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor’s report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor’s report. However, future events or conditions may cause the Company to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Company to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

The engagement partner on the audit resulting in this independent auditor's report is Jean-Luc Tremblay.

PricewaterhouseCoopers LLP[1]

Montréal, Quebec
April 29, 2020

[1] CPA auditor, CA, public accountancy permit No. A125840

IOU FINANCIAL INC.

Consolidated Statements of Financial Position
As at December 31, 2019 and 2018
(in Canadian dollars, except as otherwise noted)

	Note	**2019** **$**	2018 $
Assets			
Cash and cash equivalents		5,332,532	6,761,170
Restricted cash		1,378,989	1,970,080
Sales taxes receivable		23,286	26,754
Commercial loans receivable, net	**5**	54,449,029	32,332,180
Servicing assets	**5**	1,405,302	1,920,794
Other receivables		211,940	239,540
Prepaid expenses and deposits		114,772	159,172
Equipment and leasehold improvements	**6**	145,233	178,036
Intangible assets	**7**	54,940	143,372
Right-of-use assets	**8**	716,787	-
Total Assets		63,832,810	43,731,098
Liabilities			
Accounts payable and accrued liabilities	**9**	2,042,877	1,709,751
Financing credit facilities	**10**	37,954,729	19,758,556
Convertible debentures	**11**	9,931,181	10,407,017
Lease liabilities	**8**	753,645	-
Total Liabilities		50,682,432	31,875,324
Shareholders' Equity			
Share capital	**13**	26,988,530	27,171,722
Contributed surplus		4,477,383	4,189,397
Accumulated other comprehensive income		2,077,163	2,410,662
Deficit		(20,392,698)	(21,916,007)
Total Shareholders' Equity		13,150,378	11,855,774
Total Liabilities and Shareholders' Equity		63,832,810	43,731,098

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

Approved by the Board on April 29, 2020

Phil Marleau (*signed*), Director
Wayne Pommen (*signed*), Director

IOU FINANCIAL INC.

Consolidated Statements of Comprehensive Income
For the Years Ended December 31, 2019 and 2018
(in Canadian dollars, except as otherwise noted)

	Note	2019 $	2018 $
Revenue			
Interest revenue	**15**	**17,861,394**	13,464,475
Other fees and servicing income	**15**	**1,754,589**	1,792,625
Net gain recognized on sale of loans	**5**	**3,650,733**	3,910,949
Gross Revenue		**23,266,716**	19,168,049
Cost of Revenue			
Interest expense		**3,998,673**	3,355,496
Provision for loan losses, net of recoveries	**5**	**7,703,592**	4,682,324
Total Cost of Revenue		**11,702,265**	8,037,820
Net Revenue		**11,564,451**	11,130,229
Operating expenses	**17**	**9,919,772**	8,535,687
Earnings Before Income Taxes		**1,644,679**	2,594,542
Income tax expense (recovery)	**16**	**121,370**	(115,676)
Net Earnings for the Year		**1,523,309**	2,710,218
Currency translation differences		**(454,869)**	1,563,882
Income tax	**16**	**121,370**	(115,676)
Other comprehensive (loss) income		**(333,499)**	1,448,206
Comprehensive Income for the Year		**1,189,810**	4,158,424
Earnings per Share:			
Basic	**12**	**0.02**	0.03
Diluted	**12**	**0.02**	0.03

Net earnings and comprehensive income are entirely attributable to the shareholders of the Company. Other comprehensive income is entirely subject to be reclassified to net earnings.

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

IOU FINANCIAL INC.

Consolidated Statements of Changes in Shareholders' Equity
For the Years Ended December 31, 2019 and 2018
(in Canadian dollars, except as otherwise noted)

	Note	Common Shares (#)	Share Capital ($)	Contributed Surplus ($)	Accumulated OCI [1] ($)	Deficit ($)	Shareholders' Equity ($)
Balance as at December 31, 2017, as published		87,825,309	27,171,722	4,023,120	962,456	(23,927,886)	8,229,412
Impacts of adopting IFRS 9		-	-	-	-	(698,339)	(698,339)
Balance at January 1, 2018, as adjusted		87,825,309	27,171,722	4,023,120	962,456	(24,626,225)	7,531,073
Comprehensive income for the year		-	-	-	1,448,206	2,710,218	4,158,424
Stock-based compensation	**13**	-	-	166,277	-	-	166,277
Balance as at December 31, 2018		**87,825,309**	**27,171,722**	**4,189,397**	**2,410,662**	**(21,916,007)**	**11,855,774**
Comprehensive income for the year		**-**	**-**	**-**	**(333,499)**	**1,523,309**	**1,189,810**
Warrants exercised	**13**	**348,313**	**69,662**	**-**	**-**	**-**	**69,662**
Debentures exercised	**11**	**200,000**	**100,000**	**-**	**-**	**-**	**100,000**
Shares repurchased	**13**	**(1,665,500)**	**(352,854)**	**-**	**-**	**-**	**(352,854)**
Stock-based compensation	**13**	**-**	**-**	**287,986**	**-**	**-**	**287,986**
Balance as at December 31, 2019		**86,708,122**	**26,988,530**	**4,477,383**	**2,077,163**	**(20,392,698)**	**13,150,378**

[1] OCI: Other Comprehensive Income

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

IOU FINANCIAL INC.

Consolidated Statements of Cash Flows
For the Years Ended December 31, 2019 and 2018
(in Canadian dollars, except as otherwise noted)

	Note	2019 $	2018 $
Operating Activities			
Net earnings for the year		**1,523,309**	2,710,218
Non-cash items included in net earnings	**18**	**(17,181,434)**	(13,875,748)
Change in non-cash working capital items	**18**	**(114,955,469)**	(92,588,061)
Sale of commercial loans		**93,261,010**	95,692,623
Interest received		**16,177,700**	12,319,263
Interest expense		**4,062,894**	3,355,496
Interest paid		**(4,110,655)**	(3,392,030)
Cash (used) generated in operating activities		**(21,222,645)**	4,221,761
Investing Activities			
Additions to equipment and leasehold improvements		**(42,334)**	(33,888)
Additions to intangible assets		**-**	(10,697)
Deductions (Additions) to restricted cash		**591,091**	(106,378)
Cash used in investing activities		**548,757**	(150,963)
Financing Activities			
Transaction costs paid		**(81,546)**	(465,571)
Issuance of equity, net of transaction costs	**13**	**(183,192)**	-
Proceeds from financing credit facilities	**10**	**19,906,790**	-
Repayment of financing credit facilities	**10**	**-**	(1,280,900)
Decrease in lease liabilities		**(154,491)**	-
Cash generated (used) in financing activities		**19,487,561**	(1,746,471)
(Decrease) Increase in Cash		**(1,186,327)**	2,324,327
Exchange rate difference on cash		**(242,311)**	460,848
Cash			
Beginning of period		**6,761,170**	3,975,995
End of period		**5,332,532**	6,761,170

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

Notes to the Consolidated Financial Statements
For the Years Ended
December 31, 2019 and 2018
(in Canadian dollars, except as otherwise noted)

1. General Information

IOU Financial Inc. ("IOU Financial") was incorporated under Part IA of the Companies Act (Quebec) and is governed by the Business Corporations Act (Quebec). The registered office of IOU Financial is located at 1 Place Ville-Marie, Suite 1670, Montréal, Quebec, Canada.

IOU Financial's wholly owned subsidiary IOU Central Inc. ("IOU Central") was incorporated under the Canada Business Corporations Act on August 10, 2006 and presently operates an internet-based commercial lending business in the United States of America, through its subsidiary, IOU Central Inc. (USA) ("IOU USA"), based in the state of Georgia (incorporated in Delaware on August 16, 2006). On January 1, 2020, IOU Central was dissolved, leaving IOU USA to be a subsidiary of IOU Financial.

IOU Financial's wholly owned subsidiary IOU Financial Canada Inc. ("IOUF Canada") was incorporated on December 1, 2015 under the Business Corporations Act (Quebec). IOUF Canada is engaged in the commercial lending business in Canada.

IOU USA's wholly owned subsidiary IOU Small Business Asset Fund, LLC ("IOU SBAF") was incorporated on December 9, 2015 as a Delaware limited liability company and currently holds a portfolio of commercial loans receivable.

IOU USA's new wholly owned subsidiary, IOU Small Business Asset Fund II, LLC ("IOU SBAF II"), was incorporated on January 2, 2019 as a Delaware limited liability company and currently holds a portfolio of commercial loans receivable.

IOU Financial is a public company listed on the TSX Venture Exchange (TSX-V).

The term "Company" in these consolidated financial statements refers collectively to IOU Financial and its wholly owned subsidiaries: IOU Central, IOU USA, IOUF Canada, IOU SBAF and IOU SBAF II.

These consolidated financial statements were authorized for issuance by the Board of Directors of the Company on April 29, 2020.

2. Going Concern

These financial statements have been prepared using Canadian generally accepted accounting principles applicable to a going concern, which contemplates the realization of assets and settlement of liabilities in the normal course of business as they become due.

For the year ended December 31, 2019, the consolidated net earnings of IOU Financial were $1,523,309 (2018 - $2,710,218). IOU Financial met all of its covenants as at December 31, 2019. However, commencing in March 2020, as disclosed in note 21, the coronavirus pandemic ("Covid-19") caused disruption, slowdown and even temporary closures of several of the Company's clients. In an effort to help its clients, in late March 2020, management began the process of effecting modified payment plans for clients manifesting bona fide hardships directly attributable to the impacts of the Covid-19 pandemic. The nature and duration of the modified plans varied according to the degree of hardship experienced by each client. As a result of the disruption cause by the Covid-19 pandemic and of entering into these modified plans, IOU Financial exceeded the concentration limits set forth in the financing credit facilities creating over advances on March 27, 2020 and on April 1, 2020 for the 2019 Credit Facility and the 2016 Credit Facility, respectively.

The availability of the above noted financing credit facilities is subject to IOU Financial maintaining the financial covenants on a quarterly basis, otherwise the financing credit facilities become repayable. These circumstances give significant doubt as to the ability of IOU Financial to meet its obligations as they come due and, accordingly, the appropriateness of the use of accounting principles applicable to a going concern.

In recognition of these circumstances, the Company and the financing credit facilities are working together to remedy the situation. Nevertheless, there is no assurance that these initiatives will be successful.

These financial statements do not reflect the adjustments to the carrying values of assets and liabilities and the reported expenses and balance sheet classifications that would be necessary If the Company were unable to realize its assets and settle its liabilities as a going concern in the normal course of operations. Such adjustments could be material.

3. Basis of Preparation

The consolidated financial statements of the Company have been prepared in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB"). These consolidated financial statements have been prepared under the historical cost convention. Other measurement bases used are described in the applicable notes.

4. Significant Accounting Policies

The principal accounting policies applied in the preparation of these consolidated financial statements are consistent with those applied in the previous financial year, except as described below.

4.1 Current and Future Changes in Accounting Policies

The Company has adopted the following new and revised standards, along with any consequential amendments, effective January 1, 2019.

a) New standards adopted during the year

IFRS 16, Leases

On January 1, 2019, the Company adopted IFRS 16, *Leases*, which supersedes IAS 17, *Leases*, and the related interpretations on leases: IFRIC 4, *Determining Whether an Arrangement Contains a Lease*; SIC 15, *Operating Leases – Incentives* and SIC 27, *Evaluating the Substance of Transactions Involving the Legal Form of a Lease*. The Company has adopted the new standard for its annual periods beginning on January 1, 2019, on a modified retrospective basis whereby comparative information has not been adjusted. That new standard affects mostly the Company's operating lease commitments presented in Note 19 to the annual consolidated financial statements. Following the adoption of the new standard, the operating lease commitments are recognized in the Company's consolidated statements of financial position with an increase in assets due to the recognition of the right to use the leased assets (right-of-use assets) and an increase in liabilities due to recognition of the obligation to make lease payments (lease liabilities). Furthermore, given that the previous linear operating lease expense, which approximates the amount of the contractual lease payments, has been replaced by an amortization of the right-of-use assets separately from an interest expense on the lease liability, the nature of the operating expenses of the Company differs.

IFRIC 23, Uncertainty over Income Tax Treatments

On January 1, 2019, the Company adopted IFRIC 23, which provides guidance on when the recognition of a current or deferred tax asset or liability is appropriate when there are amounts for which the ultimate income tax treatment is uncertain. The Company has evaluated that there is no impact on its consolidated financial statements.

b) New Standards and Interpretations not yet Adopted that Are Relevant to the Company

A number of new standards and amendments to standards and interpretations are effective for annual periods beginning after January 1, 2020 and have not been applied in preparing these consolidated financial statements. None of these is expected to have a significant effect on the consolidated financial statements of the Company.

4.2 Use of Estimates and Judgments

The preparation of consolidated financial statements in conformity with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgment in the process of applying the Company's accounting policies. Estimates and judgments are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. The areas involving a higher degree of judgment or complexity, or areas where assumptions and estimates are significant to the consolidated financial statements are described below:

1. Critical Accounting Estimates and Assumptions

   The Company makes estimates and assumptions concerning the future. The resulting accounting estimates will, by definition, seldom equal the related actual results. The estimates and assumptions that have a significant risk of causing a significant adjustment to the carrying amounts of assets and liabilities within the next financial year are addressed below.

   1.1 Deferred Tax Estimation

   The recognition of deferred tax assets and liabilities involves making assumptions including estimating the timing of the reversal of temporary differences or if it is probable that temporary differences will not reverse in the foreseeable future.

   The realization of deferred tax assets ultimately depends on taxable profits being available in the future. Deferred tax assets should be recognized when it is probable that taxable profits will be available against which the deferred tax asset can be utilized and it is probable that the entity will earn sufficient taxable profit in future periods to benefit from a reduction in tax payments. This involves the Company making assumptions within its overall tax-planning activities and periodically reassessing them in order to reflect changed circumstances as well as tax regulations. Moreover, the measurement of a deferred tax asset or liability reflects the manner in which the Company expects to recover the asset's carrying value or settle the liability.

1.2 Servicing Assets

The initial recognition of servicing assets requires the Company to make estimates of the fair value of the service to be provided, which is based on market expectations at the time of the sale of the loan and may vary from the actual cash flows received.

1.3 Valuation of Commercial Loans

Management exercises judgment to determine the expected credit losses ("ECL") based on all available reasonable and supportable information about past events, current conditions and forecasts of future events and economic conditions. Further details on the estimates used to determine any allowance for impaired loans receivable are provided in the accounting policy "Impairment of OTH Loans".

Basis of Consolidation

The consolidated financial statements include the accounts of IOU Financial and its subsidiaries, which are the entities over which IOU Financial has control. The Company controls an entity when the Company is exposed to, or has the rights to, variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity. Subsidiaries are fully consolidated from the date on which control is transferred to the Company. They are deconsolidated from the date that control ceases.

All intercompany transactions, balances, income and expenses are eliminated in full on consolidation.

Segment Reporting

Operating segments are reported in a manner consistent with the internal reporting provided to the chief operating decision-maker. The chief operating decision-maker, who is responsible for allocating resources and assessing performance of the operating segments, has been identified as the Chief Executive Officer ("CEO").

Equipment and Leasehold Improvements

Equipment and leasehold improvements are stated at historical cost less residual value, accumulated depreciation and impairment losses. Historical cost includes expenditures that are directly attributable to the acquisition of the items. The depreciation rate, residual value and useful life of equipment are reviewed annually and adjusted if appropriate. Depreciation based on the estimated useful life of the assets is calculated as follows:

Office Equipment	20% straight-line method
Computer Equipment	30% straight-line method
Leasehold Improvements	Over remaining lease term

An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount.

Intangible Assets

The costs to develop software for the Company's website and online loan platform are capitalized when management has authorized and committed project funding, preliminary development efforts are successfully completed, and it is probable that the project will be completed and the software will be used as intended. Capitalized software development costs primarily include fees paid to outside consultants and salaries for employees directly involved in the development efforts. Costs incurred prior to meeting these criteria, together with costs incurred for training and maintenance, are expensed. Costs incurred for upgrades and enhancements that are considered to be probable to result in additional functionality are capitalized. The Company capitalizes expenditures for betterments and expenses amounts for maintenance, repairs and renewals as they are incurred.

Internal use software is stated at cost less accumulated amortization. Amortization and useful lives are reviewed annually. Capitalized costs are amortized using the straight-line method over their expected lives, which presently approximate three years.

Leases

Before January 1, 2019 (IAS 17)

Leases are classified as finance leases when the terms of the lease transfer substantially all the risks and rewards of ownership to the lessee. All other leases are classified as operating leases.

Operating lease payments are recognized as an expense on a straight-line basis over the lease term.

Starting January 1, 2019 (IFRS 16)

IFRS 16 eliminates the classification of leases as either operating or finance leases and introduces a single accounting model for the lessee under which a lease liability and a right-of-use asset are recognized for all leases with a term of more than 12 months (except if the value of the underlying asset is low).

The lease liabilities and right-of-use assets are initially measured at the present value of the lease payments payable over the lease term, discounted at the Company's incremental borrowing rate.

Each month, the right-of-use assets are amortized on a linear basis until the end of the lease. Lease payments are apportioned between the lease liabilities and interest expense.

Lessors must still classify their leases as finance or operating, as the approach to lessor accounting is substantially unchanged.

Impairment of Tangible and Intangible Assets

At the end of each reporting period, the Company reviews the carrying amounts of its tangible and intangible assets to determine whether there is any indication of impairment. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss, if any. Where it is not possible to estimate the recoverable amount of an individual asset, the Company estimates the recoverable amount of the cash-generating unit ("CGU") to which the asset belongs. Where a reasonable and consistent basis of allocation can be identified, corporate assets are also allocated to individual CGUs.

Recoverable amount is the higher of fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset for which the estimates of future cash flows have not been adjusted.

If the recoverable amount of an asset is estimated to be less than its carrying amount, the carrying amount of the asset is reduced to its recoverable amount. An impairment loss is recognized immediately in the consolidated statements of comprehensive income (loss).

Where an impairment loss subsequently reverses, the carrying amount of the asset is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognized for the asset in prior years. A reversal of an impairment loss is recognized immediately in the consolidated statements of comprehensive income (loss).

Financial Instruments

Classification and Measurement – Financial Assets

At initial recognition, all financial assets are recorded at fair value on the consolidated statements of financial position. After initial recognition, financial assets are classified either at (i) amortized cost; (ii) fair value through profit or loss (“FVTPL”); or (iii) fair value through other comprehensive income (“FVOCI”).

Such classification is based on:

- the contractual cash flow characteristics of the financial assets; and
- the Company’s business model for managing these financial assets.

The contractual cash flows associated with the financial asset must be solely payments of principal and interest on the outstanding principal amount for the asset to be classified at amortized cost or for a debt instrument held to be classified as FVOCI; otherwise it must be classified and measured at FVTPL.

The table below presents the different classifications for each of the three possible business models that can be used to manage, on a portfolio basis, a group of financial assets to achieve their respective business objectives.

Business Model	Business Objective	Classification
Originated to hold (OTH)	Solely the collection of the contractual cash flows of the financial assets	Amortized cost
Originated to sell (OTS)	Sale of the financial assets or managed on a fair value basis	FVTPL
Originated to hold and sell	Both the collection of contractual cash flows of the financial assets and their sale	FVOCI

In addition, debt instruments held that would otherwise be measured at amortized cost or at FVOCI can be designated upon initial recognition using the fair value option if doing so would reduce an accounting mismatch. Equity instruments held are always measured at FVTPL unless they are designated upon initial recognition at FVOCI, whereby subsequent changes in fair value would be recorded in OCI and would never be reclassified to net income (loss).

The following table presents the Company's classification of its financial assets. The Company has no financial assets at FVOCI and has not used the fair value option.

Financial Assets	Classification
Cash	Amortized cost
Restricted cash	Amortized cost
OTH loans	Amortized cost
OTS loans	FVTPL
Other receivables	Amortized cost

Commercial Loans Receivable
The Company recognizes commercial loans receivable when cash is advanced to a borrower. Commercial loans are initially recognized at fair value plus directly attributable costs and are subsequently measured at amortized cost using the effective interest method for OTH loans or at fair value for OTS loans.

Presentation
OTH loans are presented net of allowances for expected credit losses on the consolidated statements of financial position.

The interest income on OTS loans is recorded in interest revenue in the consolidated statements of comprehensive income (loss). Changes in the fair value of OTS loans are recognized in net gain recognized on sale of loans in the consolidated statements of comprehensive income (loss).

Reclassifications
The portfolio of commercial loans designated as OTS at initial recognition would be reclassified as OTH only in rare situations when there is a change in the business model used to manage the portfolio. Such a reclassification would be applied prospectively from the reclassification date.

Impairment of OTH Loans
At the end of each reporting period, the Company applies a three-stage forward-looking impairment approach to measure the ECLs on its OTH loans. The stages are based on the change in the credit quality of the OTH loan since initial recognition. Measurement of ECLs at each reporting period reflects reasonable and supportable information about past events, current conditions, and forecasts of future events and economic conditions.

The following table presents the three stages of the Company's impairment model.

Stage	Credit Quality – Reporting Date vs. Initial Recognition	Impairment Amount
1	No significant increase	Equals to 12-month ECL
2	Significant increase	Equals to lifetime ECL
3	Credit-impaired	Equals to lifetime ECL or the financial asset is written off

Interest Income
The interest income is calculated on the gross carrying amount of the OTH loans in stages 1 and 2 and on the net carrying amount of the OTH loans in stage 3.

Changes in Credit Risk
The Company considers that a significant increase in credit risk exists after a commercial loan has one missed payment or earlier if other reasonable and supportable information exists to support the estimated increase in probability of default of the OTH loan. The assessment of a significant increase in credit risk requires significant judgment.

If the credit risk of an OTH loan improves such that there is no longer a significant increase in credit risk since initial recognition, the OTH loan reverts from stage 2 to stage 1.

Credit-Impaired Loans
The definition of default used by the Company to identify its credit-impaired OTH loans is consistent with the definition of default used for internal credit risk management purposes. The Company considers that an event of default occurs when a payment is late by more than 90 days or earlier when one or more events that have a detrimental impact on the estimated future cash flows of the commercial loan have occurred.

Write offs
Commercial loans are written off when the Company considers the probability of recovery to be non-existent due to:

(i) having exhausted reasonable recovery efforts; or
(ii) the borrower is bankrupt or winding up, and balances owing are not likely to be recovered.

ECL Measurement
ECLs are measured as the probability-weighted present value of all expected cash shortfalls over the remaining expected life of the financial instrument, and reasonable and supportable information about past events, current conditions and forecasts of future events and economic conditions is considered. The estimation and application of forward-looking information requires significant judgment. The cash shortfall is the difference between all contractual cash flows owed to the Company and all the cash flows that the Company expects to receive.

The measurement of ECLs is primarily based on the product of the OTH loan's:
- probability of default;
- loss given default; and
- exposure at default.

Forward-looking macroeconomic factors such as credit default indices, interest rates and gross domestic product are incorporated into the risk parameters. The estimate of ECL losses reflects an unbiased and probability-weighted amount that is determined by evaluating a range of possible outcomes. Due to the short-term nature of the Company's commercial loans, the forward-looking macroeconomic factors are generally of a lesser importance to the Company.

The Company applies experienced credit judgment to adjust the modelled ECL results when it becomes evident that known or expected risk factors and information were not considered in the credit risk rating and modelling process.

Classification and Measurement – Financial Liabilities
The following table presents the Company's classification of its financial liabilities.

Financial Liabilities	**Classification**
Accounts payable and accrued liabilities	Amortized cost
Financing credit facilities	Amortized cost
Convertible debentures	Amortized cost

Definitions – Financial Instruments

Term	Meaning
Amortized cost	The principal is generally the fair value of the financial instrument at initial recognition. The interest consists of consideration for the time value of money, the credit risk associated with the principal amount outstanding during a particular period of time, and other basic lending risks and costs as well as of a profit margin.
Exposure at default	Outstanding balances anticipated at each point in time and assuming previous payments were made. Expected exposure at default decreases over time until it reaches zero upon loan maturity.
Fair value	The fair value on initial recognition is the transaction price, which is the fair value of the consideration given or received. Subsequent to initial recognition, fair value is determined by management using available market information or other valuation methodologies.
Fair value option (for a financial asset)	Irrevocable designation at FVTPL at initial recognition. Certain conditions must be met: - elimination or significant reduction in a measurement or recognition inconsistency that would otherwise arise from measuring financial assets or financial liabilities or recognizing gains and losses on them on different bases; and - fair values are reliable.
FVOCI option	Irrevocable designation, at initial recognition, of an investment in an equity instrument that is neither held for trading nor a contingent consideration recognized in a business combination as being measured at FVOCI.
Modified loans	OTH loans for which the contractual cash flows have been renegotiated or otherwise modified.
Loss given default	Reflects the losses expected should default occur and considers such factors as repayments of principal and interest between the consolidated statement of financial position date and the time of default.
Probability of default	Probabilities of a default occurring over the determined period, based on conditions existing at the consolidated statement of financial position date and on future economic conditions that have, or will have, an impact on credit risk.

Calculation of Interest Income

Type of revenue	Method of calculation
Interest – OTH loans	Effective interest rate method on the gross carrying amount
Interest – credit-impaired loans	The effective interest rate method is applied to the amortized cost of a credit-impaired loan (i.e. net of the stage 3 allowance for that loan) in subsequent reporting periods, until the loan is fully impaired or written off
Interest – modified loans	The gross carrying amount of a modified loan is recalculated as the present value of the renegotiated or modified contractual cash flows that are discounted at the loan's original effective interest rate
Interest – OTS loans	Effective interest rate method

Definitions – Calculation of Interest Income

Term	Meaning
Effective interest rate	Rate that discounts estimated future cash flows through the expected life of the financial instrument back to the net carrying amount considering all contractual cash flows, including, for commercial loans, loan origination fees, net of any transaction costs that are directly attributable to the financial instrument but, for financial assets, not future credit losses (*)
Expected life	Represents the remaining contractual life of commercial loans receivable
Loan origination fees	Fee income charged to the borrower on the origination of the financial asset

(*) Under the effective interest method, the interest realized is not necessarily the same as the stated interest rate on the agreement. The application of this method has the effect of recognizing interest on the financial instrument evenly in proportion to the amount outstanding over the period of repayment.

Loan Sales

In the normal course of business, the Company may sell its interests in commercial loans receivable. The Company derecognizes loans receivable sold only when it has transferred substantially all the risks and rewards of ownership of the assets, which occurs when the Company no longer considers itself to have any significant exposure to the variability in the present value of the future cash flows from the loans receivable. Outstanding proceeds of sold or discharged loans receivable are reported separately from other loans receivable and are measured at their realizable value, net of expected transaction costs.

Where the Company retains the servicing rights of loans sold, the benefits of servicing are assessed against market expectations. When the benefits of servicing are more than market expectations, a servicing asset is recognized. Servicing assets are carried at amortized cost. Amortization is calculated on a straight-line basis over the term of the servicing agreement, which approximates one year. When the benefits of servicing are less than market expectations, a servicing liability is recognized.

Transaction Costs

Transaction costs incurred as a necessary part of completing an equity transaction are accounted for as part of that transaction and deducted from equity, net of any related income tax benefit. Transaction costs that relate to the issue of a compound financial instrument are allocated to the liability and equity components of the instrument in proportion to the allocation of proceeds. Transaction costs for all financial instruments not at FVPTL are added to the carrying amount of the instrument.

Interest Revenue

Interest revenue is recognized in the consolidated statements of comprehensive income (loss) for all financial assets measured at amortized cost using the effective interest rate method. The effective interest rate is the rate that discounts estimated future cash flows through the expected life of the financial asset back to the net carrying amount. This calculation takes into account all contractual terms of the financial instrument including the loan origination fees, net of any transaction costs that are directly attributable to the financial asset but not future credit losses. Under the effective interest method, the interest realized is not necessarily the same as the stated interest rate on the loan. The application of this method has the effect of recognizing revenue on the financial asset evenly in proportion to the amount outstanding over the period of repayment.

When a loan is classified as impaired, the original expected timing and amount of future cash flows may be revised to reflect new loan circumstances. Interest revenue continues to be recognized using the effective interest rate used to discount the future cash flows for the purpose of measuring the impairment loss. This is offset by a corresponding adjustment to the allowance for loan loss charge to reflect the fact that this additional revenue may not be collectible.

Interest income and guarantee fee income is thereafter recognized on this impaired carrying value using the effective interest rate. Additional changes to the amount or timing of future cash flows could result in further loan losses, or the reversal of prior loan losses, which would also impact the amount of subsequent income recognized.

Interest Expense

Interest expense comprises interest expense on debt borrowings and is recognized in profit or loss, in the period in which it is incurred, under the effective interest method.

Provisions

Provisions are recognized when the Company has a present legal or constructive obligation as a result of a past event, it is probable that the Company will be required to settle the obligation, and a reliable estimate can be made of the amount of the obligation.

The amount recognized as a provision is the best estimate of the consideration required to settle the present obligation at the end of the reporting period, taking into account the risks and uncertainties surrounding the obligation. Where a provision is measured using the cash flows estimated to settle the present obligation, its carrying amount is the present value of those cash flows.

Revenue Recognition

Revenue is recognized when the Company has transferred control of goods or a service (i.e. the performance obligation is satisfied). Management must use its judgment to determine when performance obligations are satisfied and establish the transaction price and the amounts allocated to such obligations.

Other Fees and Servicing Income

Fee income that is integral to the effective yield of a financial asset is recognized as an adjustment to the effective interest rate calculation and is included in financing revenue as previously described.

Fee and servicing revenue comprise service fees, insufficient funds and other administrative fees, and referral fees.

Service fees are charged on loans sold to third parties where the Company retains the servicing rights on the loans.

Insufficient funds and other administrative fee revenue is charged and collected on all missed payments or for other administrative reasons and is recognized as it is earned.

Referral fee revenue is collected upon the successful referral and funding of unfunded loan applications to third parties. This revenue is recognized when it is earned.

Cash and Restricted Cash

Cash and restricted cash comprise cash in hand, deposits held at call with banks and restricted cash. Restricted cash comprises bonding insurance collateral and cash held as security for payment clearing activities.

Convertible Debentures

Convertible debentures are separated into their liability and equity components. The fair value of the liability component at the time of issue is determined based on an estimated interest rate of the debenture without the conversion feature. The amount attributed to the equity component is determined as the difference between the fair value of the convertible debenture as a whole and the fair value of the liability component.

Subsequent to initial recognition, the liability component is measured at amortized cost using the effective interest method. The equity component is not remeasured subsequent to initial recognition and is reclassified within equity on conversion or expiry.

Share Capital

Common shares are classified as equity. Incremental costs directly attributable to the issue of new common shares are shown in equity as a deduction, net of tax, from the proceeds.

Contributed Surplus

Contributed surplus is used to record the accumulated fair value of stock options recognized as stock-based payments and warrants issued. Contributed surplus is increased by the compensation charge over the vesting period and is reduced by corresponding amounts when the options and warrants are exercised, forfeited or expire.

Foreign Exchange

a) Functional and Presentation Currency

Items included in the financial statements of each of the Company's entities are measured using the currency of the primary economic environment in which the entity operates (the "functional currency"). The consolidated financial statements are presented in Canadian dollars. The functional currency of IOU USA, IOU SBAF and IOU SBAF II is the US dollar, while the rest of the Company uses the Canadian dollar as its functional currency.

b) Group Companies

The assets and liabilities of the subsidiaries with a US dollar functional currency are translated at the exchange rate prevailing on the reporting date, and revenues and expenses at the average rates during the reporting period. Foreign currency gains or losses resulting from the translation of those subsidiaries are recorded in other comprehensive income (loss) with a corresponding increase or decrease to the foreign currency translation reserve component of accumulated other comprehensive income (loss), which is a component of shareholders' equity.

Stock-Based Compensation

The Company operates an equity-settled stock-based compensation plan, under which the entity receives services from employees as consideration for equity instruments (options) of the Company. The fair value of the employee and others providing similar services received in exchange for the grant of options is recognized as an expense with a corresponding increase to contributed surplus. The total amount to be expensed is determined by reference to the fair value of the options granted at the grant date.

Each tranche of a stock-based compensation award with a different vesting date is considered a separate grant for the calculation of fair value, and the resulting fair value is amortized over the vesting period of the respective tranches, based on the Company's estimate of equity instruments that will eventually vest. At the end of each reporting period, the Company revises its estimate of the number of equity instruments expected to vest. The impact of the revision of the original estimates, if any, is recognized in the consolidated statements of comprehensive income (loss), such that the cumulative expense reflects the revised estimate with a corresponding adjustment to contributed surplus.

When the options are exercised, the Company issues new shares. The proceeds received net of any directly attributable transaction costs are credited to share capital. Any amounts previously credited to contributed surplus relating to the original stock-based compensation is also allocated to share capital.

Taxation

Income tax expense or recovery represents the sum of the tax currently payable and deferred tax.

a) Current Tax

The tax currently payable is based on taxable income for the year. Taxable income differs from net earnings as reported in the consolidated statements of comprehensive income (loss) because of items of income or expense that are taxable or deductible in other years and items that are never taxable or deductible. The Company's liability for current tax is calculated using tax rates that have been enacted or substantively enacted by the end of the reporting period.

b) Deferred Tax

Deferred tax is recognized, using the balance sheet method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated statements of financial position. Deferred tax is calculated using tax rates and laws that have been enacted or substantively enacted at the end of the reporting period, and which apply when the related deferred income tax asset is expected to be realized or the deferred income tax liability is expected to be settled.

i) Deferred Tax Liabilities:

- are generally recognized for all taxable temporary differences; and
- are not recognized on temporary differences that arise from goodwill which is not deductible for tax purposes or the initial recognition of an asset or liability in a transaction which is not a business combination and at the time of the transaction, affects neither accounting nor taxable profit (loss).

ii) Deferred Tax Assets:

- are recognized to the extent it is probable that taxable profits will be available against which the deductible temporary differences can be utilized; and
- are reviewed at the end of the reporting period and reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the asset to be recovered.

Deferred tax assets and liabilities are offset when there is a legally enforceable right to set off current tax assets against current tax liabilities and when they relate to income taxes levied by the same taxation authority and the Company intends to settle its current tax assets and liabilities on a net basis.

c) Current and Deferred Tax for the year

Current and deferred tax are recognized as an expense or income in net earnings, except when they relate to items that are recognized outside profit or loss (whether in other comprehensive income (loss) or directly in equity), in which case the tax is also recognized outside profit or loss, or where they arise from the initial accounting for a business combination. In the case of a business combination, the tax effect is included in the accounting for the business combination.

Basic and Diluted Earnings per Share

Earnings per share is calculated using the weighted average number of shares outstanding during the year. Diluted earnings per share is computed using the treasury stock method, giving effect to the exercise of all stock options, warrants and convertible debentures. The diluted earnings per share is equal to the basic earnings per share due to the anti-dilutive effect of these elements.

4.3 Impacts of IFRS 16 Adoption

Following the adoption of the aforementioned IFRS 16, the Company has updated its significant accounting policies as follows.

IOU as Lessee

The Company subleases office spaces under agreements having original terms between 5 and 12 years that are non-cancellable prior to August 31, 2023. These leases are renewable at the end of the respective lease terms.

(in Canadian dollars, except as otherwise noted)

The Company rents its Canadian office space from Palos Management Inc. The lease may be cancelled after October 2021 upon the payment of a termination fee. The Company also rents office space in the United States. The termination date for that lease is December 31, 2023. Upon adopting IFRS 16 as at January 1, 2019, instead of having solely a rent expense, the Company now recognizes right-of-use assets which equal the amount of the initial measurement of the lease liabilities.

The following table reconciles operating lease commitments as at December 31, 2018 and lease liabilities recognized in the consolidated balance sheet as at January 1, 2019:

Operating lease commitments reported as at December 31, 2018	1,698,912
Adjustment related to the Company's incremental borrowing rate as at January 1, 2019	(793,405)
Adjustment related to common areas	182,750
Lease liabilities as at January 1, 2019	**1,088,257**

IOU as Lessor

The Company classifies the subleases as operating leases by reference to the right-of-use assets arising from the head lease. Therefore, the impact of the modifications of the standard is not material to the Company's consolidated financial position.

5. Commercial Loans Receivable

As at December 31, 2019 and 2018, the Company held commercial loans receivable as part of its regular operations.

	2019	2018
	$	$
Principal balance of OTH loans	**56,871,350**	34,504,755
Unamortized fees and transaction costs	**2,092,854**	1,151,539
OTH loans	**58,964,204**	35,656,294
Allowance for expected credit losses	**(4,515,175)**	(3,324,114)
Commercial loans receivable, net	**54,449,029**	32,332,180

The loans bear fixed interest at rates ranging between 9.25% and 15.99% (2018: 9.25% and 15.99%) and mature no later than 18 months (2018: 15). As at December 31, 2019, 10.70% (2018: less than 1.00%) of commercial loans receivable have a maturity date over 12 months. Guarantee fees charged on each loan range between 7.00% and 29.00% (2018: 7.00% and 23.00%) of the original loan amount. At inception, the loans have an average date to maturity of 12.0 months (2018: 11.6 months). The loans are being repaid daily or weekly over their terms. Loans are not collateralized but are backed by a general security agreement against all of the assets of the business and are personally guaranteed by the owner(s) of the business. The commercial loans receivable is substantially all denominated in US dollars. Transaction costs and unamortized fees comprise broker commissions and loan closing fees and are recognized over the term of the loan through the effective rate mechanism.
The fair value of these loans is estimated to be equivalent to the carrying amount, due to the residual short-term nature of these loans.

Credit Quality of OTH Loans

The following table presents the gross carrying amount of commercial loans receivable as at December 31, 2019, according to credit quality and ECL impairment stages.

	%	Gross Carrying Amount	Allowance for Expected Credit Losses	Net Carrying Amount
Stage 1	85.89	50,643,436	(1,005,219)	49,638,217
Stage 2	3.45	2,037,037	(285,065)	1,751,972
Stage 3	10.66	6,283,731	(3,224,891)	3,058,840
Total	**100.00**	**58,964,204**	**(4,515,175)**	**54,449,029**

(in Canadian dollars, except as otherwise noted)

The following table presents the gross carrying amount of commercial loans receivable as at December 31, 2018, according to credit quality and ECL impairment stages.

	%	Gross Carrying Amount	Allowance for Expected Credit Losses	Net Carrying Amount
Stage 1	87.28	31,121,368	(620,256)	30,501,112
Stage 2	6.14	2,188,016	(447,926)	1,740,090
Stage 3	6.58	2,346,910	(2,255,932)	90,978
Total	100.00	35,656,294	(3,324,114)	32,332,180

Movement in the Allowances for Losses on OTH Loans

The following table presents the movements of the allowance for expected credit losses as at December 31, 2019.

	Stage 1	Stage 2	Stage 3	Total
Balance, December 31, 2018	620,256	447,926	2,255,932	3,324,114
Transfers to stage 1	4,295,537	(4,295,537)	-	-
Transfers to stage 2	(3,263,488)	3,263,488	-	-
Transfers to stage 3	(3,052,229)	(76,904)	3,129,133	-
Impact of originations	4,006,047	-	-	4,006,047
Net remeasurement	(1,560,339)	975,386	3,937,972	3,353,019
Net variation of the allowance	425,528	(133,567)	7,067,105	7,359,066
Loans written off	-	-	(6,198,651)	(6,198,651)
Recoveries of loans previously written off	-	-	248,043	248,043
Net write offs	-	-	(5,950,608)	(5,950,608)
Translation differences	(40,565)	(29,294)	(147,538)	(217,397)
Balance, December 31, 2019	**1,005,219**	**285,065**	**3,224,891**	**4,515,175**

Amounts charged to the allowance are charged off when there is no expectation of recovering additional cash.

Loans with a contractual amount of $6,198,651 written off during the period are still subject to enforcement activity.

Loan sales and servicing assets

During the year ended December 31, 2019, the Company sold some of its commercial loans receivable, on a non-recourse basis, at face value, for total proceeds of $93.3 million (2018: $95.7 million). At the time of sale, the Company transferred to the purchaser all rights and risks associated with the loans sold, and the Company determined that the criteria for derecognition had been met.

However, as per the debt assignment agreements, the Company retained the servicing rights (payment collections) to the loans, and the purchaser agreed to be charged a servicing fee over the term of the loans. The Company recognized a net gain on sale of the commercial loans of $3,650,733 for the year ended December 31, 2019 (2018: $3,910,949), along with servicing assets that are amortized to the consolidated statements of comprehensive income over the term of the assignment agreements. As at December 31, 2019, the carrying amount of these assets amounted to $1,405,302 (2018: $1,920,794). The servicing asset is determined by comparing the actual expected cash flows to be received to the fair value of providing such services. The fair value of the servicing was determined by using readily available third-party pricing for a similar type of service, which is around 1% of the total principal and interest collected over the term of the servicing period.

(in Canadian dollars, except as otherwise noted)

6. Equipment and Leasehold Improvements

The following table presents the carrying amount of the equipment and leasehold improvements as at December 31, 2019.

	Office Equipment $	Computer Equipment $	Leasehold Improvements $	Total $
Cost				
Balance at December 31, 2017	172,732	147,948	178,807	499,487
Translation differences	7,732	9,882	2,800	20,414
Additions	3,138	30,750	-	33,888
Balance at December 31, 2018	183,602	188,580	181,607	553,789
Translation differences	(4,672)	(6,400)	(1,727)	(12,799)
Additions	-	7,977	34,357	42,334
Balance at December 31, 2019	**178,930**	**190,157**	**214,237**	**583,324**
Accumulated Depreciation				
Balance at December 31, 2017	113,935	128,798	49,406	292,139
Translation differences	6,440	8,615	172	15,227
Depreciation expense for the year	28,547	15,909	23,931	68,387
Balance at December 31, 2018	148,922	153,322	73,509	375,753
Translation differences	(4,287)	(5,667)	(1,151)	(11,105)
Depreciation expense for the year	25,950	15,413	32,080	73,443
Balance at December 31, 2019	**170,585**	**163,068**	**104,438**	**438,091**
Carrying Amounts				
At December 31, 2018	34,680	35,258	108,098	178,036
At December 31, 2019	**8,345**	**27,089**	**109,799**	**145,233**

(in Canadian dollars, except as otherwise noted)

7. Intangible Assets

The following table presents the carrying amount of the intangible assets as at December 31, 2019. Intangible assets comprise internal use software.

	2019 **$**	2018 $
Cost		
Balance at beginning of year	**1,854,440**	1,670,550
Translation differences	**(103,462)**	173,193
Additions	**-**	10,697
Balance at end of year	**1,750,978**	1,854,440
Accumulated Amortization		
Balance at beginning of year	**1,711,068**	1,481,474
Translation differences	**(98,629)**	160,419
Amortization charge for the year	**83,599**	69,175
Balance at end of year	**1,696,038**	1,711,068
Carrying Amount	**54,940**	143,372

(in Canadian dollars, except as otherwise noted)

8. Right-of-use assets and lease liabilities

The following table presents the value of the right-of-use assets and lease liabilities as at December 31, 2019.

	2019 **$**	2018 $
Right-of-use Assets		
Balance at January 1, 2019	**1,088,257**	-
Depreciation of right-of-use assets	**(191,349)**	-
Translation differences	**(180,121)**	-
Balance at December 31, 2019	**716,787**	-
Lease Liabilities		
Balance at January 1, 2019	**1,088,257**	-
Principal payments	**(154,491)**	-
Translation differences	**(180,121)**	-
Balance at December 31, 2019	**753,645**	-

9. Accounts Payable and Accrued Liabilities

	2019 **$**	2018 $
Trade payables	**573,882**	341,114
Payable to loan purchasers	**792,916**	266,139
Other payables and accruals	**676,079**	1,102,498
Total	**2,042,877**	1,709,751

10. Financing Credit Facilities

	2019 **$**	2018 $
Balance at beginning of year	**19,758,556**	19,652,382
Proceeds	**19,906,790**	-
Repayments	**-**	(1,280,900)
New transaction costs incurred	**(375,083)**	-
Transaction costs incurred	**-**	(797,530)
Amortization of transaction costs	**461,373**	568,412
Translation differences	**(1,796,907)**	1,616,192
Balance at end of year	**37,954,729**	19,758,556

At year-end, the carrying value of the liability was composed of:

	2019 **$**	2018 $
Financing credit facilities	**38,936,865**	20,463,000
Unamortized transaction costs	**(982,136)**	(704,444)
	37,954,729	19,758,556

The carrying amount of current borrowings is a reasonable approximation of the fair value, as the facilities bear interest at a floating rate and the contractual spreads are commensurate with the spreads the Company estimates it could currently obtain.

2016 Credit Facility

On April 22, 2016, the Company entered into a US$50.0 million credit facility with a third-party lender (the “2016 Credit Facility”). The facility consisted of a US$25.0 million term loan, expandable to US$50.0 million at the Company’s request and the lender’s acceptance. The facility is denominated in US dollars and the interest rate is LIBOR plus 8.50%, which represented 10.19% as at December 31, 2019.

In February and July 2018, the 2016 Credit Facility was modified and extended until December 31, 2020, the date on which the full amount will be due. The amount of the modified facility is US$22.0 million, with a term portion equal to US$15.0 million and a revolver amount of US$7.0 million.

In December 2019, the Company modified and extended its 2016 Credit Facility until December 31, 2022. The modified interest rate of the 2016 Credit Facility is LIBOR plus 5.50%, down from LIBOR plus 8.50%. The new rate came into effect in 2020.

(in Canadian dollars, except as otherwise noted)

2019 Credit Facility

On March 5, 2019, the Company entered into a new US$50.0 million credit facility (the "2019 Credit Facility"). The facility has an initial commitment amount of US$50.0 million and is expandable to US$100.0 million at the Company's request and the lender's acceptance. The interest rate on the facility is 90-day LIBOR plus 4.50%, which represents 6.41% as at December 31, 2019. The term of the facility is three years with a revolving period ending on March 5, 2021 and an amortization period beginning after the revolving period and ending on March 5, 2022. The amount outstanding as at December 31, 2019 is US$14.0 million.

Transaction costs

Transaction costs directly attributable to the implementation and subsequent modification of the financial liabilities described above have been included in the measurement of the liabilities and are amortized over the term of the agreements using the effective rate. For the year ended December 31, 2019, amortization of $375,083 (2018: $568,412) has been included in operating expenses (Note 17).

Pledged assets

With respect to the 2016 Credit Facility, all assets held by the subsidiary IOUF SBAF are pledged as collateral for the facility. The following table presents the carrying amounts of assets pledged as collateral.

Asset	**2019** **$**	2018 $
Commercial loans receivable, net	**28,547,715**	32,332,180
Cash	**2,356,398**	3,180,786

With respect to the 2019 Credit Facility, all assets held by the subsidiary IOUF SBAF II are pledged as collateral for the facility. The following table presents the carrying amounts of assets pledged as collateral.

Asset	**2019** **$**	2018 $
Commercial loans receivable, net	**25,901,314**	-
Cash	**1,303,424**	-

Financial covenants

As part of the 2016 and the 2019 Credit Facilities, the Company must respect certain financial covenants. All financial covenants were met as at December 31, 2019.

11. Convertible Debentures

On November 2, November 20 and December 17, 2015, the Company closed tranches of an offering for convertible unsecured subordinated debentures (the “Debentures”) for aggregate gross proceeds of $11,500,000. The Debentures mature on December 31, 2020 and bear interest at a rate of 10% per annum, payable monthly. The Debentures are convertible at the holders’ option into common shares (see Note 13) at a price of $0.75 per common share, representing a conversion rate of 1,333.33 common shares for each $1,000 principal amount of the Debentures. The Company has the right to force the conversion of the Debentures into common shares at any time on or after December 31, 2018 should the 20-day volume weighted average price of the common shares on the TSX-V exceed 125% of the conversion price. The issue costs were $621,159, resulting in net proceeds of $10,878,841. The fair value of the liability component at the time of issuance was based on an estimated interest rate of 11.90% for a debt without the conversion feature. The net proceeds were attributed to the liability and equity components amounting to $10,092,467 (net of transaction costs of $576,268) and $786,374 (net of transaction costs of $44,891), respectively. Considering the issuance costs, the effective interest rate on the liability component of the Debentures is 12.14%.

On August 2, 2019, the Company amended the Debentures according to the terms below.

a) extended the maturity date of the Debentures from December 31, 2020 to December 31, 2023;
b) eliminated the condition that the Debentures be redeemable by the Company only when the current market price is 125% of the conversion price;
c) modified the conversion price of the Debentures from $0.75 to $0.50 per share;
d) eliminated the Company’s right to carry out a forced of the Debentures; and
e) eliminated the Company’s right to redeem or repay the principal amount of the Debentures with freely tradeable shares.

The conversion period for the Debentures remains unchanged and is set to expire at 5:00 p.m. on the last business day prior to December 31, 2020.

The Company issued the Debentures by way of a private placement pursuant to a trust indenture dated November 2, 2015 and entered into a supplemental trust indenture with Computershare Trust Company of Canada, the debenture trustee.

Following the amendment, the liability component of the Debentures was determined to be $10,012,175, resulting in a gain of $485,579.

On October 21, 2019, an amount of $100,000 of the Debentures was converted to 200,000 common shares at $0.50 per share, bringing the par value of Debentures from $11,500,000 to $11,400,000, and resulting in a gain of $9,028.

(in Canadian dollars, except as otherwise noted)

The Debentures recognized in the consolidated statements of financial position are calculated as follows:

	2019 **$**	2018 $
Par value of the Debentures	**11,400,000**	11,500,000
Unamortized discount and transaction costs	**(1,468,819)**	(1,092,983)
Liability component amount	**9,931,181**	10,407,017

12. Earnings per Share

	2019 **$**	2018 $
Basic and Diluted Earnings per Share		
Net earnings	**1,523,309**	2,710,218
Weighted average number of common shares for the purposes of basic earnings per share	**87,547,924**	87,825,309
Basic earnings per share	**0.02**	0.03
Effect of dilutive securities: Warrants	**-**	-
Weighted average number of common shares for the purposes of diluted earnings per share	**87,547,924**	87,825,309
Diluted earnings per share	**0.02**	0.03

The following potential common shares are anti-dilutive and are therefore excluded from the weighted average number of common shares for the purposes of diluted earnings per share.

	2019	2018
Stock options	**6,861,500**	6,201,000
Warrants	**-**	479,125
Debentures	**22,800,000**	15,333,333
Number of shares	**29,661,500**	22,013,458

(in Canadian dollars, except as otherwise noted)

13. Share Capital

Authorized

Unlimited number of common shares

Issued and Outstanding

	2019 $	2018 $
86,708,122 Common shares	**26,988,530**	
87,825,309 Common shares		27,171,722

On May 24, 2019, 348,313 warrants were exercised for total proceeds of $69,662.

As part of the Normal Course Issuer Bid ("NCIB"), in December 2019, the Company repurchased and cancelled 1,665,500 common shares in the market for a total cost of $352,854 including $4,087 of transaction costs.

On October 31, 2019, 100,000 Debentures were converted into 200,000 common shares.

Warrants

A continuity schedule of outstanding common share purchase warrants for the years presented is as follows:

	Warrants Outstanding (#)	**Average Exercise Price per Warrant ($)**
Balance as at December 31, 2017	811,148	0.36
Expired	(332,023)	0.60
Balance as at December 31, 2018	479,125	0.20
Exercised	(348,313)	0.20
Expired	(130,812)	0.20
Balance as at December 31, 2019	**-**	**-**

(in Canadian dollars, except as otherwise noted)

Stock-Based Compensation

Movements in options for the years presented are as follows:

	Options Outstanding (#)	Average Exercise Price ($)
Balance as at December 31, 2017	6,386,500	0.44
Granted	2,225,000	0.22
Forfeited	(2,410,500)	0.46
Balance as at December 31, 2018	6,201,000	0.35
Granted	2,385,000	0.23
Forfeited	(1,724,500)	0.48
Balance as at December 31, 2019	**6,861,500**	**0.28**

Stock options are granted to directors, officers, selected employees and consultants. The exercise price of the granted options is determined by the Board of Directors at a price which shall not be lower than the greater of the closing market price of the shares on the TSX,V on (a) the trading day prior to the grant of the options and (b) the date of the grant of the options.

The employee options vest over a two-year period, with one-third vesting immediately and one-third vesting on each of the first and second anniversaries of the date of the grant. Each option is exercisable for a period of five years from the date of grant, provided that it has vested.

The following summarizes information about stock options outstanding as at December 31, 2019:

Exercise Price ($)	Outstanding Options (#)	Exercisable (#)	Expiry Date
0.55	887,500	887,500	November 2020
0.27	1,699,000	1,699,000	June 2022
0.27	500,000	333,333	July 2023
0.20	1,395,000	930,000	July 2023
0.20	100,000	66,667	July 2023
0.27	500,000	166,667	March 2024
0.22	1,610,000	536,667	March 2024
0.22	100,000	16,667	March 2024
0.22	70,000	23,333	August 2024
Total	**6,861,500**	**4,659,834**	

On March 20, 2019, the Company granted options entitling certain directors, officers, employees and consultants to acquire up to 2,385,000 common shares of which 2,221,000 options remain outstanding as of December 31, 2019. The exercise price is $0.22 per share for 1,815,000 options and $0.27 per share for 500,000 options. From those options, (i) 2,215,000 vest over a two-year period, with one-third vesting immediately and one-third vesting on each of the first and second anniversaries of the date of the grant and exercisable for a period of five years from the date of grant, provided that it has vested; and (ii) 100,000 vest over a two-year period, with one-twelfth (1/12) vesting quarterly during the first 12 months and one-third vesting on each of the first and second anniversaries of the date of the grant and exercisable for a period of five years from the date of grant, provided that it has vested. The grant-date fair value has been established at $0.15 per option using the following assumptions: expected volatility of 68%, risk-free interest rate of 1.67% and an expected life to maturity that equals the term.

On August 27, 2019, the Company granted options entitling one employee to acquire up to 70,000 common shares at an exercise price of $0.22 per share. Those options are vested over a two-year period, with one-third vesting immediately and one-third vesting on each of the first and second anniversaries of the date of the grant and exercisable for a period of five years from the date of grant, provided that it has vested.

14. Financial Risk Management

The Company is exposed to a variety of financial risks including credit risk, liquidity risk and market risk (including foreign exchange and interest rate risks). The Company's overall risk management program focuses on the unpredictability of financial markets and seeks to minimize potential adverse effects on the Company's financial performance.

14.1 Financial Risks

a) Credit risk

Credit risk is managed on a Company-wide basis and results from the possibility that a loss may occur from the failure of another party to perform according to the terms of the contract. The Company regularly monitors the credit risk exposure and takes steps to mitigate the likelihood of those exposures resulting in actual loss.

(in Canadian dollars, except as otherwise noted)

The Company, in the normal course of business, monitors the financial condition of its customers and reviews the credit risk history of each customer. These policies cover the approval of credit applications, attribution of risk ratings, management of impaired loans, establishment of provisions and risk-based pricing. The Company establishes an allowance for ECLs that corresponds to the credit risk of its customers, historical trends and future economic circumstances. The Company does not believe it is exposed to an unusual level of customer credit risk. The Company's maximum credit risk is the carrying value of the cash, restricted cash, other receivables and commercial loans receivable. Refer to Note 5 for information related to the commercial loans receivable at year-end and the related allowance for ECLs.

In addition, financial instruments that potentially subject the Company to significant concentrations of credit risk consist of deposits in the form of cash and restricted cash. The Company invests with major North American financial institutions with external credit ratings varying from A- to A+. The Company has investment policies that are designed to provide for the safety and preservation of principal, the Company's liquidity needs and appropriate yields.

b) Liquidity risk

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they become due. The Company's approach in managing liquidity is to ensure, as far as possible, that it will have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Company's reputation.

The Company manages liquidity risk through the management of its capital structure. The Company has been financed mainly through equity and debt offerings, commercial loan sales and the use of its credit facilities. In order to meet its liabilities when they come due, the Company is dependent on the continued availability of such financing activities.

The following table presents the contractual maturities of financial liabilities.

			As at December 31, 2019	
	Carrying Amount	**0 to 1 Month**	**1 to 12 Months**	**Over 1 Year**
	$	**$**	**$**	**$**
Accounts payable and accrued liabilities	2,042,877	573,639	1,237,486	231,753
Financing credit facilities	37,954,729	232,514	2,333,630	41,698,550
Convertible debentures	9,931,181	94,962	1,044,582	14,818,632
Lease liabilities	753,645	18,266	204,125	853,127

Amounts denominated in foreign currency or based on variable rates are determined based on the spot rates as at December 31, 2019.

c) Foreign exchange risk

The Company, due to its operations being conducted primarily in the United States, is exposed to foreign exchange risk arising from currency exposure with respect to the US dollar. Foreign exchange risk arises from foreign denominated future commercial transactions and recognized assets and liabilities.

The Company does not use derivative financial instruments to reduce its foreign exchange exposure. Fluctuations in foreign exchange rates could cause unanticipated fluctuations in the Company's operating results.

The Company's foreign exchange exposure arising from financial instruments that would affect net earnings as at December 31, 2019 and 2018 relates to US dollar balances of the Canadian dollar functional entities and Canadian dollar balances of US dollar functional entities.

Based on the Company's foreign currency exposure noted above, varying the above foreign exchange rates to reflect a 10% strengthening of the Canadian dollar would have increased the net earnings by approximately $473,765 (2018: $618,016), assuming that all other variables remained constant. An assumed 10% weakening of the Canadian dollar would have had an equal but opposite effect on the above currencies to the amounts shown above, on the basis that all other variables remain constant.

d) Interest rate risk

The Company is subject to interest rate risk on its cash, restricted cash and financing credit facilities. A 10% increase in interest rates over a 12-month horizon based on the balances as at December 31, 2019 would decrease net earnings by approximately $285,601 (2018: $217,909).

None of the Company's current commercial lending is based on variable interest rates. The Company is also exposed to changes in the value of a loan when that loan's interest rate is at a rate other than current market rate. The Company mitigates this risk by lending for short terms, with terms at the inception of the loan generally varying from 6 to 18 months.

(in Canadian dollars, except as otherwise noted)

14.2 Management of Capital

The Company defines capital to be total shareholders' equity, which includes share capital, and certain debt, specifically the financing credit facilities and Debentures.

The Company's objective in managing capital is to ensure a sufficient liquidity position to market its loans, to finance its sales and marketing activities, research and development activities, general and administrative expenses, working capital and overall capital expenditures, including those associated with equipment and intangible assets. The ability to fund these requirements in the future depends on the Company's ability to access additional capital and generate additional cash flow from its operations.

Since inception, the Company has financed its liquidity needs primarily through private placements, the sale of loans and convertible debentures. When possible, the Company tries to optimize its liquidity needs by non-dilutive sources. The capital management objectives listed above have not changed since the previous fiscal year.

The Company is subject to covenants under the 2016 and 2019 Credit Facilities. The Company has complied with those covenants as at December 31, 2019 and 2018. As at December 31, 2019, the tangible net worth for the purpose of the 2016 Credit Facility was $22.9 million (2018: $22.0 million), and the tangible net worth for the purpose of the 2019 Credit Facility was $23.0 million.

15. Revenue by Category

The following table presents an analysis of revenue by category.

	2019 $	2018 $
Interest Revenue	**17,861,394**	13,464,475
Other Fees and Servicing Income		
Other fees	**944,041**	921,615
Servicing fees	**4,516,728**	3,614,111
Amortization of servicing assets	**(3,706,180)**	(2,743,101)
Total other fees and servicing income	**1,754,589**	1,792,625

(in Canadian dollars, except as otherwise noted)

16. Income Tax

Income tax expense (recovery) comprises:

	2019 **$**	2018 $
Current tax expense	**5,694**	-
Deferred tax expense (recovery)	**115,676**	(115,676)
Total income tax (recovery) expense	**121,370**	(115,676)

The tax on the Company's income before income tax differs from the theoretical amount that would arise using the federal and provincial statutory tax rates applicable to income of the consolidated entities. The statutory tax rates for 2019 decreased from 26.7% to 26.6%. This decrease is in line with Quebec's tax rate reduction from 11.7% to 11.6%. The difference between the Company's income tax and theoretical tax is as follows:

	2019	2018
Canadian statutory tax rates	26.6%	26.7%
Statutory income taxes	**$437,485**	$692,742
Non-deductible expenses	**$52,892**	$53,874
Difference in foreign tax rates	**$(29,254)**	$(68,571)
Net change to unrecognized tax assets	**$(339,753)**	$(793,721)
Effective income tax (recovery) expense	**$121,370**	$(115,676)

The adjustment in respect of differences in foreign tax rates includes amounts arising from the differences in taxable income under US jurisdictions in which the Company operates.

(in Canadian dollars, except as otherwise noted)

Recognized Deferred Tax Assets and Liabilities

The following tables presents the composition of recognized deferred income tax assets and liabilities.

					For the Year Ended December 31, 2019
	Opening balance $	**Recognized in net earnings $**	**Recognized in OCI[1] $**	**Recognized in equity $**	**Closing balance $**
Temporary Differences					
Tax credit for salaries and wages	**(34,455)**	**8,980**	**-**	**-**	**(25,475)**
Financing fees	**11,466**	**(3,822)**	**-**	**-**	**7,644**
Fixed assets	**(649)**	**128,279**	**-**	**-**	**127,630**
Unrealized foreign exchange gain	**(115,676)**	**-**	**115,676**	**-**	**-**
Convertible debentures	**(208,389)**	**(150,142)**	**-**	**-**	**(358,531)**
	(347,703)	**(16,705)**	**115,676**	**-**	**(248,732)**
Tax Losses and Credits					
Tax losses	**347,703**	**16,705**	**-**		**364,408**
	-	**-**	**115,676**	**-**	**115,676**

					For the Year Ended December 31, 2018
	Opening balance $	Recognized in net earnings $	Recognized in OCI[1] $	Recognized in equity $	Closing balance $
Temporary Differences					
Tax credit for salaries and wages	(37,607)	3,152	-	-	(34,455)
Financing fees	81,967	(26,402)	-	(44,099)	11,466
Fixed assets	(13,123)	12,474	-	-	(649)
Unrealized foreign exchange gain	-	-	(115,676)	-	(115,676)
Convertible debentures	(208,389)	-	-	-	(208,389)
	(177,152)	(10,776)	(115,676)	(44,099)	(347,703)
Tax Losses and Credits					
Tax losses	177,152	126,452	-	44,099	347,703
	-	115,676	(115,676)	-	-

As at December 31, 2019, no deferred income tax asset has been recognized on approximately $9,401,000 and $9,605,000 of Federal and Provincial tax loss carry forwards, respectively and on approximately $6,766,000 of tax loss carry forwards in the United States (expressed in Canadian dollars). These tax loss carry forwards remain available for use in the future to reduce taxable income, no later than as follows:

	Federal	Provincial	United States
	$	$	$
2027	29,000	29,000	-
2028	-	-	-
2029	-	-	-
2030	195,000	195,000	-
2031	361,000	361,000	-
2032	373,000	373,000	-
2033	243,000	243,000	1,196,000
2034	502,000	502,000	1,579,000
2035	2,551,000	2,551,000	725,000
2036	1,570,000	1,570,000	492,000
2037	1,500,000	1,500,000	2,774,000[1]
2038	1,287,000	1,491,000	-
2039	790,000	790,000	-
Total	9,401,000	9,605,000	6,766,000

[1] Gross tax losses of $2,796,000 for the United States less recognized amount of $22,000.

As at December 31, 2019, the Company had approximately $98,000 of unused Federal tax credits that are not recognized in the consolidated financial statements. Those unused tax credits will expire between 2026 and 2033.

As at December 31, 2019, the Company had other deductible temporary differences of approximately $1,432,000 for the Federal, $1,541,000 for the Provincial and $4,854,000 in the United States (expressed in Canadian dollars) for which no deferred income tax asset is recognized.

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17. Operating Expenses

The following table presents the details of operating expenses for the years ended December 31.

	Note	2019 $	2018 $
Wages and salaries		**5,554,087**	4,728,486
Credit on qualifying wages		**(96,132)**	(130,020)
Stock-based compensation		**287,986**	166,277
Consulting fees		**-**	66,023
Depreciation of right-of-use assets	**8**	**191,349**	-
Rental liability interest expense	**8**	**64,221**	-
Rental expense		**136,353**	320,521
Insurance		**125,684**	128,380
Amortization of transaction costs – financing credit facilities	**10**	**461,373**	568,412
Bank charges		**252,651**	142,373
Professional fees		**177,894**	146,574
Legal and accounting fees		**1,160,791**	1,192,586
Business fees and licences		**142,884**	73,402
Travel and entertainment		**182,583**	169,005
Telecommunications		**62,478**	69,476
Data services and IT costs		**976,580**	380,540
Filing fees		**-**	16,384
Advertising and promotion		**394,628**	237,231
Depreciation and amortization		**157,042**	137,562
Other		**172,899**	122,475
Non-recurring gain on revaluation of Debentures	**11**	**(485,579)**	-
Total Operating Expenses		**9,919,772**	8,535,687

(in Canadian dollars, except as otherwise noted)

18. Supplemental Cash Flow Information

Non-cash items included in net earnings comprise the following:

	Note	2019 $	2018 $
Depreciation of equipment and leasehold improvements	6	**73,443**	68,387
Amortization of intangible assets	7	**83,599**	69,175
Amortization of servicing asset		**3,706,180**	2,743,101
Amortization of right-of-use asset		**191,349**	-
Stock-based compensation		**287,986**	166,277
Interest revenue		**(17,861,394)**	(13,464,475)
Net gain recognized on sale of loans		**(3,650,733)**	(3,910,949)
Income tax expense (recovery)		**121,370**	(115,676)
Amortization of transaction costs – financing credit facility		**461,373**	568,412
Revaluation of convertible debentures	11	**(594,607)**	-
		(17,181,434)	(13,875,748)

Change in non-cash working capital items comprises the following:

	2019 $	2018 $
Sales taxes receivable	**3,468**	1,010
Commercial loans receivable	**(115,237,057)**	(93,333,418)
Other receivables	**27,600**	34,947
Prepaid and deposits	**44,400**	24,825
Accounts payable and accrued liabilities	**206,120**	684,575
	(114,955,469)	(92,588,061)

(in Canadian dollars, except as otherwise noted)

19. Related Party Transactions

Transactions in the Normal Course of Operations

The Company had the following transactions with related parties in the normal course of its operations:

i) The CEO and director of IOUF Canada is a shareholder in a company that owns a significant stake in Palos Capital Corporation ("Palos"), the parent company of Palos Management Inc. No servicing fees have been earned by the Company on outstanding servicing portfolio balances of loans that had previously been sold to Palos (2018: $12,453). Palos also received no agency fees during the year (2018: $973) relating to the outstanding servicing portfolio balance related to a third-party purchaser.

ii) The Company rents its Canadian office space from Palos. The lease may be cancelled after October 2021 upon the payment of a termination fee. The terms of this operating lease are similar to those that would have been present for an arm's-length transaction. The amount of $122,018 is expensed as rental expense for the period (2018: rent expense of $200,925). That amount does not include the amortization of right-of-use assets and the interest on the lease liabilities. Future non-cancellable lease liabilities under this agreement amount to $853,193.

Key Management Compensation

Key management includes directors (executive and non-executive), the Chief Operating Officer and the Chief Financial Officer who is also the Company Secretary. The compensation paid or payable to key management for employee services is shown below:

	2019	2018
	$	$
Salaries and other short-term employee benefits	**885,529**	771,082
Stock-based payments	**169,496**	107,400
	1,055,025	878,482

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20. Segment Information

The Company determines its reportable operating segments according to the manner in which the information is used by the chief operating decision-maker and has determined that the Company operates in one reportable operating segment with two main activities: lending and servicing. Those activities have been identified on the basis of services provided.

The Company's lending activity originates and retains loans as part of its commercial loans receivable portfolio. The Company's servicing activity services commercial loans that have been sold to third party purchasers on a non-recourse basis in exchange for a servicing fee.

Substantially all of the Company's assets are located in the United States.

Revenues by activity are as follows:

	2019			2018		
	Lending $	**Servicing $**	**Total $**	Lending $	Servicing $	Total $
Revenue						
Interest revenue	**17,861,394**	**-**	**17,861,394**	13,464,475	-	13,464,475
Other fees	**944,041**	**-**	**944,041**	921,615	-	921,615
Servicing fees	**-**	**4,516,728**	**4,516,728**	-	3,614,111	3,614,111
Accelerated recognition of transaction costs on loans sold	**-**	**377,091**	**377,091**	-	444,065	444,065
Amortization of servicing asset	**-**	**(3,706,180)**	**(3,706,180)**	-	(2,743,101)	(2,743,101)
Gain on sale of loans	**-**	**3,273,642**	**3,273,642**	-	3,466,884	3,466,884
Gross Revenue	**18,805,435**	**4,461,281**	**23,266,716**	14,386,090	4,781,959	19,168,049

21. Events after the reporting date

a) As part of the NCIB (Note 13) after December 31,2019 and before April 29, 2020, the Company repurchased and cancelled 279,000 common shares in the market for a total cost of $54,565 including $744 of transaction costs.

b) The Company's principal balance of its loan and servicing portfolios is diversified both across industry type and location within North America, mostly in the United States. Due to the Covid-19 pandemic, the Company has modified its underwriting standards to cease lending to industries and geographical areas which are strongly impacted by Covid-19. The Company continues to originate loans and support businesses deemed essential by various governments.

The duration of the current situation with the pandemic is unknown and considering the uncertainty faced by the North American economy over the coming months, the Company retracted in March 2020 its previously disclosed long-term outlook for loan origination growth of 25% to 30%. However, the Company also sees potential for a greater than expected need for small business loans as significant working capital will be required once the situation normalizes. Furthermore, the Company is working closely with various government agencies to assist some of its clients who may encounter hardships as a result of the Covid-19 pandemic. In an effort to help the Company's clients, in late March 2020, management began the process of effecting modified payment plans for clients manifesting bona fide hardships directly attributable to the impacts of the Covid-19 pandemic. The nature and duration of the modified plans varied according to the degree of hardship experienced by each client. As a result of the disruption caused by the Covid-19 pandemic and of entering into these modified plans, IOU Financial exceeded the concentration limits set forth in the financing credit facilities creating over advances on March 27, 2020 and on April 1, 2020 for the 2019 Credit Facility and the 2016 Credit Facility, respectively. As a result of the concentration limits breach, the 2016 Credit Facility is charging additional default interest of 3% for a total interest rate of LIBOR plus 8.5% effective April 1, 2020.

Due to the uncertainty surrounding the current situation, the Company furloughed approximately 40% of its full-time employees and implemented a temporary 20% reduction in salary for all remaining employees commencing on April 1, 2020. IOU Financial also announced, in April 2020, that more than two-thirds of the value of the Company's convertible debenture holders have agreed to defer the payment of interest from the April 30, 2020 payment period to the June 30, 2020 payment period ("reprieve period") and capitalizing the accrued interest over the reprieve period to the principal amount of the debentures at the end of the reprieve period, in accordance to the terms of the trust indenture under which such debentures were issued.

While the current unprecedented economic situation due to the pandemic remains uncertain, the Company is prepared to react quickly as the situation may require and looks forward to emerging as a stronger business coming out of this downturn.

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