Interim Condensed Consolidated Financial Statements of

# MEDICAL FACILITIES CORPORATION

For the three months ended March 31, 2020
(Unaudited)
(In U.S. dollars)

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# MEDICAL FACILITIES CORPORATION

Interim Condensed Consolidated Balance Sheets
(In thousands of U.S. dollars)

| | Note | March 31, 2020 $ (Unaudited) | December 31, 2019 $ |
|---|---|---|---|
| **ASSETS** | | | |
| **Current assets** | | | |
| Cash and cash equivalents | | 39,438 | 31,986 |
| Accounts receivable | | 59,732 | 66,454 |
| Supply inventory | | 8,318 | 7,456 |
| Prepaid expenses and other | | 7,707 | 7,060 |
| Income tax receivable | | 5,506 | 450 |
| Assets held for sale | 5.1 | 25,052 | 43,420 |
| **Total current assets** | | **145,753** | **156,826** |
| **Non-current assets** | | | |
| Loan receivable | 12.1 | 8,875 | - |
| Deferred income tax assets | | 115 | 143 |
| Property and equipment | | 81,374 | 81,310 |
| Right-of-use assets | | 63,793 | 64,373 |
| Goodwill | | 135,983 | 135,983 |
| Other intangibles | | 28,328 | 30,349 |
| Other assets | 12.1 | 2,521 | 1,563 |
| **Total non-current assets** | | **320,989** | **313,721** |
| **TOTAL ASSETS** | | **466,742** | **470,547** |
| **LIABILITIES AND EQUITY** | | | |
| **Current liabilities** | | | |
| Dividends payable | | 1,548 | 1,118 |
| Accounts payable | | 22,579 | 23,601 |
| Accrued liabilities | | 17,352 | 17,768 |
| Income tax payable | | 2,415 | 2,212 |
| Current portion of long-term debt | | 24,399 | 18,062 |
| Current portion of lease liabilities | | 14,395 | 15,400 |
| Liabilities directly associated with assets held for sale | 5 | - | 7,121 |
| **Total current liabilities** | | **82,688** | **85,282** |
| **Non-current liabilities** | | | |
| Long-term debt | | 47,244 | 48,523 |
| Lease liabilities | | 52,906 | 51,981 |
| Deferred income tax liability | | 7,286 | 4,611 |
| Corporate credit facility | | 84,800 | 84,800 |
| Exchangeable interest liability | | 14,979 | 22,006 |
| **Total non-current liabilities** | | **207,215** | **211,921** |
| **Total liabilities** | | **289,903** | **297,203** |
| **Equity** | | | |
| Share capital | 7 | 398,114 | 398,114 |
| Contributed surplus | | 1,485 | 1,400 |
| Deficit | | (267,421) | (274,466) |
| **Equity attributable to owners of the Corporation** | | 132,178 | 125,048 |
| **Non-controlling interest** | | 44,661 | 48,296 |
| **Total equity** | | **176,839** | **173,344** |
| **TOTAL LIABILITIES AND EQUITY** | | **466,742** | **470,547** |

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

# MEDICAL FACILITIES CORPORATION

Interim Condensed Consolidated Statements of Changes in Equity
(In thousands of U.S. dollars)
(Unaudited)

| | | Attributable to Owners of the Corporation | | | | Non-controlling Interest | Total Equity |
|---|---|---|---|---|---|---|---|
| | Note | Share Capital $ | Contributed Surplus $ | Retained Earnings/ (Deficit) $ | Total $ | $ | $ |
| **2020** | | | | | | | |
| Balance at January 1, 2020 | | 398,114 | 1,400 | (274,466) | 125,048 | 48,296 | 173,344 |
| Net income and comprehensive income for the period | | - | - | 8,593 | 8,593 | 4,182 | 12,775 |
| Share-based compensation | 14.1 | - | 85 | - | 85 | - | 85 |
| Dividends to owners of the Corporation | | - | - | (1,548) | (1,548) | - | (1,548) |
| Distributions to non-controlling interest | | - | - | - | - | (6,675) | (6,675) |
| Redemption of non-controlling interest in City Place Surgery Center | | - | - | - | - | (111) | (111) |
| Sale of controlling interest in Unity Medical and Surgical Hospital | 5.1 | - | - | - | - | (1,031) | (1,031) |
| **Balance at March 31, 2020** | | **398,114** | **1,485** | **(267,421)** | **132,178** | **44,661** | **176,839** |
| **2019** | | | | | | | |
| Balance at January 1, 2019 | | 397,639 | 934 | (261,189) | 137,384 | 58,254 | 195,638 |
| Net income (loss) and comprehensive income (loss) for the period | | - | - | (10,285) | (10,285) | 5,002 | (5,283) |
| Share-based compensation | 14.1 | - | 94 | - | 94 | - | 94 |
| Dividends to owners of the Corporation | | - | - | (6,609) | (6,609) | - | (6,609) |
| Distributions to non-controlling interest | | - | - | - | - | (7,448) | (7,448) |
| Acquisition of additional interest in Unity Medical and Surgical Hospital | | - | - | - | - | (154) | (154) |
| Investment in Black Hills Surgical Hospital, LLP by non-controlling interest | | - | - | - | - | 305 | 305 |
| **Balance at March 31, 2019** | | **397,639** | **1,028** | **(278,083)** | **120,584** | **55,959** | **176,543** |

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

# MEDICAL FACILITIES CORPORATION

Interim Condensed Consolidated Statements of Income (Loss) and Comprehensive Income (Loss)
(In thousands of U.S. dollars, except per share amounts)
(Unaudited)

| | | Three Months Ended March 31, | |
|---|---|---|---|
| | Note | 2020<br>$ | 2019<br>$ |
| **Facility service revenue** | | **92,762** | **93,383** |
| **Operating expenses** | | | |
| Salaries and benefits | | 28,587 | 28,088 |
| Drugs and supplies | | 30,415 | 30,141 |
| General and administrative expenses | | 15,652 | 14,437 |
| Depreciation of property and equipment | | 2,483 | 3,133 |
| Depreciation of right-of-use assets | | 2,569 | 1,898 |
| Amortization of other intangibles | | 2,021 | 2,847 |
| | | **81,727** | **80,544** |
| **Income from operations** | | **11,035** | **12,839** |
| **Finance costs (income)** | | | |
| Change in value of convertible debentures | | - | 1,012 |
| Change in value of exchangeable interest liability | | (7,027) | 12,793 |
| Interest expense on exchangeable interest liability | | 1,907 | 1,940 |
| Interest expense, net of interest income | 11 | 1,436 | 1,949 |
| Loss (gain) on foreign currency | | 34 | (234) |
| | | **(3,650)** | **17,460** |
| Share of equity income (loss) in associates | 12.1 | (458) | 1 |
| **Income (loss) before income taxes** | | **14,227** | **(4,620)** |
| Income tax recovery | 10 | (380) | (1,945) |
| **Net income (loss) for the period from continuing operations** | | **14,607** | **(2,675)** |
| **Discontinued operations** | | | |
| Net loss for the period from discontinued operations, net of tax | 5.2 | (1,832) | (2,608) |
| **Net income (loss) and comprehensive income (loss) for the period** | | **12,775** | **(5,283)** |
| **Attributable to:** | | | |
| Owners of the Corporation | | 8,593 | (10,285) |
| Non-controlling interest | | 4,182 | 5,002 |
| | | **12,775** | **(5,283)** |
| **Earnings (loss) per share** | | | |
| From continuing and discontinued operations | | | |
| Basic | 6 | $ 0.28 | $ (0.33) |
| Fully diluted | 6 | $ 0.13 | $ (0.33) |
| From continuing operations | | | |
| Basic | 6 | $ 0.30 | $ (0.26) |
| Fully diluted | 6 | $ 0.16 | $ (0.26) |

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

# MEDICAL FACILITIES CORPORATION

Interim Condensed Consolidated Statements of Cash Flows
(In thousands of U.S. dollars)
(Unaudited)

| | Note | Three Months Ended March 31, 2020 $ | 2019 $ |
|---|---|---|---|
| **Cash flows from operating activities** | | | |
| Net income (loss) for the period | | 12,775 | (5,283) |
| Adjustments for: | | | |
| Depreciation of property and equipment | | 2,483 | 3,472 |
| Depreciation of right-of-use assets | | 2,569 | 1,976 |
| Amortization of other intangibles | | 2,021 | 3,701 |
| Share of equity loss (income) in associates | 12.1 | 458 | (1) |
| Change in value of convertible debentures | | - | 1,012 |
| Change in value of exchangeable interest liability | | (7,027) | 12,793 |
| Loss (gain) on foreign currency | | 34 | (234) |
| Income tax recovery | | (2,118) | (2,754) |
| Share-based compensation | 14.1 | 85 | 94 |
| Interest expense, net of interest income | | 4,099 | 4,665 |
| Other non-cash loss (gain) | | 238 | (949) |
| | | 15,617 | 18,492 |
| Changes in non-cash operating working capital | 8 | 3,392 | 4,797 |
| | | 19,009 | 23,289 |
| Interest paid, net of received | | (3,317) | (3,244) |
| Income and withholding taxes received | | 23 | 582 |
| **Net cash provided by operating activities** | | **15,715** | **20,627** |
| **Cash flows from investing activities** | | | |
| Purchase of property and equipment | | (2,548) | (3,285) |
| Redemption of non-controlling interest in City Place Surgery Center | | (111) | - |
| Proceeds from sale of controlling interest in Unity Medical and Surgical Hospital | | 1,100 | - |
| Investment in Unity Medical and Surgical Hospital subsequent to sale | | (793) | - |
| Acquisition of additional interest in Unity Medical and Surgical Hospital | | - | (154) |
| Investment in Black Hills Surgical Hospital, LLP by non-controlling interest | | - | 305 |
| Investment in short-term bank investments | | - | (289) |
| **Net cash used in investing activities** | | **(2,352)** | **(3,423)** |
| **Cash flows from financing activities** | | | |
| Net proceeds from (repayments of) revolving credit facilities and issuance of notes payable | | 7,461 | (11) |
| Repayments of notes payable at the Facilities | | (2,403) | (1,290) |
| Payments of lease liabilities | | (3,142) | (2,861) |
| Distributions to non-controlling interest | | (6,675) | (7,448) |
| Dividends paid | | (1,118) | (6,562) |
| **Net cash used in financing activities** | | **(5,877)** | **(18,172)** |
| **Increase (decrease) in cash and cash equivalents** | | **7,486** | **(968)** |
| Effect of exchange rate fluctuations on cash balances held | | (34) | 234 |
| Cash and cash equivalents, beginning of the period | | 31,986 | 36,686 |
| **Cash and cash equivalents, end of the period** | | **39,438** | **35,952** |

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

## 1. REPORTING ENTITY

Medical Facilities Corporation (the “Corporation”) is a British Columbia corporation. The address of the Corporation’s head office is 4576 Yonge Street, Suite 701, Toronto, Ontario, Canada. The common shares of the Corporation are listed on the Toronto Stock Exchange under the ticker symbol “DR”.

The Corporation’s operations are based in the United States. Through its wholly-owned subsidiaries, the Corporation owns controlling interests in four specialty hospitals and seven ambulatory surgery centers (the “Facilities”). The Corporation also owns a 92% controlling interest in RRI Mishawaka Hospital, LP, an entity which owns the land and building for Unity Medical and Surgical Hospital (“UMASH”). As described below, an agreement has been entered into for the sale of UMASH property.

On February 24, 2020, the Corporation sold the majority of its interest (decreasing to 31.7% from 87.6%) in UMASH to a group of local investors (the “Buyers”), including leading physicians affiliated with South Bend Orthopedics, The South Bend Clinic, and Allied Physicians of Michiana. As of the date of the transaction, the Corporation does not consolidate the financial results of UMASH and accounts for its interest under the equity method of accounting.

In connection with this transaction, the Corporation also announced the agreement for the sale of the real estate assets underlying UMASH, consisting of land and building, for approximately $25,000 in cash consideration, subject to adjustments for confirmatory due diligence and closing costs, to investors affiliated with the Buyers. The sale of the real estate assets is expected to close during the second quarter of 2020.

The Corporation received $1,100 in cash consideration for its equity interests, subject to customary adjustments. In connection with the transaction, UMASH’s debt obligation to the Corporation was reduced by $3,000, with the remaining $20,000 being structured on a five-year term at an interest rate of 6.75%, adjusted annually, secured by the Buyers’ equity in UMASH. The Buyers have options to acquire more of the Corporation’s equity interest in UMASH on both the first and second anniversaries of the transaction closing for the greater of the current per share purchase price or the fair market value of the interest at the time the purchase option is exercised. In the event that the Corporation’s ownership in UMASH falls below 25%, all of the UMASH debt owed to the Corporation would be required to be immediately repaid. The parties have made capital contributions to fund working capital post-closing; the Corporation’s total obligation is approximately $1,400, of which $793 has been funded.

In connection with this transaction, the Corporation recorded a gain on sale of $11,164, which was offset by an impairment loss reserved on the loan receivable from UMASH (note 5). The Corporation also incurred transaction costs of $450 which are included in general and administrative expenses from continuing operations.

(In thousands of U.S. dollars, except per share amounts and where otherwise indicated)

## 1. REPORTING ENTITY (Continued)

The Corporation's ownership interest in, and the location of, its operating subsidiaries are as follows:

| | | Ownership Interest March 31, | |
|---|---|---|---|
| **Subsidiary** | **Location** | **2020** | **2019** |
| Arkansas Surgical Hospital, LLC ("ASH") | North Little Rock, Arkansas | 51.0% | 51.0% |
| Oklahoma Spine Hospital, LLC ("OSH") | Oklahoma City, Oklahoma | 64.0% | 62.8% |
| Black Hills Surgical Hospital, LLP ("BHSH") | Rapid City, South Dakota | 54.2% | 54.2% |
| Sioux Falls Specialty Hospital, LLP ("SFSH") | Sioux Falls, South Dakota | 51.0% | 51.0% |
| The Surgery Center of Newport Coast ("SCNC") | Newport Beach, California | 51.0% | 51.0% |
| MFC Nueterra ASCs(1) | Various | 46.4% | 48.2% |

*(1) The Corporation has an average ownership interest of 46.4% based on values as at the reporting date. The six ambulatory surgery centers are situated in Michigan, Missouri, Nebraska, Ohio, Oregon and Pennsylvania.*

## 2. STATEMENT OF COMPLIANCE

These unaudited interim condensed consolidated financial statements ("consolidated financial statements") have been prepared in accordance with International Accounting Standard IAS 34 *Interim Financial Reporting* as issued by the International Accounting Standards Board ("IASB") using the accounting policies as described in the audited consolidated financial statements for the year ended December 31, 2019 ("annual financial statements") and presented in note 15 to these consolidated financial statements.

These consolidated financial statements were approved for issue by the Corporation's Board of Directors on May 13, 2020.

## 3. BASIS OF PREPARATION

These consolidated financial statements do not contain all of the disclosures that are required in annual financial statements prepared under International Financial Reporting Standards ("IFRS") and should be read in conjunction with the Corporation's annual financial statements, which include information necessary or useful to understand the Corporation's business and financial statement presentation.

Income from operations for the interim period is not necessarily indicative of the results for the full year. Facility service revenue and certain directly related expenses are subject to seasonal fluctuations due to the timing of case scheduling, which can be impacted by the vacation schedules of surgeons, as well as the extent to which patients have remaining deductibles on their insurance coverage, based on the time of year. Occupancy related expenses, certain operating expenses, depreciation and amortization, and interest expense remain relatively steady throughout the year.

The Corporation's consolidated financial statements are reported in U.S. dollars which is its functional and presentation currency. All financial information presented in U.S. dollars has been rounded to the nearest thousand, unless otherwise indicated.

## 4. COVID-19

On March 11, 2020, the World Health Organization designated COVID-19 as a global pandemic. The outbreak began to impact the Corporation's and Facilities' operations in the latter half of March 2020. All Facilities were impacted by the pandemic as elective cases were restricted, either voluntarily or by government mandate, including the temporary closure of three of the MFC Nueterra ASCs. Management expects the patient volumes and revenues to be negatively impacted until the effects of the pandemic begin to subside and the economy begins to stabilize.

Management believes the extent of the COVID-19 pandemic's adverse impact on the Corporation's operating results and financial condition will be driven by many factors, most of which are beyond management's control and ability to forecast. Such factors include, but are not limited to, the scope and duration of stay-at-home policies and business closures, continued decreases in patient volumes for an indeterminable length of time, increases in the number of uninsured and underinsured patients as a result of higher unemployment, incremental expenses required for supplies and personal protective equipment, and changes in professional and general liability exposure. Because of these and other uncertainties, management cannot estimate the length or severity of the impact of the pandemic on the business. Decreases in cash flows and results of operations may have an impact on the inputs and assumptions used in significant accounting estimates, including management's assessment of future compliance with financial covenants, estimated implicit price concessions related to uninsured patient accounts, professional and general liability reserves, and potential impairments of goodwill and long-lived assets.

The Coronavirus Aid, Relief, and Economic Security (CARES) Act (the "Act") was signed into law on March 27, 2020. The Act includes provisions for financial assistance to hospitals, surgery centers and health care providers via, among other provisions, the Public Health and Social Services Emergency Fund ("PHSSEF"), the Paycheck Protection Program ("PPP") and expansion of an existing Centers for Medicare and Medicaid Services accelerated payment program.

The PHSSEF is administered by the Department of Health and Human Services ("HHS") to provide eligible healthcare providers with relief funds to cover non-reimbursable expenses, including forgone revenue, attributable to COVID-19. The Facilities received $7,732 in funding from the HHS through May 13, 2020 and may be eligible for further funding. Funds not utilized for eligible expenses must be returned.

The PPP expands the guaranteed lending program under Section 7(a) of the Small Business Act administered by the US Small Business Administration ("SBA"). Under the PPP, the Facilities have received $11,940 through May 13, 2020. The loan amounts received are eligible for forgiveness to the extent they are used for certain qualifying expenses and to maintain payroll levels and related expenses during the eight-week period following loan origination.

Under the expansion of the Medicare Accelerated and Advance Payment Program most providers and suppliers can request an advance of three to six months of Medicare payments. Repayment of these accelerated/advance payments begins 120 days after issuance and will be offset against future Medicare claims. Certain Facilities have received advances of $24,464 through May 13, 2020.

(In thousands of U.S. dollars, except per share amounts and where otherwise indicated)

## 5. DISCONTINUED OPERATIONS

### 5.1 Sale of UMASH

On February 24, 2020, the Corporation sold the majority of its interest in UMASH for cash proceeds of $1,100 and estimated receivable for working capital adjustments of $272. The net assets sold were as follows:

| | $ |
|---|---|
| Cash and cash equivalents | 643 |
| Accounts receivable | 3,252 |
| Supply inventory | 648 |
| Prepaid expenses and other | 1,772 |
| Deferred income tax assets | 3,160 |
| Property and equipment | 1,383 |
| Right-of-use assets | 670 |
| Other intangibles | 5,776 |
| **Total assets** | **17,304** |
| Accounts payable | 1,965 |
| Accrued liabilities | 2,293 |
| Lease liabilities | 1,445 |
| **Total liabilities** | **5,703** |
| **Net assets sold** | **11,601** |

The gain on sale was calculated as follows:

| | $ |
|---|---|
| Cash proceeds received | 1,100 |
| Working capital adjustments | 272 |
| Loan receivable from UMASH | 8,875 |
| Equity investment retained in UMASH | 623 |
| Non-controlling interest of UMASH | 1,031 |
| Less: Escrow reserve | (300) |
| Less: Net assets sold | (11,601) |
| **Total gain on sale of UMASH, net of tax** | **-** |

The Corporation expects to close the sale of the real estate assets underlying UMASH during the second quarter of 2020. As at March 31, 2020, the real estate assets of $25,052 have been classified as held for sale.

(In thousands of U.S. dollars, except per share amounts and where otherwise indicated)

## 5. DISCONTINUED OPERATIONS (Continued)

### 5.2 Results of discontinued operations

| | Three Months Ended March 31, | |
|---|---|---|
| | **2020** | **2019** |
| | **$** | **$** |
| **Facility service revenue** | **3,079** | **5,712** |
| **Operating expenses** | | |
| Salaries and benefits | 1,707 | 3,229 |
| Drugs and supplies | 1,115 | 1,826 |
| General and administrative expenses | 1,592 | 2,027 |
| Depreciation of property and equipment | - | 339 |
| Depreciation of right-of-use assets | - | 78 |
| Amortization of other intangibles | - | 854 |
| | **4,414** | **8,353** |
| **Loss from operations** | **(1,335)** | **(2,641)** |
| Interest expense, net of interest income | 756 | 776 |
| **Loss before income taxes** | **(2,091)** | **(3,417)** |
| Income tax recovery | (259) | (809) |
| **Net loss for the period from discontinued operations, net of tax** | **(1,832)** | **(2,608)** |

### 5.3 Cash flows from discontinued operations

| | Three Months Ended March 31, | |
|---|---|---|
| | **2020** | **2019** |
| | **$** | **$** |
| Net cash provided by (used in) operating activities | 334 | (1,482) |
| Net cash provided by (used in) investing activities | 386 | (21) |
| Net cash provided by (used in) financing activities | (338) | 250 |
| **Net cash flow for the period** | **382** | **(1,253)** |

(In thousands of U.S. dollars, except per share amounts and where otherwise indicated)

## 6. EARNINGS (LOSS) PER SHARE

Basic earnings (loss) per share attributable to owners of the Corporation are calculated as follows:

| | | Three Months Ended March 31, | | | | | |
|---|---|---|---|---|---|---|---|
| | | 2020 | | | 2019 | | |
| | | Continuing Operations | Discontinued Operations | Total | Continuing Operations | Discontinued Operations | Total |
| Net income (loss) for the period attributable to owners of the Corporation | $ | 9,423 | (830) | 8,593 | (8,207) | (2,078) | (10,285) |
| Divided by weighted average number of common shares outstanding for the period | | 31,106,259 | 31,106,259 | 31,106,259 | 31,054,500 | 31,054,500 | 31,054,500 |
| **Basic earnings (loss) per share attributable to owners of the Corporation** | **$** | **0.30** | **(0.02)** | **0.28** | **(0.26)** | **(0.07)** | **(0.33)** |

Fully diluted earnings (loss) per share attributable to owners of the Corporation are calculated as follows:

| | | Three Months Ended March 31, | | | | | |
|---|---|---|---|---|---|---|---|
| | | 2020 | | | 2019 | | |
| | | Continuing Operations | Discontinued Operations | Total | Continuing Operations | Discontinued Operations | Total |
| Net income (loss) for the period attributable to owners of the Corporation | $ | 9,423 | (830) | 8,593 | (8,207) | (2,078) | (10,285) |
| Change in value of exchangeable interest liability (tax effected) | | (5,341) | - | (5,341) | - | - | - |
| Interest expense on exchangeable interest liability | | 1,907 | - | 1,907 | - | - | - |
| Modified net income (loss) for the period attributable to owners of the Corporation | $ | 5,989 | (830) | 5,159 | (8,207) | (2,078) | (10,285) |
| Weighted average number of common shares: | | | | | | | |
| Outstanding for the period | | 31,106,259 | 31,106,259 | 31,106,259 | 31,054,500 | 31,054,500 | 31,054,500 |
| Deemed to be issued on the exchange of the outstanding exchangeable interest liability | | 5,995,966 | 5,995,966 | 5,995,966 | - | - | - |
| Weighted average number of common shares [1][2] | | 37,102,225 | 37,102,225 | 37,102,225 | 31,054,500 | 31,054,500 | 31,054,500 |
| **Fully diluted earnings (loss) per share** | **$** | **0.16** | **(0.03)** | **0.13** | **(0.26)** | **(0.07)** | **(0.33)** |

*[1] For the three months ended March 31, 2020, the impact of convertible debentures was excluded from the dilutive weighted average number of common shares calculation because convertible debentures were repaid. The impact of share-based compensation was excluded from the dilutive weighted average number of common shares calculation because it was not applicable based on the share price prevailing at March 31, 2020.*

*[2] For the three months ended March 31, 2019, the impacts of exchangeable interest liability, convertible debentures, and share-based compensation were excluded from the dilutive weighted average number of common shares calculation because they were not applicable based on the share price prevailing at March 31, 2019.*

(In thousands of U.S. dollars, except per share amounts and where otherwise indicated)

## 7. NORMAL COURSE ISSUER BIDS

The Corporation's current normal course issuer bid for up to 621,144 of its common shares, is in effect from May 16, 2019 to May 15, 2020. During the three month periods ended March 31, 2020 and March 31, 2019, the Corporation did not purchase any of its common shares.

## 8. NET CHANGES IN NON-CASH WORKING CAPITAL

The net changes in non-cash working capital included in the interim condensed consolidated statements of cash flows consist of the following:

| | **Three Months Ended March 31,** | |
|---|---|---|
| | **2020**<br>**$** | **2019**<br>**$** |
| Accounts receivable | 6,722 | 6,037 |
| Supply inventory | (862) | (423) |
| Prepaid expenses and other | (924) | 378 |
| Accounts payable | (1,022) | (2,598) |
| Accrued liabilities | (522) | 1,403 |
| **Net changes in non-cash working capital** | **3,392** | **4,797** |

(In thousands of U.S. dollars, except per share amounts and where otherwise indicated)

## 9. FINANCIAL INSTRUMENTS

### 9.1 Fair values and classification of financial instruments

The fair value of exchangeable interest liability is determined based on the closing trading price of common shares at each reporting period. The fair values of notes payable and revolving credit facilities at the Facilities' level approximate their book values as the interest rates are similar to prevailing market rates. The fair values of all other financial instruments of the Corporation, due to the short-term nature of these instruments, approximate their book values.

The following table presents the carrying values and classification of the Corporation's financial instruments as at March 31, 2020 and December 31, 2019:

| | March 31, 2020<br>$ | December 31, 2019<br>$ |
|---|---|---|
| **Financial assets** | | |
| Fair value through profit or loss | | |
| Cash and cash equivalents | 39,438 | 31,986 |
| Amortized cost | | |
| Accounts receivable | 59,732 | 66,454 |
| Loan receivable | 8,875 | - |
| **Financial liabilities** | | |
| Fair value through profit or loss | | |
| Exchangeable interest liability | 14,979 | 22,006 |
| Amortized cost | | |
| Dividends payable | 1,548 | 1,118 |
| Accounts payable | 22,579 | 23,601 |
| Accrued liabilities | 17,352 | 17,768 |
| Corporate credit facility | 84,800 | 84,800 |
| Long-term debt | 71,643 | 66,585 |

The financial instruments of the Corporation that are recorded at fair value have been classified into levels using a fair value hierarchy. The following tables represent the fair value hierarchy of the Corporation's financial instruments that were recognized at amortized cost or fair value through profit or loss as of March 31, 2020 and December 31, 2019. It does not include fair value information for financial instruments which are short-term in nature.

(In thousands of U.S. dollars, except per share amounts and where otherwise indicated)

## 9. FINANCIAL INSTRUMENTS (Continued)

| | March 31, 2020 | | | |
|---|---|---|---|---|
| | **Level 1** **$** | **Level 2** **$** | **Level 3** **$** | **Total** **$** |
| **Financial assets** | | | | |
| Cash and cash equivalents | 39,438 | - | - | 39,438 |
| **Financial liabilities** | | | | |
| Exchangeable interest liability | - | 14,979 | - | 14,979 |
| Corporate credit facility | - | 84,800 | - | 84,800 |
| Long-term debt | - | 71,643 | - | 71,643 |
| **Total** | **39,438** | **171,422** | **-** | **210,860** |

| | December 31, 2019 | | | |
|---|---|---|---|---|
| | **Level 1** **$** | **Level 2** **$** | **Level 3** **$** | **Total** **$** |
| **Financial assets** | | | | |
| Cash and cash equivalents | 31,986 | - | - | 31,986 |
| **Financial liabilities** | | | | |
| Exchangeable interest liability | - | 22,006 | - | 22,006 |
| Corporate credit facility | - | 84,800 | - | 84,800 |
| Long-term debt | - | 66,585 | - | 66,585 |
| **Total** | **31,986** | **173,391** | **-** | **205,377** |

## 9.2 Measurement of fair values

The following is the valuation technique used in measuring Level 2 fair values (the Corporation does not have any Level 3 fair values).

| Financial Instrument | Valuation Technique |
|---|---|
| Exchangeable interest liability | *Market comparison technique:* The number of the Corporation's common shares to issue is based on the contractual agreements with the holders of non-controlling interest that have exchange agreements with the Corporation and take into account the distributions to the non-controlling interest over the prior twelve months. The liability is valued based on the market price of the Corporation's common shares converted to the reporting currency as of the reporting date. |
| Corporate credit facility | *Market comparison technique:* Interest rates are based on the lending agreements with various banks of corporate credit facility, and they are prime rates adjusted for the Corporation's risk rating, secured assets and other terms of agreements. The liability is valued based on debt principals. |
| Long-term debt | *Market comparison technique:* Interest rates are based on the lending agreements with various banks and creditors of long-term debt, and they are prime or LIBOR rates adjusted for the Facilities' risk rating, secured assets and other terms of agreements. The liability is valued based on debt principals and interest payments discounted to present value. |

(In thousands of U.S. dollars, except per share amounts and where otherwise indicated)

## 10. INCOME TAXES

The U.S. tax return for the Corporation is prepared on a consolidated basis for U.S. entities and includes balances and amounts attributable to these entities.

The effective tax rate decreased for the three months ended March 31, 2020 compared to the three months ended March 31, 2019 due to a decrease in tax expense resulting primarily from tax rate differential in tax years in which United States losses can be carried back to as allowed under the Act enacted on March 27th, 2020.

The Act provides tax relief with a number of measures. It includes a temporary change to section 172 of the U.S. Internal Revenue Code of 1986, as amended (the "Code") such that non-operating losses ("NOL") can be carried back five years. Based on the expected application of NOL carry backs generated in the 2019 and 2020 tax years, the company has recorded refunds of approximately $5,100 as a result of the change due to the Act.

The anticipated NOL for 2019 and 2020 stems primarily from temporary changes under the Act to two other provisions under the Code. The business interest deduction limit under section 163(j) of the Code is increased from 30% to 50% of a taxpayer's adjusted taxable income for tax years beginning in 2019 and 2020. As a result, the Corporation expects to realize additional interest expense deductions with a current tax impact of approximately $3,900. The other significant change is that the Act clarifies that Qualified Improvement Property ("QIP") is eligible for bonus depreciation (i.e. 100% expensing) under section 168(k) of the Code, for which the Corporation estimates current tax savings of approximately $1,100.

The Canadian income tax return for the Corporation is prepared on a stand-alone basis and includes non-consolidated balances attributable to the Canadian entity only.

Income taxes from continuing operations reported in these consolidated financial statements are as follows:

| | Three Months Ended March 31, | |
|---|---|---|
| **Provision for Income Taxes** | **2020<br>$** | **2019<br>$** |
| Current | (4,448) | 737 |
| Deferred | 4,068 | (2,682) |
| **Total income tax recovery from continuing operations** | **(380)** | **(1,945)** |

(In thousands of U.S. dollars, except per share amounts and where otherwise indicated)

## 11. INTEREST EXPENSE, NET OF INTEREST INCOME

Interest expense, net of interest income, from continuing operations included in the interim condensed consolidated statements of income and comprehensive income consist of the following:

| | Three Months Ended March 31, | |
|---|---|---|
| | **2020** | **2019** |
| | **$** | **$** |
| Interest expense at Facilities' level | 675 | 690 |
| Interest expense on convertible debentures | - | 456 |
| Interest expense at corporate level | 759 | 797 |
| Interest expense on lease liabilities | 759 | 769 |
| Amortization of available credit facility stand-by fees | 168 | 123 |
| Interest income at Facilities' level | (10) | (14) |
| Interest income at corporate level | (915) | (872) |
| **Interest expense, net of interest income, from continuing operations** | **1,436** | **1,949** |

## 12. RELATED PARTY TRANSACTIONS AND BALANCES

### 12.1 Equity accounted investments

The following investments comprise the 'Other assets' on the interim condensed consolidated balance sheets.

| | | March 31, 2020 | | December 31, 2019 | |
|---|---|---|---|---|---|
| **Entity** | **Accounting Method** | **Ownership Interest** | **Investment Balance $** | **Ownership Interest** | **Investment Balance $** |
| Mountain Plains Real Estate Holdings, LLC ("MPREH") | Equity | 54.2% | 737 | 54.2% | 733 |
| South Dakota Interventional Pain Institute, LLC ("SDIPI")[(1)] | Equity | 32.0% | 4 | 32.0% | 4 |
| Black Hills Surgical Physicians, LLC ("BHSP") | Cost | 0.4% | 341 | 0.4% | 341 |
| St. Luke's Surgery Center of Chesterfield, LLC ("St. Luke's ASC") | Equity | 28.0% | 480 | 28.0% | 485 |
| UMASH[(2)(3)] | Equity | 31.7% | 959 | 87.6% | nil |
| | | | 2,521 | | 1,563 |

[(1)] *During the three months ended June 30, 2019, SFSH purchased substantially all of the net assets of SDIPI, including real estate and loans. As of March 31, 2020, SFSH had a balance payable to SDIPI of $1,016 (December 31, 2019: $1,016). The Corporation's ownership interest in SDIPI did not change.*

[(2)] *On February 24, 2020, the Corporation sold the majority of its interest in UMASH, decreasing its interest to 31.7% from 87.6%. The investment balance includes the Corporation's share of losses from February 25, 2020 onwards of $458.*

[(3)] *The Corporation has a loan receivable of $8,875 from UMASH as at March 31, 2020.*

## 12. RELATED PARTY TRANSACTIONS AND BALANCES (Continued)

### 12.2 Related party transactions

A member of the Corporation's Board of Directors is a minority owner of a Facility of the Corporation and a member of an ownership group that owns and leases hospital real estate to the Facility, for which the Facility paid rent for the three months ended March 31, 2020 of $1,155 (March 31, 2019: $1,125).

Certain Facilities routinely enter into transactions with related parties for provision of services relating to the use of facilities and equipment. These parties are considered related as the Facilities have significant influence over these parties. Such transactions are in the normal course of operations and are measured at the exchange amount, which is the amount of consideration established and agreed to by the related parties. For the three months ended March 31, 2020, BHSH paid MPREH $45 for the use of a facility (March 31, 2019: $45).

### 12.3 Other transactions

Certain of the physicians, who indirectly own the non-controlling interest in each of the Facilities, routinely provide professional services directly to patients utilizing the services of the Facilities and reimburse the Facilities for the space and staff utilized. Also, certain of the physicians serve on the boards of management of the Facilities and two such individuals perform the duties of Medical Director at the respective Facilities and are compensated in recognition of their contribution to the Facilities. Also, a physician with a non-controlling interest in SFSH is its Chief Executive Officer and the Chief Medical Officer of the Corporation.

## 13. COMMITMENTS AND CONTINGENCIES

### 13.1 Commitments

In the normal course of operations, the Facilities lease certain equipment under non-cancellable long-term leases and enter into various commitments with third parties. In addition, certain of the Facilities lease their facility space from related and non-related parties. With the adoption of IFRS 16, *Leases* ("IFRS 16"), on January 1, 2019, significant portions of such lease commitments were recognized on the interim condensed consolidated balance sheets.

### 13.2 Contingencies

In the normal course of business, the Facilities are, from time to time, subject to allegations that may result in litigation. Certain allegations may not be covered by the Facilities' commercial and liability insurance. The Facilities evaluate such allegations by conducting investigations to determine the validity of each potential claim. Based on the advice of legal counsel, management records an estimate of the amount of the ultimate expected loss for each of these matters. Events could occur that would cause the estimate of the ultimate loss to differ materially from the amounts recorded.

(In thousands of U.S. dollars, except per share amounts and where otherwise indicated)

## 14. SHARE-BASED COMPENSATION

### 14.1 Stock options

The following table summarizes the outstanding number of stock options as of March 31, 2020:

| Optionee | Number of Options Held | Exercise Price | Grant Date |
|---|---|---|---|
| Chief Executive Officer | 450,000 | C$14.03 | March 29, 2018 |
| | 350,000 | C$16.47 | May 18, 2017 |
| Chief Financial Officer | 300,000 | C$12.79 | June 24, 2019 |
| Chief Development Officer | 350,000 | C$21.15 | September 19, 2016 |
| Chief Operating Officer | 50,000 | C$ 2.64 | March 19, 2020 |
| Former Chief Executive Officer | 223,562 | C$17.24 | May 1, 2016 |
| Former Chief Financial Officer | 221,344 | C$17.98 | November 21, 2016 |
| **Total number of outstanding options** | **1,944,906** | | |

Outstanding options (the “Options”) vest after five years of employment. The Options must be exercised by the tenth anniversary of the respective grant dates, subject to blackout exceptions. As of March 31, 2020, 444,906 of the Options relating to Former Chief Executive Officer and Former Chief Financial Officer are vested.

During the three months ended March 31, 2020, the Corporation recognized $85 (March 31, 2019: $94) relating to the Options in salaries and benefits expense. On March 19, 2020, the Options to acquire 50,000 common shares of the Corporation were granted to its Chief Operating Officer.

The grant date fair values of the Options were measured based on the Black-Scholes model. Expected volatility is estimated by considering historic average share price volatility. The inputs used in the measurement of the fair values at the grant date of the share-based compensation plan are as follows:

| | Q1 2020 Grant Issued | Q2 2019 Grant Issued | Q1 2018 Grant Issued | Q2 2017 Grant Issued | Q4 2016 Grant Issued | Q3 2016 Grant Issued | Q2 2016 Grant Issued |
|---|---|---|---|---|---|---|---|
| **Fair value of Options, grants and assumptions** | | | | | | | |
| Fair value at grant date | C$0.45 | C$ 1.20 | C$ 1.33 | C$ 1.27 | C$ 1.41 | C$ 2.00 | C$ 1.33 |
| Share price at grant date | C$2.64 | C$12.90 | C$14.03 | C$16.68 | C$18.19 | C$21.57 | C$17.01 |
| Exercise price | C$2.64 | C$12.79 | C$14.03 | C$16.47 | C$17.98 | C$21.15 | C$17.24 |
| Expected volatility (weighted average volatility) | 50.70% | 29.77% | 27.76% | 22.77% | 21.77% | 21.95% | 23.60% |
| Option life (expected weighted average life) | 5 years | 5 years | 5 years | 5 years | 5 years | 5 years | 5 years |
| Expected dividends | 10.61% | 8.72% | 8.02% | 6.74% | 6.18% | 5.22% | 6.61% |
| Risk-free rate | 0.68% | 1.34% | 1.96% | 0.99% | 0.99% | 0.73% | 1.03% |

(In thousands of U.S. dollars, except per share amounts and where otherwise indicated)

## 14. SHARE-BASED COMPENSATION (Continued)

### 14.2 Deferred share units

Compensation for directors includes a deferred share unit ("DSU") component, for which grants based on the value of the Corporation's common shares are made quarterly. The DSUs accrue dividends, vest immediately and can be redeemed only when a participant ceases to serve as a director of the Corporation. The participant's entitlement in respect of the DSUs then held will be settled in cash based on a formula tied to the value of the Corporation's common shares at the relevant time. For the three months ended March 31, 2020, director compensation included DSU grants of $117 (March 31, 2019: $140), while the change in market value of outstanding DSUs for the same period was a recovery of $230 (March 31, 2019: expense of $310).

The following table summarizes changes in the DSUs for three months ended March 31, 2020:

| | **2020** |
|---|---|
| Opening balance of DSUs at January 1, 2020 | 199,574 |
| DSUs granted on director fees | 46,771 |
| DSUs granted on dividend reinvestment | 1,986 |
| **Total number of DSUs at March 31, 2020** | **248,331** |

### 14.3 Restricted share units

Compensation for executive officers of the Corporation includes a restricted share unit ("RSU") component, for which grants based on the value of the Corporation's common shares were initially made annually up to 2018 and then from time to time. Effective 2018, annual RSU grants were replaced by annual performance share unit ("PSU") grants. The RSU grants vest over three years, participate in the Corporation's quarterly dividends, and settle in cash. To date, grants were made on November 21, 2016 for 14,920 RSUs, July 1, 2017 for 21,804 RSUs, and on May 10, 2018 for 17,040 RSUs. The value of the expense and liability associated with the RSUs is determined based on the Corporation's share price at the end of each reporting period. For the three months ended March 31, 2020, operating expenses included an RSU recovery of $12 (March 31, 2019: expense of $86). As at March 31, 2020, the liability for RSUs was $43.

The following table summarizes changes in the RSUs for the three months ended March 31, 2020:

| | **2020** |
|---|---|
| Opening balance of RSUs at January 1, 2020 | 24,921 |
| RSUs granted on dividend reinvestment | 248 |
| **Total number of RSUs at March 31, 2020** | **25,169** |

(In thousands of U.S. dollars, except per share amounts and where otherwise indicated)

## 14. SHARE-BASED COMPENSATION (Continued)

### 14.4 Performance Share Unit Plan

Until 2020, annual grants of PSUs were awarded under the Corporation's Performance Share Unit Plan ("PSU Plan"). In March 2020, the Board amended the PSU Plan to allow grants of share units ("SUs") in the form of PSUs or deferred share units ("Executive DSUs"). Starting with the 2020 annual grant, awards under the PSU Plan will be granted in the form of Executive DSUs until plan participants' minimum share ownership requirements have been met. Plan participants can elect to receive PSUs once they have achieved their minimum share ownership requirements.

Awards under the PSU Plan vest three years following their grant date, subject to achievement of performance objectives set at the time of the grant. The PSUs are settled in cash on vesting while Executive DSUs are settled in cash upon a plan participant's separation from the Corporation. The units granted under the PSU Plan participate in the Corporation's quarterly dividend.

#### 14.4.1 Performance share units

To date, PSU grants were made on March 29, 2018 for 59,003 PSUs, and on March 29, 2019 for 51,077 PSUs. The value of the expense and liability associated with the PSUs is determined based on the Corporation's share price at the end of each reporting period. For the three months ended March 31, 2020, operating expenses included a PSU recovery of $33 (March 31, 2019: expense of $56). As at March 31, 2020, the liability for PSUs was $66.

The following table summarizes changes in the PSUs for the three months ended March 31, 2020:

| | **2020** |
|---|---|
| Opening balance of PSUs at January 1, 2020 | 70,962 |
| PSUs granted on dividend reinvestment | 706 |
| **Total number of PSUs at March 31, 2020** | **71,668** |

#### 14.4.2 Share units

The first grant of SUs was made on March 31, 2020 for 346,638 Executive DSUs. The value of the expense and liability associated with the SUs is determined based on the Corporation's share price at the end of each reporting period. For the three months ended March 31, 2020, operating expenses included an SU expense of $nil (March 31, 2019: $nil). As at March 31, 2020, the liability for SUs was $nil.

The following table summarizes changes in the SUs for the three months ended March 31, 2020:

| | **2020** |
|---|---|
| Opening balance of SUs at January 1, 2020 | - |
| SUs granted | 346,638 |
| **Total number of SUs at March 31, 2020** | **346,638** |

## 15. SIGNIFICANT ACCOUNTING POLICIES

The accounting policies set out below have been applied consistently to all periods presented in these consolidated financial statements and have been applied consistently by the Facilities.

### 15.1 Basis of measurement

These consolidated financial statements have been prepared on the historical cost basis except for certain financial instruments, which are measured at fair value.

### 15.2 Functional and presentation currency

The Corporation translates monetary assets and liabilities denominated in Canadian dollars, principally its convertible debentures, exchangeable interest liability and certain of its cash balances, which are all denominated in Canadian dollars, at exchange rates in effect at the reporting date. Non-monetary items are translated at rates of exchange in effect when the assets were acquired or obligations were incurred. Revenue and expenses are translated at rates in effect at the time of the transactions. Foreign exchange gains and losses, including translation adjustments, are included in the determination of net income and comprehensive income.

### 15.3 Basis of consolidation

Subsidiaries are entities controlled by the Corporation. Control exists when the Corporation (a) has the power over the entity, (b) is exposed, or has rights, to variable returns from its involvement with the entity, and (c) has the ability to use its power to affect its returns. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences, until the date that control ceases. Non-controlling interest represents the portion of a subsidiary's net earnings and net assets that are attributable to shares of such subsidiary not held by the Corporation.

The non-controlling interest in the equity of the Corporation's subsidiaries is included as a separate component of equity.

All intra-company balances and transactions have been eliminated in preparing these consolidated financial statements. The accounting policies of subsidiaries have been changed when necessary to align them with the policies adopted by the Corporation.

### 15.4 Business combinations

Business combinations are accounted for using the acquisition method as of the date when control is transferred to the Corporation. The Corporation measures goodwill as the excess of the sum of the fair value of the consideration transferred over the net identifiable assets acquired and liabilities assumed, all measured as at the acquisition date. Transaction costs that the Corporation incurs in connection with a business combination, other than those associated with the issue of debt or equity securities, are expensed as incurred.

## 15. SIGNIFICANT ACCOUNTING POLICIES (Continued)

Any contingent consideration is measured at fair value at the date of acquisition. If an obligation to pay contingent consideration that meets the definition of a financial instrument is classified as equity, then it is not re-measured and settlement is accounted for within equity. Otherwise, subsequent changes in the fair value of the contingent consideration are recognized in net income and comprehensive income.

At the date of the acquisition, the non-controlling interest is measured at the non-controlling interest's proportionate share of the fair value of identifiable assets of the acquiree. Contingent consideration in respect of certain acquisitions, accounted for as exchangeable interest liability, is recorded on the consolidated balance sheet with periodic changes in fair value of that liability reflected in net income and comprehensive income.

### 15.5 Segment information

The operations and productive capacity of the Facilities revolve around the provision of surgical procedures. Each Facility is organized as an individual entity and separate financial statements are prepared for each entity. The chief operating decision makers of the Corporation, being the Chief Executive Officer and the Chief Financial Officer, regularly review performance of each individual Facility to make decisions about resources to be allocated to each Facility and assess their performance. Therefore, each Facility represents a separate operating segment.

Management of the Corporation has concluded that the operating segments of the Corporation meet the criteria for aggregation pursuant to IFRS 8, *Operating Segments* and, therefore, discloses a single reportable segment. In forming its conclusion about the aggregation of the Facilities, management of the Corporation evaluated the long-term economic characteristics of each Facility, the comparative nature of the Facilities' operations, and the level of regulation of each Facility.

The services delivered by each Facility and the patients who use those services are similar. The vast majority of patients are insured through private insurance or government insurance programs (i.e., Medicaid or Medicare), which allows for a wide group of patients electing to have their procedures performed at one of the Facilities. The Facilities principally provide surgical facilities, support staff and pre- and post-surgical care related to surgeries. Finally, the Facilities have similar economic characteristics, which management defines as comparable long-term operating margins, recognizing differences between the Facilities in payor mix, surgical specialties and local healthcare markets.

## 15. SIGNIFICANT ACCOUNTING POLICIES (Continued)

### 15.6 Discontinued operations

A discontinued operation is a component of the Corporation's business which can be clearly distinguished from the rest of the Corporation, both operationally and for financial reporting purposes. Classification as a discontinued operation occurs at the earlier of disposal or when the operation meets the criteria to be classified as held for sale. When an operation is classified as a discontinued operation, the comparative consolidated statement of income and comprehensive income is re-presented as if the operation has been discontinued from the start of the comparative year. Discontinued operations are excluded from the results of continuing operations and are presented as a single net of tax amount as net income from discontinued operations in the consolidated statements of net income and comprehensive income.

### 15.7 Cash and cash equivalents

Cash and cash equivalents consist of cash on hand and all liquid investments purchased with a maturity of six months or less from the purchase date and which can be redeemed by the Corporation.

### 15.8 Short-term and long-term investments

Investments represent liquid investments purchased with a maturity of more than six months. Investments with maturities of more than six months but less than twelve months are classified as short-term and investments with maturities of twelve months or more are classified as long-term. The Corporation limits its exposure to credit risk through application of its investment policy. The policy permits investment of its cash and cash equivalents and short-term and long-term investments in (i) liquid securities issued or guaranteed by the Governments of Canada and the United States of America, or political subdivisions thereof and with (ii) certain Canadian chartered banks or banks regulated by the United States of America as listed in the policy. The carrying amount of investments represents the Corporation's maximum exposure to credit risk for such investments.

## 15. SIGNIFICANT ACCOUNTING POLICIES (Continued)

### 15.9 Accounts receivable

Accounts receivable are recorded at the time services are rendered at the amounts estimated to be recoverable from third-party payors and patients, by applying the following policies:

(i) Amounts billed are reduced by an allowance for third-party payor adjustments which are maintained at a level management believes reflects the estimated adjustments that will be applied upon collection of the amounts billed. The allowance is established using the third-party payor contracts effective at period end and/or based on historical payment rates.

(ii) An allowance for non-collectible receivable balances is recognized at a level management believes is adequate to absorb probable losses. Management determines the adequacy of the allowance based on historical data, current economic conditions, and other pertinent factors for the respective Facility. Patient receivables are written off as non-collectible when all reasonable collection efforts have been exhausted.

Payments from third-party payors are generally received within 60 days of the billing date. However, accounts involving non-contracted payment sources, such as auto and general liability insurance, are subject to recovery efforts, including rebilling and insurance litigation, until they are collected or considered not collectible. Residual amounts due from patients, such as co-payments and deductibles, are considered past due 30 days after receiving payment from third-party payors.

### 15.10 Supply inventory

Supply inventory consists of medical supplies, including implants and pharmaceuticals. It is stated at the lower of cost or net realizable value, using the first-in, first-out valuation method.

### 15.11 Property and equipment

Property and equipment are stated at cost less accumulated depreciation. Cost includes expenditures that are directly attributable to the acquisition of the asset.

Depreciation of property and equipment is computed using the straight-line method over the estimated useful lives of the assets. Land is not depreciated. The estimated useful lives of property and equipment are as follows:

| | |
|---|---|
| Building and improvements | 3-40 years |
| Equipment and furniture | 3-20 years |

Depreciation methods, useful lives and residual values are reviewed on an annual basis.

## 15. SIGNIFICANT ACCOUNTING POLICIES (Continued)

### 15.12 Right-of-use assets

Depreciation of right-of-use assets is computed using the straight-line method over the shorter of the lease term and their useful lives unless it is reasonably certain that the Facilities will obtain ownership by the end of the lease term.

### 15.13 Goodwill

Goodwill arises on the acquisition of subsidiaries and represents the excess of cost over the fair value of identifiable net assets acquired. For business acquisitions occurring after the date of transition to IFRS (January 1, 2010), goodwill is also recognized on non-controlling interest based on elections made independently for each acquisition. Goodwill is stated at cost less accumulated impairment losses. Goodwill is not amortized but is reviewed at least annually for impairment and when events or changes in circumstances indicate that the carrying amount may not be recoverable.

### 15.14 Other intangibles

Other intangibles are recognized only when it is probable that the expected future economic benefits attributable to the assets will be realized by the Corporation and the cost can be reliably measured. Other intangibles represent the value of the hospital operating licenses, non-compete agreements, medical charts and records, care networks and trade names. Other intangibles are stated at cost less accumulated amortization and accumulated impairment losses, when applicable.

Upon recognition of an intangible asset, the Corporation determines if the asset has a definite or indefinite life. In making the determination, the Corporation considers the expected use, expiry of agreements, nature of assets, and whether the value of the assets decreases over time.

Amortization is recognized on a straight-line basis over the estimated useful lives of other intangibles from the date they are available for use. The estimated useful lives of other intangibles are as follows:

| | |
|---|---|
| Hospital operating licenses | 5 years - indefinite life |
| Non-compete agreements | 3-5 years |
| Medical charts and records | 5-7 years |
| Care networks | 9-15 years |
| Trade names | 20 years - indefinite life |

Trade names represent the value assigned to the reputation of the hospitals and their standing in the business and local community which allow them to earn higher than average returns.

## 15. SIGNIFICANT ACCOUNTING POLICIES (Continued)

### 15.15 Impairment of non-financial assets

Non-financial assets that have an indefinite useful life, such as goodwill, certain trade names and certain hospital operating licenses, are tested at least annually for impairment and when events or changes in circumstances indicate that the carrying amount may not be recoverable. Non-financial assets that have a definite useful life which are subject to amortization are reviewed for impairment when events or changes in circumstances indicate that the carrying amount may not be recoverable.

For the purposes of assessing impairment, assets are grouped at the cash-generating unit ("CGU") level, which is the lowest level for which there are separately identifiable cash flows. Management considers each Facility as a CGU, with the exception of the six MFC Nueterra ASCs which collectively constitute a single CGU.

An impairment loss is recognized for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is calculated based on two approaches: 1) the estimated future cash flows, discounted to their present value using a post-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset, and 2) the trailing twelve months and estimated future EBITDA multiplied by a market multiple relevant to the CGU.

An impairment loss is recognized in net income and comprehensive income. It is allocated first to reduce the carrying amount of any goodwill allocated to the respective Facility, and then to reduce the carrying amount of the other assets of the respective Facility on a pro rata basis.

### 15.16 Financial assets and liabilities

The Corporation initially recognizes financial assets on the date that they originate or on the trade date at which the Corporation becomes a party to the contractual provisions of the instrument. The Corporation derecognizes a financial asset when the contractual rights to the cash flows from the asset expire, or it transfers the rights to receive the contractual cash flows on the financial asset in a transaction in which substantially all the risks and rewards of ownership of the financial asset are transferred. The Corporation assesses financial assets for impairment at each reporting date.

### 15.17 Impairment of non-derivative financial assets

Financial assets not designated as fair value through profit or loss ("FVTPL"), including interests in equity accounted investees, are assessed at each reporting date to determine whether there is objective evidence of impairment.

## 15. SIGNIFICANT ACCOUNTING POLICIES (Continued)

### 15.17.1 Financial assets measured at amortized cost

The Corporation considers evidence of impairment for financial assets measured at amortized cost on both an individual and collective basis. In assessing impairment, the Corporation uses historical information on the timing of recoveries and the amount of loss incurred, and makes an adjustment if current economic and credit conditions are such that actual losses are likely to be greater or lesser than suggested by historical trends.

The Corporation applies expected credit loss ("ECL") models to the assessment of impairment on accounts receivables and other financial assets of the Corporation. The ECL model requires considerable judgment, including consideration of how changes in economic factors affect ECLs, which is determined on a probability-weighted basis. The impairment model is applied, at each balance sheet date, to financial assets measured at amortized cost or those measured at fair value through other comprehensive income, except for investments in equity instruments. The Corporation adopts the practical expedient to determine ECL on trade receivables using a provision matrix based on historical credit loss experiences to estimate lifetime ECL. The ECL model applied to other financial assets also requires judgment, assumptions and estimations on changes in credit risks, forecasts of future economic conditions and historical information on the credit quality of the financial asset.

Impairment losses are recorded in general and administrative expenses in the consolidated statements of income and comprehensive income with the carrying amount of the financial asset or group of financial assets reduced through the use of impairment allowance accounts. In periods subsequent to the impairment where the impairment loss has decreased, and such a decrease can be related objectively to conditions and changes in factors occurring after the impairment was initially recognized, the previously recognized impairment loss is reversed through the consolidated statements of income and comprehensive income. The impairment reversal is limited to the lesser of the decrease in impairment or the extent that the carrying amount of the financial asset at the date the impairment is reversed does not exceed what the amortized cost would have been had the impairment not been recognized, after the reversal.

An impairment loss is calculated as the difference between an asset's carrying amount and the present value of the estimated future cash flows discounted at the asset's original effective interest rate. Losses are recognized in net income and comprehensive income and reflected in an allowance account. If the amount of an impairment loss subsequently decreases, then the amount is reversed through net income and comprehensive income.

### 15.17.2 Equity-accounted investee

An impairment loss in respect of an equity-accounted investee is measured by comparing the recoverable amount of the investment with its carrying amount. An impairment loss is recognized in net income and comprehensive income and is reversed if there has been a favourable change in the estimates used to calculate that recoverable amount.

## 15. SIGNIFICANT ACCOUNTING POLICIES (Continued)

### 15.18 Measurements of fair value

A number of the Corporation's accounting policies and disclosures require the measurement of fair value for both financial and non-financial assets and liabilities.

Management of the Corporation regularly reviews significant unobservable inputs and valuation adjustments. If third-party information, such as broker quotes or pricing services, is used to measure fair values, then management assesses the evidence obtained from these sources to support the conclusion that such valuations meet the requirements of IFRS, including the level in the fair value hierarchy in which such valuations should be classified.

When measuring the fair value of an asset or a liability, the Corporation uses observable market data to the extent possible. Fair values are categorized into different levels in a fair value hierarchy based on the inputs used in the valuation technique as follows:

Level 1 – unadjusted quoted prices available in active markets for identical assets or liabilities;

Level 2 – inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly (i.e., as prices) or indirectly (i.e., derived from prices); and

Level 3 – inputs for the asset or liability that are not based on observable market data (unobservable inputs).

If the inputs used to measure the fair value of an asset or liability fall into different levels of the fair value hierarchy, then the fair value measurement is categorized in its entirety in the same level of the fair value hierarchy as the lowest level input that is significant to the entire measurement. The Corporation recognizes transfers between levels of the fair value hierarchy at the end of the reporting period during which the change has occurred.

The following accounting policies apply to the subsequent measurement of relevant financial assets:

(i) Financial assets at FVTPL – These assets are subsequently measured at fair value. Net gains and losses, including any interest or dividend income, are recognized in net income and comprehensive income.

(ii) Financial assets at amortized cost – These assets are subsequently measured at amortized cost using the effective interest method. The amortized cost is reduced by impairment losses. Interest income, foreign exchange gains and losses, impairment, and any gain or loss on derecognition are recognized in net income and comprehensive income.

## 15. SIGNIFICANT ACCOUNTING POLICIES (Continued)

### 15.19 Provisions

A provision is recognized if, as a result of a past event, the Corporation has a present legal or constructive obligation that can be estimated reliably and it is probable that an outflow of economic benefits will be required to settle the obligation. Provisions are measured at the estimated expenditures required to settle the present obligation, based on the most reliable evidence available at the reporting date, including the risks and uncertainties associated with the present obligation. Provisions are discounted to their present values where the time value of money is material. All provisions are reviewed at each reporting date and adjusted to reflect the current best estimate.

### 15.20 Convertible debentures

Until their maturity, the Corporation's convertible debentures were convertible into a fixed number of common shares at the option of the holder. The number of common shares to be issued did not vary with changes in the market value of the convertible debentures.

The convertible debentures were denominated in Canadian dollars while the Corporation's functional currency is U.S. dollars, which required the Corporation to deliver a variable amount of cash to settle the obligation. Because the conversion option required the Corporation to deliver a fixed number of common shares to settle a variable liability, the convertible debentures were considered hybrid financial instruments. The Corporation elected to account for the convertible debentures as a financial liability measured at FVTPL. The changes in the recorded amounts of the liability, resulting from the changes in the fair value of the convertible debentures and fluctuations in foreign exchange rates between the periods, were reflected in prior year's net income and comprehensive income.

On December 31, 2019, the Corporation fully repaid the principal and interest of the convertible debentures upon maturity.

### 15.21 Exchangeable interest liability

Exchangeable interest liability represents an estimated liability for the remaining portion of the interest in the Facilities held by the non-controlling interest which can be exchanged, subject to certain restrictions, for common shares of the Corporation. The exchangeable interest liability is measured at fair value. The fair value is measured at the end of each reporting period taking into account (i) the calculated amount of common shares potentially issuable for the remaining portion of the exchangeable interest in the Facilities held by the non-controlling interest, (ii) the market value of common shares, and (iii) the exchange rate between Canadian and U.S. dollars at the end of the reporting period. The change in value of the exchangeable interest liability is included in net income and comprehensive income for the respective periods.

## 15. SIGNIFICANT ACCOUNTING POLICIES (Continued)

### 15.22 Leases

At the inception of a contract, the Corporation assesses whether a contract is or contains a lease based on the definition of a lease in IFRS 16. A contract is, or contains, a lease if the contract conveys a right to control the use of an identified asset for a period of time in exchange for considerations.

The Facilities' lease assets include premises, medical equipment and office equipment. Under IFRS 16, the Corporation recognizes right-of-use assets and lease liabilities for most leases, except for those leases that are of low value or short term (such as certain office equipment). The Corporation recognizes the payments associated with these leases as an expense on a straight-line basis over the lease term.

The Corporation recognizes a right-of-use asset and a lease liability at the lease commencement date. The right-of-use asset is initially measured at cost, which comprises the initial amount of the lease liability adjusted for any lease payments made at or before the commencement date, plus any initial direct costs incurred and an estimate of costs to dismantle and remove the underlying asset or to restore the underlying asset or the site on which it is located, less any lease incentives received.

The right-of-use asset is subsequently depreciated using the straight-line method from the commencement date to the end of the lease term, unless the lease transfers ownership of the underlying asset to the Corporation by the end of the lease term or the cost of the right-of-use asset reflects that the Corporation will exercise a purchase option. In that case the right-of-use asset will be depreciated over the useful life of the underlying asset, which is determined on the same basis as those of property and equipment. In addition, the right-of-use asset is periodically reduced by impairment losses, if any, and adjusted for certain remeasurements of the lease liability.

The lease liability is initially measured at the present value of the lease payments that are not paid at the commencement date, discounted using the incremental borrowing rate. The Corporation determines its incremental borrowing rate by obtaining interest rates from various external financing sources and makes certain adjustments to reflect the terms of the lease and type of the asset leased.

The lease liability is subsequently increased by the interest cost on the lease liability and decreased by lease payment made. It is remeasured when there is a change in future lease payments arising from a change in an index or rate, a change in the estimate of the amount expected to be payable under a residual value guarantee, or as appropriate, changes in the assessment of whether a purchase or extension option is reasonably certain to be exercised or a termination option is reasonably certain not to be exercised.

When the lease liability is remeasured in this way, a corresponding adjustment is made to the carrying amount of the right-of-use asset, or is recorded in the consolidated statement of income and other comprehensive income if the carrying amount of the right-of-use asset has been reduced to zero.

**15. SIGNIFICANT ACCOUNTING POLICIES (Continued)**

The Corporation has applied judgment to determine the lease term for some lease contracts that include renewal options. The assessment of whether the Corporation is reasonably certain to exercise such options impacts the lease term, which significantly affects the amount of lease liabilities and right-of-use assets recognized.

### 15.23 Facility service revenue

Facility service revenue ("revenue") consists of the actual amounts received and the estimated net realizable amounts receivable from patients and third-party payors. Revenue is derived from the provision of the facilities and ancillary services for the performance of scheduled (as opposed to emergency) surgical, imaging, and diagnostic procedures. The Facilities bill either their patients or the patients' third-party payors as of the date of service upon completion of the procedure. Facility service revenue is recognized as of the date of the service when the recovery of consideration is probable and the Corporation is satisfied with the performance objectives.

A small amount of revenue is received directly from self-paying patients while the majority of revenue is received from third-party payors that provide insurance and coverage to patients. Where collection is not probable for self-paying patients, a bad debt expense is recorded against revenues. Each Facility has agreements with third-party payors that provide for payments at amounts different from the Facility's established rates. Payment arrangements include pre-determined rates per diagnosis, reimbursed costs, discounted charges, and per diem payments. As a result of established agreements with third-party payors, settlements under reimbursement arrangements are determined with a high degree of accuracy and are accrued on an estimated basis in the period the services are rendered, and are adjusted in future periods, as final settlements are determined. Differences between the estimated amounts accrued and interim and final settlements are reported in operations in the period of settlement.

### 15.24 Income taxes

Income tax expense (recovery) consists of current and deferred taxes. Income tax expense (recovery) is recognized in the consolidated statements of income and comprehensive income except to the extent that it relates to a business combination or items recognized directly in equity, in which case it is recognized in equity or in other comprehensive income.

Current tax is the expected tax payable on the taxable income for reporting period, using tax rates enacted or substantively enacted on the reporting date, and any adjustment to tax payable in respect of previous years.

## 15. SIGNIFICANT ACCOUNTING POLICIES (Continued)

The Corporation calculates deferred income taxes using the asset and liability method on temporary differences between the carrying amounts of assets and liabilities and their tax bases. Deferred tax assets and liabilities are calculated, without discounting, at tax rates that are expected to apply to their respective period of realization, provided they are enacted or substantively enacted at the end of the reporting period. The effect on tax assets and liabilities of a change in tax rates is recognized in net income and comprehensive income in the period that includes the date of enactment or substantive enactment.

A deferred tax asset is recognized to the extent that it is probable that future taxable profits will be available against which the temporary difference can be utilized. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realized. Deferred tax liabilities are always recognized in full. Deferred tax assets and liabilities are offset when they relate to income taxes levied by the same taxation authority and the Corporation intends to settle its current tax assets and liabilities on a net basis. Deferred tax is provided on temporary differences arising on investments in subsidiaries, except where the timing of the reversal of temporary differences is controlled by the Corporation and it is probable that the temporary differences will not reverse in the foreseeable future.

### 15.25 Share-based payments

The Corporation has an equity settled, share-based compensation plan under which the entity receives services from key executives as consideration for the Options of the Corporation. The fair value of the services received in exchange for the grants of the Options is recognized as an expense. The total amount to be expensed is determined by reference to the fair value of the Options granted.

Non-market vesting conditions are included in assumptions about the number of Options that are expected to vest. The total expense is recognized over the vesting period, which is the period over which all of the specified vesting conditions are to be satisfied. When the Options are exercised, the Corporation issues new common shares. The proceeds received, together with the amount recorded in contributed surplus, are credited to share capital when the Options are exercised.

The dilutive effect of outstanding Options is reflected as additional share dilution in the computation of fully diluted earnings per share.

### 15.26 New and revised IFRS not yet adopted

There are no relevant new and revised IFRS that have been issued but are not yet effective, and not yet adopted by the Corporation.