Interim Condensed Consolidated Financial Statements

Element Fleet Management Corp.

September 30, 2020

Element Fleet Management Corp.

INTERIM CONDENSED CONSOLIDATED STATEMENTS OF FINANCIAL POSITION

(unaudited, in thousands of Canadian dollars)

	As at September 30, 2020	As at December 31, 2019
	$	$
ASSETS		
Cash	**75,633**	24,224
Restricted funds (note 6)	**488,250**	434,128
Finance receivables (note 3 and 16)	**10,145,518**	11,986,974
Equipment under operating leases (note 4)	**2,022,871**	2,101,367
Accounts receivable and other assets	**208,161**	219,676
Derivative financial instruments (note 16)	**63,665**	41,396
Property, equipment and leasehold improvements, net	**121,978**	141,626
Intangible assets, net	**825,089**	793,279
Deferred tax assets	**485,269**	440,952
Goodwill	**1,275,435**	1,245,981
	15,711,869	17,429,603
LIABILITIES AND SHAREHOLDERS' EQUITY		
Liabilities		
Accounts payable and accrued liabilities	**911,719**	924,936
Derivative financial instruments (note 16)	**88,962**	39,145
Borrowings (note 6)	**10,735,285**	11,892,861
Convertible debentures (note 7 and 16)	**153,113**	711,791
Deferred tax liabilities	**88,233**	48,225
	11,977,312	13,616,958
Shareholders' equity (note 8)	**3,734,557**	3,812,645
	15,711,869	17,429,603

See accompanying notes

On behalf of the Board:

Director Director

Element Fleet Management Corp.

INTERIM CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

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

	Three-month period ended September 30, 2020	Three-month period ended September 30, 2019
	$	$
NET REVENUE		
Interest income, net (note 10)	**122,100**	157,633
Rental revenue and other (note 10)	**159,381**	183,270
Depreciation of equipment under operating leases (note 4)	**(104,908)**	(118,767)
	176,573	222,136
Interest expense	**73,301**	121,605
Net financing revenue	**103,272**	100,531
Fleet service revenue (note 10)	**135,488**	133,034
Direct costs of fixed rate service contracts (note 10)	**(10,754)**	(10,853)
Servicing income, net	**124,734**	122,181
Syndication revenue, net (note 10)	**15,246**	23,084
Net revenue	**243,252**	245,796
OPERATING EXPENSES		
Salaries, wages and benefits	**74,910**	79,904
General and administrative expenses	**28,789**	27,765
Depreciation and amortization (note 15)	**10,568**	10,477
Amortization of convertible debenture discount (note 7)	**843**	2,504
Share-based compensation (note 9)	**5,591**	4,360
	120,701	125,010
OTHER EXPENSES		
Amortization of intangible assets from acquisitions	**9,338**	8,948
Restructuring and transformation costs (note 17)	**24,213**	34,055
Loss on investments	**710**	240
Income before income taxes from operations	**88,290**	77,543
Provision for income taxes	**17,512**	7,398
Net income for the period	**70,778**	70,145
Basic earnings per share (note 12)	**$ 0.14**	$ 0.14
Diluted earnings per share (note 12)	**$ 0.14**	$ 0.13

See accompanying notes

Element Fleet Management Corp.

INTERIM CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(unaudited, in thousands of Canadian dollars, except for per share amounts)

	Nine-month period ended September 30, 2020	Nine-month period ended September 30, 2019
	$	$
NET REVENUE		
Interest income, net (note 10)	**403,490**	491,916
Rental revenue and other (note 10)	**481,833**	559,411
Depreciation of equipment under operating leases (notes 4)	**(319,099)**	(360,893)
	566,224	690,434
Interest expense	**266,992**	379,471
Net financing revenue	**299,232**	310,963
Fleet service revenue (note 10)	**396,227**	398,384
Direct costs of fixed rate service contracts (note 10)	**(31,131)**	(33,793)
Servicing income, net	**365,096**	364,591
Syndication revenue, net (note 10)	**51,666**	62,039
Net revenue	**715,994**	737,593
OPERATING EXPENSES		
Salaries, wages and benefits	**225,239**	244,551
General and administrative expenses	**89,170**	86,155
Depreciation and amortization (notes 15)	**32,134**	31,307
Amortization of convertible debenture discount (note 7)	**5,401**	10,651
Share-based compensation (note 9)	**15,455**	14,940
	367,399	387,604
DISPOSITION OF 19TH CAPITAL		
Gain on settlement of debt (note 5)	**38,580**	—
Loss on sale of assets (note 5)	**(52,442)**	—
Net loss on disposition	**(13,862)**	—
OTHER EXPENSES		
Amortization of intangible assets from acquisitions	**29,221**	27,236
Restructuring and transformation costs (note 17)	**57,871**	62,742
Loss on investments	**764**	1,332
Income before income taxes from operations	**246,877**	258,679
Provision for income taxes	**38,147**	44,000
Net income for the period	**208,730**	214,679
Basic earnings per share (note 12)	**$ 0.40**	$ 0.42
Diluted earnings per share (note 12)	**$ 0.40**	$ 0.41

See accompanying notes

Element Fleet Management Corp.

INTERIM CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(unaudited, in thousands of Canadian dollars)

	Three-month period ended September 30, 2020	Three-month period ended September 30, 2019
	$	$
Net income for the period	**70,778**	70,145
OTHER COMPREHENSIVE (LOSS) INCOME		
Items that may be reclassified subsequently to profit or loss:		
Cash flow and foreign exchange hedges (loss) gain	**(1,654)**	125
Net unrealized foreign exchange (loss) gain	**(21,699)**	7,460
	(23,353)	7,585
Provision for income taxes	**1,739**	46
Total other comprehensive loss	**(25,092)**	7,539
Comprehensive income for the period	**45,686**	77,684

See accompanying notes

Element Fleet Management Corp.

INTERIM CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(unaudited, in thousands of Canadian dollars)

	Nine-month period ended September 30, 2020	Nine-month period ended September 30, 2019
	$	$
Net income for the period	**208,730**	214,679
OTHER COMPREHENSIVE LOSS		
Items that may be reclassified subsequently to profit or loss:		
Cash flow and foreign exchange hedges loss	**(43,292)**	(2,110)
Net unrealized foreign exchange loss	**(14,574)**	(137,813)
	(57,866)	(139,923)
Recovery of income taxes	**(9,373)**	(2,071)
Total other comprehensive loss	**(48,493)**	(137,852)
Comprehensive income for the period	**160,237**	76,827

See accompanying notes

Element Fleet Management Corp.

INTERIM CONDENSED CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY

(unaudited, in thousands of Canadian dollars)

	Common share capital	Preferred share capital	Equity component of convertible debentures	Contributed surplus	Retained earnings (deficit)	Accumulated other comprehensive income (loss)	Total shareholders' equity
	$	$	$	$	$	$	$
Balance, December 31, 2019	**3,127,714**	**680,412**	**59,603**	**68,754**	**(217,900)**	**94,062**	**3,812,645**
Comprehensive income (loss) for the period	—	—	—	—	**208,730**	**(48,493)**	**160,237**
Dividends - Preferred shares (note 8)	—	—	—	—	**(32,717)**	—	**(32,717)**
Dividends - Common shares (note 8)	—	—	—	—	**(59,729)**	—	**(59,729)**
Redemption of preferred shares (note 8)	—	**(168,543)**	—		**(3,957)**	—	**(172,500)**
Options exercised (notes 8 and 9)	**21,050**	—	—	**(7,225)**	—	—	**13,825**
Issuance of shares, net of share issue costs (note 8)	**12,171**	—	—	—	—	—	**12,171**
Employee stock option expense (note 9)	—	—	—	**625**	—	—	**625**
Balance, September 30, 2020	**3,160,935**	**511,869**	**59,603**	**62,154**	**(105,573)**	**45,569**	**3,734,557**
Balance, December 31, 2018	3,092,010	680,412	46,200	75,805	(175,426)	256,484	3,975,485
Impact on adopting IFRS 16	—	—	—	—	1,958	—	1,958
Restated opening balance under IFRS 16	3,092,010	680,412	46,200	75,805	(173,468)	256,484	3,977,443
Comprehensive income (loss) for the period	—	—	—	—	214,679	(137,852)	76,827
Dividends - Preferred shares (note 8)	—	—	—	—	(33,399)	—	(33,399)
Dividends - Common shares (note 8)	—	—	—	—	(58,473)	—	(58,473)
Options exercised (notes 8 and 9)	10,977	—	—	(7,647)	—	—	3,330
Issuance of shares, net of share issue costs (note 8)	6,577	—	—	—	—	—	6,577
Issuance of convertible debentures	—	—	18,544	—	—	—	18,544
Deferred income taxes on equity component of convertible debentures	—	—	(4,812)	—	—	—	(4,812)
Employee stock option expense (note 9)	—	—	—	2,393	—	—	2,393
Balance, September 30, 2019	3,109,564	680,412	59,932	70,551	(50,661)	118,632	3,988,430

See accompanying notes

Element Fleet Management Corp.

INTERIM CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(unaudited, in thousands of Canadian dollars)

	Nine-month period ended September 30, 2020	Nine-month period ended September 30, 2019
	$	$
OPERATING ACTIVITIES		
Net income for the period	**208,730**	214,679
Items not affecting cash		
Share-based compensation (note 9)	**625**	2,393
Depreciation of property, equipment and leasehold improvements	**21,362**	20,441
Amortization of intangible assets, including from acquisitions	**39,993**	38,102
Amortization of deferred lease costs	**19,607**	23,064
Amortization of deferred financing costs	**28,873**	31,304
Depreciation of equipment under operating leases (note 4)	**319,099**	360,893
Amortization of convertible debenture discount and deferred costs (note 7)	**8,522**	16,407
Disposal of intangible assets	**1,089**	—
Loss on investments	**764**	1,332
Loss on disposal of 19th Capital, excluding fees	**7,504**	—
Impairment of fixed assets	**4,113**	—
Provision for credit losses	**12,236**	1,399
	672,517	710,014
Changes in non-cash operating assets and liabilities		
Investment in finance receivables	**(3,959,822)**	(4,771,115)
Repayments of finance receivables	**3,703,971**	3,354,904
Investment in equipment under operating leases	**(647,178)**	(854,885)
Proceeds on disposal of equipment under operating leases	**219,174**	267,756
Syndications of finance receivables	**2,236,910**	1,950,405
Cash payments for interest portion of lease liability	**(2,197)**	(1,871)
Other non-cash operating assets and liabilities	**(69,125)**	39,557
Cash provided by operating activities	**2,154,250**	694,765
INVESTING ACTIVITIES		
Investments	**(201)**	(338)
Sale of ECAF I Holdings Ltd.	—	97,476
Sale of 19th Capital Group LLC	**63,283**	—
Purchase of property, equipment and leasehold improvements	**(5,594)**	(26,983)
Proceeds on disposals of property, equipment and leasehold improvements, and intangible assets	**814**	28,034
Purchase of intangible assets	**(43,587)**	(12,630)
Decrease in notes receivable	**1,063**	3,720
Cash provided by investing activities	**15,778**	89,279
FINANCING ACTIVITIES		
Cash payments for principal portion of lease liability	**(5,361)**	(8,012)
(Increase) / decrease in restricted funds	**(42,069)**	25,637
Increase in deferred financing costs	**(17,626)**	(21,536)
Issuance of share capital, net	**13,825**	9,907
Repayments of borrowings, net	**(1,741,867)**	(510,554)
Settlement of 19th Capital Group LLC debt	**(59,479)**	—
Dividends paid	**(79,925)**	(85,295)
Issuance of senior notes	**550,520**	—
Repayment of convertible debenture	**(567,200)**	(345,000)
Issuance of 2019 convertible debenture	—	172,500
Redemption of preferred shares	**(172,500)**	—
Cash used in financing activities	**(2,121,682)**	(762,353)
Effects of foreign exchange rates on cash	**3,063**	(2,489)
Net increase in cash during the period	**51,409**	19,202
Cash, beginning of the period	**24,224**	21,999
Cash, end of the period	**75,633**	41,201
Supplemental cash flow information:		
Cash taxes paid	**33,983**	36,348
Cash interest paid	**242,761**	347,284

See accompanying notes

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(unaudited, in thousands of Canadian dollars, except where otherwise noted and per share amounts)

1. CORPORATE INFORMATION

Element Fleet Management Corp. ("Element" or the "Company"), was incorporated under the *Business Corporations Act (Ontario)* on May 11, 2007 and commenced operations on that date. The registered office of the Company is 161 Bay Street, Suite 3600, Toronto, Ontario. The Company is a public corporation traded on the Toronto Stock Exchange (the "TSX") under the symbol "EFN".

Element is a publicly traded fleet management company with approximately $15.7 billion in assets and operations in the United States ("US"), Canada, Mexico, Australia and New Zealand. Element is a leading global fleet management company, providing world-class services and financings for commercial vehicle and equipment fleets, reaching 50 countries worldwide through the Element-Arval Global Alliance. Element provides a comprehensive range of fleet services that span the total lifecycle, from vehicle acquisition and financing to program management and remarketing – helping more than 5,500 clients optimize their fleet performance and productivity.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Statement of compliance

These unaudited interim condensed consolidated financial statements are prepared in accordance with International Financial Reporting Standards ("IFRS"), International Accounting Standard 34, *Interim Financial Reporting* ("IAS 34")*,* as issued by the International Accounting Standards Board ("IASB").

These unaudited interim condensed consolidated financial statements should be read in conjunction with the consolidated financial statements of the Company as at and for the year ended December 31, 2019, which include information necessary or useful in understanding the Company's business and financial statement presentation. The results reported in these unaudited interim condensed consolidated financial statements should not be regarded as necessarily indicative of results that may be expected for the entire year.

These unaudited interim condensed consolidated financial statements were authorized for issuance by the Board of Directors of the Company on October 27, 2020.

Accounting policies

These unaudited interim condensed consolidated financial statements have been prepared in conformity with accounting polices disclosed in the consolidated financial statements for the year ended December 31, 2019, except as discussed below.

Change in presentation - elimination of Non-Core operating segment

Following the sale of 19th Capital Group LLC ("19th Capital") on May 1, 2020, management no longer reviews the performance of the Non-Core segment separately from the Fleet Management segment. As a result, the Company modified its operating segments by eliminating the Non-Core segment effective Q2

2020 and its results of operations and financial position will be presented as one segment. Prior period comparative information has been restated to conform to this presentation.

The Company will continue to present information by geographic location with no change.

COVID-19

The extent and duration of the impact of COVID-19 on communities and the economy continues to remain unclear. In the preparation of these unaudited interim condensed consolidated financial statements, the Company has incorporated the potential impact of COVID-19 into its estimates and assumptions that affect the carrying amounts of assets and liabilities and the reported amount of earnings for the reporting periods using the best available information as at September 30, 2020. Actual results could differ from those estimates. The estimates and assumptions that the Company considers critical and/or could be impacted by COVID-19 include those underlying the estimate of any expected credit losses on its net investment in finance receivables, other receivables, and determining the values of financial instruments for disclosure purposes.

Interest Rate Benchmark Reform

During the first quarter of 2020, the Company adopted amendments ("Amendments") to IFRS 9 *Financial Instruments*, IAS 39 *Financial Instruments: Recognition and Measurement* and IFRS 7 *Financial Instruments: Disclosures (Amendments)*, applicable from November 1, 2019. These Amendments modify certain hedge accounting requirements to provide relief from the effect of uncertainty caused by interest rate benchmark reform ("the IBOR Reform") prior to the transition to alternative interest rates. The adoption of the Amendments had no impact to our unaudited interim condensed consolidated financial statements.

The Company will cease to apply these Amendments as interbank offered rate ("IBOR") based cash flows transition to new risk-free rates or when the hedging relationships to which the relief is applied are discontinued.

Hedge accounting

The Company's accounting policies relating to hedge accounting are described in note 2 and note 20 of the Company's consolidated financial statements for the year ended December 31, 2019. The Company applies hedge accounting when designated hedging instruments are highly effective in offsetting changes in the fair value or cash flows of the hedged items at inception and on an ongoing basis. Retrospective assessments are performed to demonstrate that the relationship has been effective since designation of the hedge and prospective assessments to evaluate whether the hedge is expected to be effective over the remaining term of the hedge. While uncertainty due to the IBOR Reform exists, the Company's prospective effectiveness testing is based on existing hedged cash flows or hedged risks. Any ineffectiveness arising from retrospective testing is recognized in net income.

In addition to potential sources of ineffectiveness outlined in note 20 of the Company's consolidated financial statements for the year ended December 31, 2019, the Reform may result in ineffectiveness as the transition of hedged items and related hedging instruments from IBORs to new risk-free rates may

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(unaudited, in thousands of Canadian dollars, except where otherwise noted and per share amounts)

occur at different times. This may result in different impacts on the valuation or cash flow variability of hedged items and related hedging instruments.

Cash flow hedges

The Company applies hedge accounting for cash flow hedges when the cash flows giving rise to the risk being hedged have a high probability of occurring. While uncertainty due to the IBOR Reform exists, the Company applies the relief provided by the Amendments that the IBOR benchmarks, on which the highly probable hedged cash flows are based, are not altered as a result of the Reform. In addition, associated cash flow hedge reserves are not recycled into net income solely due to changes related to the transition from IBOR to new risk-free rates.

Hedging relationships impacted by interest rate benchmark reform

The following table presents the notional amount of the Company's hedging instruments which reference IBOR that will expire after 2021 and will be affected by the Reform. The notional amounts of the Company's hedging instruments also approximate the extent of the risk exposure the Company manages through hedging relationships:

	As at September 30, 2020 Notional/Principal amount[1] $
Interest rate contracts	
USD LIBOR	**4,350,999**
	4,350,999

1. Excludes interest rate contracts and non-derivative instruments which reference rates to multi-rate jurisdictions, including the Canadian Dollar Offered Rate ("CDOR"), Australian Bank Bill Swap Rates ("BBSW"), and New Zealand Bank Bill Rates ("BBR").

Amendments to IAS 1 and IAS 8: *Definition of Material*

The Company adopted the amendments to IAS 1 and IAS 8 effective January 1, 2020. The amendments provide a new definition of material that states “information is material if omitting, misstating or obscuring it could reasonably be expected to influence decisions that the primary users of general purpose financial statements make on the basis of those financial statements, which provide financial information about a specific reporting entity.”

The amendments clarify that materiality will depend on the nature or magnitude of information, either individually or in combination with other information, in the context of the financial statements. A misstatement of information is material if it could reasonably be expected to influence decisions made by the primary users. These amendments had no impact on the interim condensed consolidated financial statements of, nor is there expected to be any future impact to the Company.

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(unaudited, in thousands of Canadian dollars, except where otherwise noted and per share amounts)

Future accounting changes

In August 2020, the IASB published *Interest Rate Benchmark Reform - Phase 2: Amendments to IFRS 9, IAS 39, IFRS 7, IFRS 4, and IFRS 16* ("Phase 2 Amendments"). The Phase 2 Amendments are effective January 1, 2021. The Company is currently evaluating the impact of the Phase 2 Amendments on its financial reporting in relation to the IBOR Reform.

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(unaudited, in thousands of Canadian dollars, except where otherwise noted and per share amounts)

3. FINANCE RECEIVABLES

The following tables present finance receivables based on the ultimate obligor's location:

	As at September 30, 2020			
	US and Canada	**Australia and New Zealand**	**Mexico**	**Total**
	$	**$**	**$**	**$**
Minimum lease payments	**8,756,754**	**265,274**	**257,779**	**9,279,807**
Unguaranteed residual values	**3,434**	**60,135**	**—**	**63,569**
Gross investment	**8,760,188**	**325,409**	**257,779**	**9,343,376**
Unearned income	**(576,034)**	**(39,995)**	**—**	**(616,029)**
Net investment	**8,184,154**	**285,414**	**257,779**	**8,727,347**
Net realizable value of impaired receivables	**26,358**	**7,949**	**—**	**34,307**
Unamortized deferred costs and subsidies	**(101,585)**	**—**	**—**	**(101,585)**
Prepaid lease payments and security deposits	**(19,446)**	**—**	**(22,197)**	**(41,643)**
Interim funding	**792,461**	**—**	**16,449**	**808,910**
Fleet management receivables	**344,745**	**36,705**	**18,169**	**399,619**
Other receivables	**213,150**	**73,191**	**51,051**	**337,392**
Allowance for credit losses (Subsection C)	**(15,084)**	**(2,354)**	**(1,391)**	**(18,829)**
Total finance receivables	**9,424,753**	**400,905**	**319,860**	**10,145,518**

	As at December 31, 2019			
	US and Canada	Australia and New Zealand	Mexico	Total
	$	$	$	$
Minimum lease payments	10,047,261	258,465	192,605	10,498,331
Unguaranteed residual values	1,150	59,790	—	60,940
Gross investment	10,048,411	318,255	192,605	10,559,271
Unearned income	(837,163)	(39,622)	—	(876,785)
Net investment	9,211,248	278,633	192,605	9,682,486
Net realizable value of impaired receivables	47,972	5,560	—	53,532
Unamortized deferred costs and subsidies	(107,257)	—	—	(107,257)
Prepaid lease payments and security deposits	(40,431)	—	(26,436)	(66,867)
Interim funding	1,311,256	—	110,351	1,421,607
Fleet management receivables	631,720	38,222	21,966	691,908
Other receivables	183,804	77,254	58,939	319,997
Allowance for credit losses (Subsection C)	(6,227)	(1,192)	(1,013)	(8,432)
Total finance receivables	11,232,085	398,477	356,412	11,986,974

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(unaudited, in thousands of Canadian dollars, except where otherwise noted and per share amounts)

A) Delinquency status of net investment in finance receivables

The following table presents the delinquency status of the net investment in finance receivables, by contract balance:

	As at September 30, 2020		As at December 31, 2019	
	$	**%**	$	%
31-60 days past due	**8,545**	**0.10**	8,410	0.09
61-90 days past due	**1,536**	**0.02**	3,433	0.04
91-120 days past due	**425**	**0.00**	3,024	0.03
Total past due	**10,506**	**0.12**	14,867	0.16
Current	**8,716,841**	**99.88**	9,667,619	99.84
Total net investment	**8,727,347**	**100.00**	9,682,486	100.00

B) Interest rate characteristics of net investment in finance lease receivables and loan receivables

	As at September 30, 2020		As at December 31, 2019	
	Leases	**Loans**	Leases	Loans
Net investment	**$ 8,629,162**	**$ 98,185**	$ 9,579,674	$ 102,812
Weighted average fixed interest rate	**4.69 %**	**8.82 %**	4.76 %	9.09 %
Weighted average floating interest rate	**2.76 %**	**5.88 %**	4.33 %	6.48 %
Percentage of portfolio with fixed interest rate	**46.02 %**	**99.91 %**	46.29 %	98.49 %

C) Allowance for credit losses

In accordance with IFRS 9, *Financial Instruments*, the Company applies the expected credit loss (“ECL”) model to loans that are financially healthy with no sign of increased credit risk (Stage 1), leases and loans that have an increased credit risk when compared to origination but are not credit impaired (Stage 2 or Performing), and impaired leases and loans (Stage 3 or Impaired) at the end of each reporting period. The ECL model requires consideration of many different factors in making an assessment of the Company’s credit risk on its leases and loans and includes forward-looking macroeconomic information such as changes in Gross Domestic Product ("GDP") and its effect on the probability of default ("PD") and forecast used vehicle market and its impact on loss given default ("LGD"). The Company continues to monitor its inputs to the model to ensure it appropriately reflects current market conditions in light of the global outbreak of COVID-19 and information available to the Company as at September 30, 2020.

PD represents the likelihood that a lease or loan will not be repaid and will go into default. The Company evaluates its credit risk exposure broadly in line with Standard & Poor’s and Moody’s ratings outlined below and will adjust internal classifications based on additional information the Company has available to it at the time of the assessment. In conjunction with the Company’s evaluation of PD as of

September 30, 2020, and consistent with the ECL model, the Company reviewed its classifications and updated its internal assessment of PD based on current information.

LGD is the amount that may not be recovered in the event of a default and is modeled on historical information. The Company's lease and loan portfolio is secured by the underlying assets and, in the event of an obligor bankruptcy, leases are typically affirmed, resulting in continued collection of lease payments. Further, all the vehicles in a client portfolio are cross-collateralized, such that the surplus collateral on (usually older) vehicles can be used to offset under-collateralized positions (usually newer vehicles), such that the net full value of the lease and loan would be recovered. As a result, the Company is often able to recover 100% of the net investment. Additionally, used vehicle pricing continued to see improvements during the three-months ended September 30, 2020 driving a decrease in the LGD as at September 30, 2020. The Company expects that the used vehicle market will continue to hold its values in the aftermath of the pandemic as drivers of vehicles keep their cars for longer periods of time (or purchase used vehicles instead of new vehicles), reducing the supply in the used car market and increasing prices. The Company does not believe the strength seen in the second and third quarters of 2020 is short lived, although some short term volatility can be expected.

Based on the Company's review of its inputs to the model during the third quarter of 2020, there were positive changes to the PD profiles and positive improvements to the LGD indicating favorability in the allowance for credit losses. The Company also considered forward-looking macroeconomic information in light of COVID-19 such as projected changes in GDP and the impact potential downward trends in GDP would have on the Company's lease and loan portfolio. The Company has also evaluated multiple scenarios related to COVID-19, including expected time periods of market slow-down and recovery. Given the continued uncertainty of the pandemic and based on forward-looking macroeconomic expectations as offset only slightly by the favorable used vehicle market, the Company maintained a relatively consistent allowance for credit losses of $18,829 at September 30, 2020.

The Company's evaluation of the above inputs to its model resulted in a (recovery of)/provision for credit losses of $(876) and $12,236 for the three- and nine-month periods ended September 30, 2020.

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(unaudited, in thousands of Canadian dollars, except where otherwise noted and per share amounts)

An analysis of the Company's allowance for credit losses under IFRS 9 is as follows:

Finance leases	**Performing**	**Impaired**	**Total**
	$	**$**	**$**
Balance as at January 1, 2020	**7,537**	**535**	**8,072**
Transfer to Performing	**493**	**(493)**	**—**
Transfer to Impaired	**(294)**	**294**	**—**
Lease originations	**12,291**	**—**	**12,291**
Changes in models and inputs, derecognition, and repayments	**(41)**	**(8)**	**(49)**
Total	**19,986**	**328**	**20,314**
Charge-offs, net of recoveries	**(1,165)**	**6**	**(1,159)**
Foreign exchange	**(368)**	**8**	**(360)**
Balance as at September 30, 2020	**18,453**	**342**	**18,795**

Fleet management receivables	**Performing**	**Impaired**	**Total**
	$	**$**	**$**
Balance as at January 1, 2020	**50**	**9**	**59**
Provision for credit losses	**39**	**44**	**83**
Charge-offs, net of recoveries	**(63)**	**(48)**	**(111)**
Foreign exchange	**2**	**—**	**2**
Balance as at September 30, 2020	**28**	**5**	**33**

Loans	**Stage 1**	**Stage 2**	**Stage 3**	**Total**
	$	**$**	**$**	**$**
Balance as at January 1, 2020	**4**	**266**	**31**	**301**
Changes in models and inputs, derecognition, and repayments	**(3)**	**(61)**	**(25)**	**(89)**
Total	**1**	**205**	**6**	**212**
Charge-offs, net of recoveries	**—**	**(207)**	**(6)**	**(213)**
Foreign exchange	**—**	**2**	**—**	**2**
Balance as at September 30, 2020	**1**	**—**	**—**	**1**

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(unaudited, in thousands of Canadian dollars, except where otherwise noted and per share amounts)

Finance leases	Performing	Impaired	Total
	$	$	$
Balance as at January 1, 2019	8,556	322	8,878
Transfer to Performing	82	(82)	—
Transfer to Impaired	(698)	698	—
Lease originations	9,276	—	9,276
Changes in models and inputs, derecognition, and repayments	(6,922)	(397)	(7,319)
Total	10,294	541	10,835
Charge-offs, net of recoveries	(2,023)	—	(2,023)
Foreign exchange	(734)	(6)	(740)
Balance as at December 31, 2019	7,537	535	8,072

Fleet management receivables	Performing	Impaired	Total
	$	$	$
Balance as at January 1, 2019	19	12	31
Provision for credit losses	2	123	125
Charge-offs, net of recoveries	31	(126)	(95)
Foreign exchange	(2)	—	(2)
Balance as at December 31, 2019	50	9	59

Loans	Stage 1	Stage 2	Stage 3	Total
	$	$	$	$
Balance as at January 1, 2019	3	207	213	423
Changes in models and inputs, derecognition, and repayments	3	166	(169)	—
Total	6	373	44	423
Charge-offs, net of recoveries	—	(109)	—	(109)
Foreign exchange	(2)	2	(13)	(13)
Balance as at December 31, 2019	4	266	31	301

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

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A summary view of the Company's allowance for credit losses is as follows:

	Nine-month period ended	Year ended
Allowance for credit losses	**September 30, 2020**	December 31, 2019
	$	$
Allowance for credit losses, beginning of the period	**8,432**	9,332
Provision for credit losses	**12,236**	2,082
Charge-offs, net of recoveries	**(1,483)**	(2,227)
Impact of foreign exchange rates	**(356)**	(755)
Allowance for credit losses, end of the period	**18,829**	8,432
Allowance as a percentage of total finance receivables before allowance	**0.19 %**	0.07%

(unaudited, in thousands of Canadian dollars, except where otherwise noted and per share amounts)

D) Credit risk exposure

The following table sets out the credit risk exposure for loans, finance leases and fleet management service receivables, and the impaired values and allowances for credit losses recorded as at September 30, 2020:

Finance leases	**Performing**	**Impaired**	**Total**
	$	**$**	**$**
Internal risk rating grade			
Low	**5,242,158**	**—**	**5,242,158**
Medium	**3,053,381**	**—**	**3,053,381**
High	**333,623**	**—**	**333,623**
Other finance receivables	**337,392**	**—**	**337,392**
Impaired	**—**	**34,214**	**34,214**
	8,966,554	**34,214**	**9,000,768**
Allowance for credit losses	**(18,453)**	**(342)**	**(18,795)**
Net carrying value	**8,948,101**	**33,872**	**8,981,973**

Fleet management receivables	**Performing**	**Impaired**	**Total**
	$	**$**	**$**
Fleet management receivables	**398,110**	**1,509**	**399,619**
Allowance for credit losses	**(28)**	**(5)**	**(33)**
Net carrying value	**398,082**	**1,504**	**399,586**

Loans	**Stage 1**	**Stage 2**	**Stage 3**	**Total**
	$	**$**	**$**	**$**
Internal risk rating grade				
Low	**—**	**5,358**	**—**	**5,358**
Medium	**6,441**	**85,035**	**—**	**91,476**
High	**—**	**1,351**	**—**	**1,351**
Impaired	**—**	**—**	**93**	**93**
	6,441	**91,744**	**93**	**98,278**
Allowance for credit losses	**(1)**	**—**	**—**	**(1)**
Net carrying value	**6,440**	**91,744**	**93**	**98,277**

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(unaudited, in thousands of Canadian dollars, except where otherwise noted and per share amounts)

The following table sets out the credit risk exposure for loans, finance leases and fleet management service receivables, and the impaired values and allowances for credit losses recorded as at December 31, 2019:

Finance leases	Performing	Impaired	Total
	$	$	$
Internal risk rating grade			
Low	5,877,562	—	5,877,562
Medium	3,538,895	—	3,538,895
High	163,217	—	163,217
Other finance receivables	319,997	—	319,997
Impaired	—	52,870	52,870
	9,899,671	52,870	9,952,541
Allowance for credit losses	(7,537)	(535)	(8,072)
Net carrying value	9,892,134	52,335	9,944,469

Fleet management receivables	Performing	Impaired	Total
	$	$	$
Fleet management receivables	688,266	3,642	691,908
Allowance for credit losses	(50)	(9)	(59)
Net carrying value	688,216	3,633	691,849

Loans	Stage 1	Stage 2	Stage 3	Total
	$	$	$	$
Internal risk rating grade				
Low	6	17,799	—	17,805
Medium	15,106	67,629	—	82,735
High	—	2,248	24	2,272
Impaired	—	—	662	662
	15,112	87,676	686	103,474
Allowance for credit losses	(4)	(266)	(31)	(301)
Net carrying value	15,108	87,410	655	103,173

(unaudited, in thousands of Canadian dollars, except where otherwise noted and per share amounts)

The Company's internal risk rating grades broadly align to external ratings as follows:

Internal risk rating grade	**Standard & Poor's**	**Moody's**
Low risk	AAA to BBB-	Aaa to Baa3
Medium risk	BB+ to B-	Ba1 to B3
High risk	CCC+ and below	Caa1 and below
Impaired receivables	Default	Default

4. EQUIPMENT UNDER OPERATING LEASES

The Company acts as a lessor in connection with operating leases and recognizes the leased assets in its unaudited interim condensed consolidated statements of financial position. The lease payments received are recognized in income as rental revenue.

	As at September 30, 2020	As at December 31, 2019
	$	$
Cost	**2,863,903**	3,155,540
Accumulated depreciation	**841,032**	1,054,173
Net carrying amount	**2,022,871**	2,101,367

5. 19TH CAPITAL

On October 19, 2018, the Company purchased the equity interest held by its joint venture partner for $5,220, (USD $4,000) thereby obtaining 100% ownership and control over 19th Capital. At the time of acquisition, 19th Capital was no longer treated as a joint venture and the assets and liabilities of 19th Capital were recorded on the Company's consolidated statement of financial position as a wholly owned subsidiary at the acquisition-date fair value.

During the fourth quarter of 2019, the Company recorded a $260,000 impairment charge on its truck portfolio as a result of its evaluation of the carrying value of the assets compared to the current market conditions at that time. At December 31, 2019, 19th Capital assets subject to impairment considerations (total assets excluding cash, deferred tax assets and right-of-use ("ROU") assets related to the Company's leases in which it is a lessee) were $133,000, which was comprised primarily of equipment under operating leases, with third-party debt of $122,000.

During the first quarter of 2020, the Company continued to shift its efforts to accelerate the run-off of 19th Capital, including ramping-up the pace of liquidation of the entity's assets, immediately reducing the scale of 19th Capital operations and engaging with third-party lenders. At March 31, 2020, 19th Capital assets (excluding cash, deferred tax assets and ROU assets) were $122,000, which was comprised primarily of equipment under operating leases, with third-party debt of $99,000.

On May 1, 2020, the Company sold the equipment under operating leases and certain other assets of 19th Capital for $63,283 resulting in a pre-tax loss on sale of $52,442. Prior to the sale and during the second quarter of 2020, the Company settled all third-party debt at a discount resulting in a pre-tax gain on the settlement of debt of $38,580. The net pre-tax loss on the sale and settlement of debt is $13,862 which is recorded in the Company's results of operations for the nine-month period ended September 30, 2020.

In conjunction with the sale, the Company entered into a transition services agreement whereby the Company performs certain administrative or overhead functions subsequent to the sale through August 1, 2020, in exchange for a fee. The reimbursement of the expenses associated with the transition services agreement is included as a reduction of general and administrative expenses in the unaudited interim condensed consolidated financial statements. The Company will have no continuing involvement in the operations, results or cash flows of 19th Capital.

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(unaudited, in thousands of Canadian dollars, except where otherwise noted and per share amounts)

6. BORROWINGS

The Company's outstanding borrowings were as follows:

	As at September 30, 2020			
	Balance outstanding	**Weighted average interest rate[1]**	**Pledged finance receivables and equipment under operating leases**	**Cash reserves**
	$	**%**	**$**	**$**
Revolving term notes in amortization	**4,815,178**	**2.23**	**4,838,100**	**54,319**
Variable funding notes	**4,006,545**	**1.33**	**4,197,066**	**56,103**
Other	**44,970**	**4.52**	**44,520**	**—**
Vehicle management asset-backed debt	**8,866,693**	**1.83**	**9,079,686**	**110,422**
Revolving senior credit facilities[2]	**1,354,470**	**1.54**	**—**	**—**
Senior notes	**532,840**	**3.85**	**—**	**—**
	10,754,003	**1.90**	**9,079,686**	**110,422**
Deferred financing costs	**(37,882)**			
Hedge accounting fair value adjustments	**19,164**			
Total borrowings	**10,735,285**			

	As at December 31, 2019			
	Balance outstanding	Weighted average interest rate[1]	Pledged finance receivables and equipment under operating leases	Cash reserves
	$	%	$	$
Revolving term notes in amortization	5,697,575	2.67	6,133,104	58,685
Variable funding notes	4,363,677	2.63	4,634,651	53,623
Other	169,485	4.87	175,019	—
Vehicle management asset-backed debt	10,230,737	2.69	10,942,774	112,308
Revolving senior credit facilities[2]	1,703,507	2.79	—	—
	11,934,244	2.70	10,942,774	112,308
Deferred financing costs	(48,804)			
Hedge accounting fair value adjustments	7,421			
Total borrowings	11,892,861			

1. Represents the weighted average stated interest rate of outstanding debt at period-end, and excludes amortization of deferred financing costs, premiums or discounts, stand-by fees and the effects of hedging.
2. Prior to December 11, 2019, the revolving senior credit facilities are secured by a general security agreement in favor of the lenders in respect of all property. The senior credit facilities are unsecured as of the December 11, 2019 amendment.

The Company was in compliance with all financial and reporting covenants with all of its lenders at September 30, 2020.

Vehicle management asset-backed debt

As at September 30, 2020, the Company had available capacity in variable rate borrowings and other of $3,654,326 (December 31, 2019 – $3,872,777) under its vehicle management asset-backed debt facilities.

During the nine-month period ended September 30, 2020, the Company issued $999,075 (USD $750,000) of revolving term notes. The proceeds from this issuance were used to pay down variable funding notes.

Revolving senior credit facilities

As at September 30, 2020, the Company had access to an additional $2,108,990 (December 31, 2019 - $1,672,593) of available financing from the revolving senior credit facilities.

Senior notes

During the three-month period ended June 30, 2020, the Company issued $532,840 (USD $400,000) in aggregate principal amount of 3.85% senior unsecured notes due June 15, 2025. The senior unsecured notes were priced at $99.985 per $100 principal amount for an effective yield of 3.853%. Interest is paid semi-annually in arrears on June 15 and December 15, commencing on December 15, 2020.

Restricted funds

As at September 30, 2020, restricted funds include (i) cash reserves of $110,422 (December 31, 2019 - $112,308), which represent collateral for secured borrowing arrangements; (ii) cash accumulated in the collection account of $352,361 (December 31, 2019 - $321,820), which represents repayments received on assets financed pursuant to the secured borrowing facilities, which are subsequently remitted back to the facilities on specific dates; and (iii) cash of $25,467 (December 31, 2019 - nil) provided to counter-parties as collateral against derivatives liabilities.

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

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7. CONVERTIBLE DEBENTURES

Convertible debentures consist of:

	As at September 30, 2020						
Issue Date	**Final maturity date**	**Conversion price per share(1)**	**Interest rate(2)**	**Face value**	**Deferred costs**	**Discount**	**Net carrying value**
		$	**%**	**$**	**$**	**$**	**$**
April 5, 2019	**June 30, 2024**	**12.05**	**4.250**	**172,500**	**(4,863)**	**(14,524)**	**153,113**

	As at December 31, 2019						
Issue Date	Final maturity date	Conversion price per share	Interest rate(2)	Face value	Deferred costs	Discount	Net carrying value
		$	%	$	$	$	$
May 29, 2015	June 30, 2020	17.19	4.250	567,200	(2,252)	(2,914)	562,034
April 5, 2019	June 30, 2024	12.05	4.250	172,500	(5,732)	(17,011)	149,757
				739,700	(7,984)	(19,925)	711,791

1. There was no change to the conversion price from the date of issuance for the April 5, 2019 issuance.
2. Stated interest rate on principal face value.

May 29, 2015 Issuance

On June 30, 2020, the $567,200 4.25% extendible convertible unsecured subordinated debentures matured and were repaid in full, including accrued interest, by the Company, on June 29, 2020, in accordance with the Trust Indenture.

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8. SHARE CAPITAL

The Company is currently authorized to issue (i) an unlimited number of common shares without nominal or par value and (ii) an unlimited number of preferred shares, issuable in series.

	Common shares	
	Shares	**Amount**
	#	**$**
Balance, December 31, 2018	433,204,448	3,092,010
Share issuance	1,655,960	19,037
Exercise of options	1,648,709	16,667
Balance, December 31, 2019	**436,509,117**	**3,127,714**
Share issuance	**1,164,435**	**12,171**
Exercise of options	**1,551,523**	**21,050**
Balance, September 30, 2020	**439,225,075**	**3,160,935**

Issuance of common shares

On October 1, 2018, Element announced the adoption of a dividend reinvestment plan ("DRIP"). The DRIP provides eligible shareholders an opportunity to reinvest their eligible cash dividends for additional common shares at a discount of 2% to the prevailing market price of the common shares on the TSX, which discount may be changed or eliminated by the Board of Element from time to time. To be eligible to participate in the DRIP, shareholders must be resident in Canada. Shareholders residing outside of Canada are not eligible to participate in the DRIP. During the three- and nine-month periods ended September 30, 2020, the Company issued 601,483 and 1,164,435 common shares under the DRIP (three- and nine-month periods ended September 30, 2019 - 295,321 and 788,058 common shares).

Common share dividends

During the three- and nine-month periods ended September 30, 2020, the Company declared $19,882 and $59,427, respectively, in common share dividends, or $0.045 and $0.136, respectively, per common share (three- and nine-month periods ended September 30, 2019 - $19,497 and $58,459, respectively, in common shares, or $0.045 and $0.134, respectively, per common share).

As at September 30, 2020, the accrued common share dividends were $19,882 (December 31, 2019 – $19,738).

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Preferred shares

The Company's cumulative 5-Year rate reset Preferred Shares series as at September 30, 2020 consist of the following:

Series	Issue date	Interest rate %	Gross $	After tax transaction costs $	Net proceeds $	Shares #
A	**December 17, 2013**	**6.93**[1]	**115,000**	**4,625**	**110,375**	**4,600,000**
C	**March 7, 2014**	**6.21**[2]	**128,160**	**3,416**	**124,744**	**5,126,400**
E	**June 18, 2014**	**5.903**[3]	**133,048**	**3,054**	**129,994**	**5,321,900**
I	**May 5, 2017**	**5.75**	**150,000**	**3,244**	**146,756**	**6,000,000**

1. On December, 20, 2018, Preferred Shares Series A dividend rate was reset from 6.60% to 6.93%.
2. On June 21, 2019, Preferred Shares Series C dividend rate was reset from 6.50% to 6.21%.
3. On September 19, 2019, Preferred Shares Series E dividend rate was reset from 6.40% to 5.903%.

Series G Preferred Shares Redemption

On September 30, 2020, the Company redeemed all of its 6,900,000 Series G Preferred Shares for a redemption price equal to $25.00 per share for a total of $172,500 together with all accrued and unpaid dividends.

Preferred share dividends

During the three- and nine-month periods ended September 30, 2020, the Company declared $10,906 and $32,717 in preferred share dividends, respectively (three- and nine-month periods ended September 30, 2019 – $11,071 an $33,399, respectively).

As at September 30, 2020, the accrued preferred share dividends were $89 (December 31, 2019 – $120).

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

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9. SHARE-BASED COMPENSATION

Share-based compensation expense consists of the following:

	Three-month period ended		Nine-month period ended	
	September 30, 2020	September 30, 2019	**September 30, 2020**	September 30, 2019
	$	$	**$**	$
(a) Stock options	**3**	535	**625**	2,393
(b) Deferred share units	**511**	496	**1,387**	1,301
(c) Performance share units	**2,249**	641	**6,805**	548
(d) Restricted share units	**2,828**	3,494	**6,638**	11,504
	5,591	5,166	**15,455**	15,746
Allocated as:				
Share-based compensation	**5,591**	4,360	**15,455**	14,940
Restructuring and transformation costs	**—**	806	**—**	806
	5,591	5,166	**15,455**	15,746

(a) Stock options

The changes in the number of stock options during the periods were as follows:

	Number of options	Weighted average exercise price
	#	$
Outstanding, December 31, 2018	25,328,610	10.01
Forfeited	(679,657)	11.13
Expired	(4,977,529)	11.58
Exercised[1]	(3,258,991)	6.14
Outstanding, December 31, 2019	**16,412,433**	**10.26**
Forfeited	**(62,984)**	**8.69**
Expired	**(1,366,387)**	**12.02**
Exercised[1]	**(1,836,528)**	**9.47**
Outstanding, September 30, 2020	**13,146,534**	**10.19**

1. Weighted average share price of options exercised during the nine-month period ended September 30, 2020 was $11.91 (year ended December 31, 2019 – $8.61).

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(unaudited, in thousands of Canadian dollars, except where otherwise noted and per share amounts)

(b) Deferred share units, performance share units and restricted share units

	Deferred share units #	Performance share units #	Restricted share units #
Outstanding, December 31, 2018	781,637	382,339	2,103,733
Granted	216,964	1,125,467	899,248
Forfeited	—	—	(88,477)
Redeemed	(315,898)	—	(1,017,564)
Outstanding, December 31, 2019	**682,703**	**1,507,806**	**1,896,940**
Granted	**139,476**	**561,981**	**730,093**
Forfeited	**—**	**(1,388)**	**(84,160)**
Redeemed	**(124,880)**	**(168,571)**	**(909,573)**
Outstanding, September 30, 2020	**697,299**	**1,899,828**	**1,633,300**

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(unaudited, in thousands of Canadian dollars, except where otherwise noted and per share amounts)

10. REVENUE

Set out below is the disaggregation of the Company's revenue before interest expense.

	Three-month period ended		Nine-month period ended	
	September 30, 2020	September 30, 2019	**September 30, 2020**	September 30, 2019
	$	$	**$**	$
Major service lines				
Interest income, net	**122,100**	157,633	**403,490**	491,916
Rental revenue	**143,139**	169,891	**445,891**	519,762
Gain on sale of equipment under operating leases	**16,242**	13,379	**35,942**	39,649
Depreciation of equipment under operating leases	**(104,908)**	(118,767)	**(319,099)**	(360,893)
Financing revenue before interest expense	**176,573**	222,136	**566,224**	690,434
Other service revenue, net	**98,119**	96,740	**287,601**	286,340
Vehicle sales and end of contract fees	**26,615**	25,441	**77,495**	78,251
Service and other revenue, net	**124,734**	122,181	**365,096**	364,591
Syndication revenue, net	**15,246**	23,084	**51,666**	62,039
Net revenue before interest expense	**316,553**	367,401	**982,986**	1,117,064
Primary geographical markets				
US and Canada	**235,476**	292,949	**758,939**	906,225
Australia and New Zealand	**50,000**	45,356	**135,207**	136,272
Mexico	**31,077**	29,096	**88,840**	74,567
Net revenue before interest expense	**316,553**	367,401	**982,986**	1,117,064
Timing of revenue recognition				
Revenue earned at a point in time	**110,417**	108,241	**313,214**	321,272
Revenue earned over time	**206,136**	259,160	**669,772**	795,792
Net revenue before interest expense	**316,553**	367,401	**982,986**	1,117,064

Revenue earned at a point in time includes gain on sale of equipment under operating leases, commissions from repairs due to accidents, fuel, title and registration fees, syndication revenue, and vendor commissions. Revenue earned over time includes interest income and rental revenue, fleet maintenance and accident management fees, and telematics fees.

(A) Contract balances

	As at September 30, 2020	As at December 31, 2019
	$	$
Contract assets	**16,992**	23,404

Contract assets represent the costs the Company incurs to enter into service contracts with customers including certain commissions. Contract assets are recorded in the unamortized deferred costs and subsidies line within note 3. During the three- and nine-month periods ended September 30, 2020, the

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Company has recorded $2,268 and $7,156, respectively, of amortization on its service contract assets (three- and nine-month periods ended September 30, 2019 - $2,719 and $7,617, respectively).

B) Performance obligations

Fixed-fee Service Contracts. The Company provides separately priced and contracted service contracts to its fleet clients that range from fuel cards, accident management services, and maintenance services. These service contracts generally have open-ended terms and can be in place as long as the client uses the underlying vehicle that is being serviced. Fees are billed monthly and revenue is recognized over the term of the agreement proportionally over the passage of time.

11. INCOME TAXES

The Company calculates the period income tax expense using the tax rate that would be applicable to the expected total annual earnings. IAS 34 requires this annual tax rate to be reviewed each quarter and applied to the profits earned to date.

The effective income tax rate was 19.8% and 15.4% for the three- and nine-month periods ended September 30, 2020, respectively (three- and nine-month periods ended September 30, 2019 - 9.4% and 17.0%, respectively). The year to date effective tax rate is slightly lower than prior years reflecting year-over-year variances in pre-tax net income and other tax related adjustments.

12. EARNINGS PER SHARE

Basic earnings per share is as follow:

	Three-month period ended		**Nine-month period ended**	
	September 30, 2020	September 30, 2019	**September 30, 2020**	September 30, 2019
	$	$	**$**	$
Net income attributable to shareholders	**70,778**	70,145	**208,730**	214,679
Cumulative dividends on preferred shares	**(10,875)**	(11,071)	**(32,687)**	(33,399)
Net income available to common shareholders	**59,903**	59,074	**176,043**	181,280
Weighted average number of common shares outstanding – basic (number)	**438,841,859**	435,139,827	**437,996,862**	434,487,190
Basic earnings per share	**$ 0.14**	$ 0.14	**$ 0.40**	$ 0.42

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(unaudited, in thousands of Canadian dollars, except where otherwise noted and per share amounts)

Diluted earnings per share is as follows for the three- and nine-month periods ended September 30:

	Three-month period ended		**Nine-month period ended**	
	September 30, 2020	September 30, 2019	**September 30, 2020**	September 30, 2019
	$	$	**$**	$
Net income available to common shareholders adjusted for the effects of dilution	**61,608**	60,625	**181,430**	184,378
Weighted average number of common shares outstanding – basic (number)(1)	**438,841,859**	435,139,827	**437,996,862**	434,487,190
Convertible debentures (number)	**14,315,353**	14,381,556	**14,315,353**	14,381,556
Dilutive stock options and warrants (number)	**1,497,772**	1,047,427	**1,487,215**	647,822
Weighted average number of common shares outstanding – diluted (number)	**454,654,984**	450,568,810	**453,799,430**	449,516,568
Diluted earnings per share	**$ 0.14**	$ 0.13	**$ 0.40**	$ 0.41

1. Prior year weighted average number of common shares outstanding has been adjusted for the impact of the issuance of shares under the DRIP by 5,902 and 5,473 shares for the three- and nine-month periods ended September 30, 2019, respectively.

Instruments outstanding as at September 30, 2020 that could potentially dilute basic earnings per share in the future, but were not included in the calculation of diluted earnings per share because they were anti-dilutive, included 7,534,573 and 7,534,573 stock options for the three- and nine-month periods ended September 30, 2020, respectively (three- and nine-month periods ended September 30, 2019, 10,795,603 and 10,795,603 stock options, respectively).

In addition, the 2015 convertible debenture (note 7) was excluded from the diluted earnings per share calculation for the three- and nine-month periods ended September 30, 2019 as it was anti-dilutive.

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(unaudited, in thousands of Canadian dollars, except where otherwise noted and per share amounts)

13. CAPITALIZATION

The Company's objectives when managing capital are to ensure sufficient liquidity to support its financial objectives and strategic plans, to ensure its financial covenants are met and to maximize shareholder value. Element's funding activities are well diversified by facility, geography, investor, and lender and include both secured and unsecured sources.

The Company's capitalization is as follows, as at:

As at	**September 30, 2020**	December 31, 2019
(in $000's)	**$**	$
Cash	**75,633**	24,224
Unsecured debt		
Senior credit facilities	**1,354,470**	1,703,507
4.250% Convertible Debentures due 2020	—	562,034
4.250% Convertible Debentures due 2024	**153,113**	149,757
3.850% Senior Notes due 2025	**532,840**	—
Vehicle Management Asset-Backed Debt		
Revolving term notes in amortization	**4,815,178**	5,697,575
Variable funding notes	**4,006,545**	4,363,677
Other	**44,970**	169,485
Deferred financing costs	**(37,882)**	(48,804)
Hedge accounting fair value adjustments	**19,164**	7,421
Total debt	**10,888,398**	12,604,652
Shareholders' equity		
Common share capital	**3,160,935**	3,127,714
Preferred share capital	**511,869**	680,412
Other	**61,753**	4,519
Total Shareholders' Equity	**3,734,557**	3,812,645
Total Capitalization	**14,622,955**	16,417,297

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(unaudited, in thousands of Canadian dollars, except where otherwise noted and per share amounts)

14. GEOGRAPHIC INFORMATION

The Company primarily operates in the US and Canada, Australia and New Zealand, and Mexico.

Selected geographic assets are as follows:

	As at September 30, 2020				As at December 31, 2019			
	US and Canada	**Australia and New Zealand**	**Mexico**	**Total**	US and Canada	Australia and New Zealand	Mexico	Total
	$	**$**	**$**	**$**	$	$	$	$
Select assets								
Finance receivables	**9,424,753**	**400,905**	**319,860**	**10,145,518**	11,232,085	398,477	356,412	11,986,974
Equipment under operating leases	**47,562**	**1,277,937**	**697,372**	**2,022,871**	174,912	1,273,173	653,282	2,101,367
Goodwill and intangible assets	**2,067,534**	**31,282**	**1,708**	**2,100,524**	2,008,079	30,537	644	2,039,260
Property, equipment and leasehold improvements	**92,474**	**17,818**	**11,686**	**121,978**	111,163	21,937	8,526	141,626
	11,632,323	**1,727,942**	**1,030,626**	**14,390,891**	13,526,239	1,724,124	1,018,864	16,269,227

Geographic selected assets are based on the location of the assets.

15. LEASES

The Company leases its office space and certain office equipment. The Company accounts for the lease components (fixed payments including rent and variable payments that depend on an index or rate) separately from the non-lease components (e.g. common-area maintenance costs).

Most leases include one or more options to renew, with renewal terms that can extend the lease term from one to 10 years or more. The exercise of lease renewal options is at the sole discretion of the Company. The depreciable life of assets and leasehold improvements are limited by the expected lease term, unless there is a transfer of title or purchase option reasonably certain of exercise. Certain of the Company's leases include rental payments adjusted periodically for inflation. The Company's lease agreements do not contain any material residual value guarantees or material restrictive covenants.

Management evaluates all facilities to ensure the Company’s footprint continues to support business activities, employees and client needs. In support of this and to align with the Company’s growth strategy, the Company closed certain facilities in the US, Canada, Australia and New Zealand during the three-months ended September 30, 2020. As a result, the Company recorded an impairment charge of $4,113 through Transformation on the right of use, property, plant, and equipment assets at the closed facilities. The remaining lease liability for the closed facilities was $3,797 as at September 30, 2020.

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(unaudited, in thousands of Canadian dollars, except where otherwise noted and per share amounts)

		As at September 30, 2020	As at December 31, 2019
		$	$
Assets	**Classification**		
Right-of-use assets	Buildings, net of accumulated depreciation[(1)]	**84,196**	95,354
Liabilities	**Classification**		
Lease liabilities	Accounts payable and accrued liabilities	**92,078**	97,439

1. As at September 30, 2020, right-of-use assets are recorded net of accumulated amortization of $25,372 (December 31, 2019 - $12,910).

		Three-month period ended		Nine-month period ended	
		September 30, 2020	September 30, 2019	**September 30, 2020**	September 30, 2019
Lease cost	**Classification**	**$**	$	**$**	$
Amortization of leased assets	Depreciation and amortization	**3,255**	3,311	**10,466**	9,883
Interest on lease liabilities	Interest expense	**712**	651	**2,197**	1,871
Net lease cost		**3,967**	3,962	**12,663**	11,754

Maturity of lease liabilities	**As at September 30, 2020**
	$
2020	**2,726**
2021	**11,491**
2022	**11,765**
2023	**10,664**
2024	**6,801**
Thereafter	**48,631**

Lease Term and Discount Rate	As at September 30, 2020	As at December 31, 2019
Weighted-average remaining lease term (years)	**11.7**	11.5
Weighted-average discount rate	**3.03 %**	3.09 %

16. FAIR VALUE OF FINANCIAL INSTRUMENTS

Fair value is defined as the price that would be received to sell an asset, or paid to transfer a liability, between market participants in an orderly transaction in the principal market at the measurement date under current market conditions (i.e., the exit price). The determination of fair value requires judgment and is based on market information, where available and appropriate. Fair value measurements are categorized into three levels within a fair value hierarchy (Level 1, 2, or 3) based on the valuation inputs used in measuring the fair value, as outlined below.

- Level 1 – Unadjusted quoted market prices in active markets for identical assets or liabilities the Company can access at the measurement date. Bid prices, ask prices or prices within the bid and ask, which are the most representative of the fair value, are used as appropriate to measure fair value. Fair value is best evidenced by an independent quoted market price for the same instrument in an active market. An active market is one where transactions are occurring with sufficient frequency and volume to provide quoted prices on an ongoing basis.

- Level 2 – Quoted prices for identical assets or liabilities in markets that are inactive or observable market quotes for similar instruments, or use of valuation techniques where all significant inputs are observable. Inactive markets may be characterized by a significant decline in the volume and level of observed trading activity or through large or erratic bid/offer spreads. In instances where traded markets do not exist or are not considered sufficiently active, we measure fair value using valuation models.

- Level 3 – Non-observable or indicative prices or use of valuation techniques where one or more significant inputs are non-observable.

Valuation methods and assumptions

Finance lease receivables, finance loan receivables, and borrowings on finance receivables

The assertion that the carrying value of the finance receivables and borrowings approximates fair value requires the use of estimates and significant judgment. The finance receivables securing the borrowings were credit scored based on an internal model that is not used in market transactions. They comprise a large number of transactions with commercial clients in different businesses, are secured by liens on various types of equipment and may be guaranteed by third parties and cross collateralized. The fair value of any receivable would be affected by a potential buyer's assessment of the transaction's credit quality, collateral value, guarantees, payment history, yield, term, documents and other legal matters, and other subjective considerations. Value received in a fair market sale transaction would be based on the terms of the sale, the buyer's views of the economic and industry conditions, the Company's and the buyer's tax considerations, and other factors.

Convertible debentures

The debt component of convertible debentures is recorded at fair value on initial recognition and subsequently carried at amortized cost. The fair market value of the debt component is calculated by discounting the stream of remaining payments at 5.50%, which represents the rate of interest prevailing for instruments of similar terms and risks without the conversion feature.

Derivatives

The fair values of derivatives are determined by the derivative counterparty using the related interest rate swap curves, foreign exchange forward values, intrinsic values and/or the Company's stock price for the total return swaps.

Investments

The fair value through profit and loss ("FVTPL") investments are valued based on bids received in the private market or using valuation techniques and/or inputs that are based on unobservable market data.

Accounts receivable, accounts payable, and accrued liabilities

The carrying value of the accounts receivable, accounts payable, and accrued liabilities approximates their fair value.

The tables below summarize the Company's fair value measurement hierarchy for its financial assets and financial liabilities. There were no transfers between Level 2 and Level 3 during the years presented and there were no significant changes in valuation techniques or the range of significant non-observable inputs used in measuring the Company's Level 3 financial assets and liabilities during the year.

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(unaudited, in thousands of Canadian dollars, except where otherwise noted and per share amounts)

		As at September 30, 2020			
		Level 1	Level 2	Level 3	
	Carrying value	Quoted market price	Observable market inputs	Non-observable market inputs	Total
	$	$	$	$	$
Financial assets					
Assets not carried at fair value					
Cash	**75,633**	**75,633**	—	—	**75,633**
Finance lease receivables	**10,047,333**	—	—	**10,047,333**	**10,047,333**
Finance loans receivables	**98,185**	—	—	**98,185**	**98,185**
Accounts receivable and other assets	**192,477**	—	—	**192,477**	**192,477**
Assets held at fair value					
Derivative financial assets					
Interest rate swaps	**62,712**	—	**62,712**	—	**62,712**
Interest rate caps	**80**	—	**80**	—	**80**
Equity swaps	**873**	—	**873**	—	**873**
Investments classified as FVTPL	**6,322**	—	—	**6,322**	**6,322**
Total financial assets	**10,483,615**	**75,633**	**63,665**	**10,344,317**	**10,483,615**
Financial liabilities					
Liabilities not carried at fair value					
Accounts payable and accrued liabilities	**911,719**	—	—	**911,719**	**911,719**
Borrowings on finance receivables	**10,735,285**	—	—	**10,735,285**	**10,735,285**
Convertible debentures	**153,113**	—	**164,568**	—	**164,568**
Liabilities held at fair value					
Derivative financial liabilities					
Interest rate swaps	**88,962**	—	**88,962**	—	**88,962**
Total financial liabilities	**11,889,079**	—	**253,530**	**11,647,004**	**11,900,534**

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(unaudited, in thousands of Canadian dollars, except where otherwise noted and per share amounts)

	As at December 31, 2019				
		Level 1	Level 2	Level 3	
	Carrying value	Quoted market price	Observable market inputs	Non-observable market inputs	Total
	$	$	$	$	$
Financial assets					
Assets not carried at fair value					
Cash	24,224	24,224	—	—	24,224
Finance lease receivables	11,884,162	—	—	11,884,162	11,884,162
Finance loans receivables	102,812	—	—	102,812	102,812
Accounts receivable and other assets	203,834	—	—	203,834	203,834
Assets held at fair value					
Derivative financial assets					
Interest rate swaps	40,555	—	40,555	—	40,555
Interest rate caps	327	—	327	—	327
Equity Swaps	514	—	514	—	514
Investments classified as FVTPL	6,266	—	—	6,266	6,266
Total financial assets	12,262,694	24,224	41,396	12,197,074	12,262,694
Financial liabilities					
Liabilities not carried at fair value					
Accounts payable and accrued liabilities	924,936	—	—	924,936	924,936
Borrowings on finance receivables	11,892,861	—	—	11,892,861	11,892,861
Convertible debentures	711,791	—	737,917	—	737,917
Liabilities held at fair value					
Derivative financial liabilities					
Interest rate swaps	39,145	—	39,145	—	39,145
Total financial liabilities	13,568,733	—	777,062	12,817,797	13,594,859

17. RESTRUCTURING AND TRANSFORMATION

During the three- and nine-month periods ended September 30, 2020, the Company recorded transformation expenses of $24,213 and $57,871, respectively (three- and nine-month periods ended September 30, 2019 - $34,055 and $62,742, respectively). All amounts have been incurred and paid or expect to be paid by the end of the fourth quarter of 2020 with the exception of accrued operating expenses on closed facilities for $2,603, included in professional fees and other, which will be paid out over the remaining term of the lease.

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(unaudited, in thousands of Canadian dollars, except where otherwise noted and per share amounts)

Transformation and restructuring expenses during the three- and nine-month periods ended September 30:

	Three-month period ended		Nine-month period ended	
	September 30, 2020	September 30, 2019	**September 30, 2020**	September 30, 2019
Nature of expenses	**$**	$	**$**	$
Severances	**8,576**	4,990	**14,347**	9,533
Professional fees and other	**15,637**	29,065	**43,524**	53,209
Total	**24,213**	34,055	**57,871**	62,742

Remaining un-paid liabilities related to transformation expenses.

	As at September 30, 2020	As at December 31, 2019
Nature of expenses	**$**	$
Severances	**6,935**	5,883
Professional fees and other	**16,293**	15,111
Employee bonuses	**—**	14,220
Total	**23,228**	35,214

18. SYNDICATIONS

The following represents the detail of the Company's syndicated assets.

		As at September 30, 2020	As at December 31, 2019
	Classification	**$**	$
Provision for early termination	Accounts payable and accrued liabilities	**11,980**	5,779
Deferred servicing fee	Finance receivables	**900**	1,181

		Three-month period ended		Nine-month period ended	
		September 30, 2020	September 30, 2019	**September 30, 2020**	September 30, 2019
	Classification	**$**	$	**$**	$
Syndication revenue, net	Syndication revenue, net	**15,246**	23,084	**51,666**	62,039
Net book value of assets syndicated	n/a	**600,442**	693,971	**2,192,614**	1,934,459

19. COMPARATIVE FIGURES

Certain comparative figures have been reclassified to conform to the current period's presentation.

20. SUBSEQUENT EVENTS

Increase in Common Share Dividend

On October 27, 2020, the Board approved the increase in the quarterly common share dividend from $0.045 to $0.065 per share.

Termination of Dividend Reinvestment Plan

On October 27, 2020, the Board approved the termination of the DRIP. No future dividends will be eligible for the DRIP.

Share Repurchase

On October 27, 2020, the Board approved of the establishment of a normal course issuer bid to repurchase EFN common shares over the next 12 months - the first year of what is envisioned to be a regular, ongoing program by the Company - subject to TSX approval and the terms and limitations applicable to such bid.