



Quarterhill Inc.

2020 Audited Consolidated
Financial Statements



MANAGEMENT'S RESPONSIBILITY FOR FINANCIAL REPORTING

The accompanying consolidated financial statements of Quarterhill Inc. ("Quarterhill" or the "Company") are the responsibility of management and have been approved by the Board of Directors (the "Board").

The consolidated financial statements have been prepared by management in accordance with the *International Financial Reporting Standards*. Management is responsible for ensuring that these consolidated financial statements, which include certain amounts based on estimates and judgments, reflect the Company's business transactions and financial position in all material respects.

Quarterhill maintains systems of internal accounting and administrative controls of high quality, consistent with reasonable cost. Such systems are designed to provide reasonable assurance that the financial information is relevant, reliable and accurate, and that the Company's assets are appropriately accounted for and adequately safeguarded.

The Board is responsible for ensuring that management fulfills its responsibilities for financial reporting and is ultimately responsible for reviewing and approving the consolidated financial statements. The Board carries out this responsibility through its Audit Committee (the "Committee"). The Committee is appointed by the Board, and all of its members are independent unrelated directors.

The Committee meets periodically with management, as well as with external auditors, to discuss internal controls over the financial reporting process, auditing matters and financial reporting items, to satisfy itself that each party is properly discharging its responsibilities, the consolidated financial statements and the external auditors' report. The Committee reports its findings to the Board for consideration when approving the consolidated financial statements for issuance to the shareholders. The Committee also considers, for review by the Board and approval by the shareholders, the engagement or re-appointment of the external auditors.

The consolidated financial statements have been audited by Ernst & Young LLP, the external auditors on behalf of the shareholders. Ernst & Young LLP has full and free access to the Committee.

March 11, 2021

/s/ Paul Hill

Paul Hill
Chief Executive Officer

/s/ John Rim

John Rim
Chief Financial Officer

Independent auditor's report

To the Shareholders of
Quarterhill Inc.

Opinion

We have audited the consolidated financial statements of **Quarterhill Inc.** and its subsidiaries [the "Group"], which comprise the consolidated statements of financial position as at December 31, 2020 and 2019, and January 1, 2019, and the consolidated statements of income and comprehensive income, consolidated statements of shareholders' equity and consolidated statements of cash flows for the years ended December 31, 2020 and 2019, and notes to the consolidated financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the consolidated financial position of the Group as at December 31, 2020 and 2019, and January 1, 2019 and its consolidated financial performance and its consolidated cash flows for the years ended December 31, 2020 and 2019, in accordance with International Financial Reporting Standards ["IFRS"].

Basis for opinion

We conducted our audit in accordance with Canadian general accepted auditing standards. Our responsibilities under those standards are further described in the *Auditor's responsibilities for the audit of the consolidated financial statements* section of our report. We are independent of the Group in accordance with the ethical requirements that are relevant to our audit of the consolidated financial statements in Canada, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Key audit matter

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the consolidated financial statements of the current period. These matters were addressed in the context of the audit of the consolidated financial statements as a whole, and in forming the auditor's opinion thereon, and we do not provide a separate opinion on these matters. For the matter below, our description of how our audit addressed the matter is provided in that context.

We have fulfilled the responsibilities described in the *Auditor's responsibilities for the audit of the consolidated financial statements* section of our report, including in relation to this matter. Accordingly, our audit included the performance of procedures designed to respond to our assessment of the risks of material misstatement of the consolidated financial statements. The results of our audit procedures, including the procedures performed to address the matter below, provide the basis for our audit opinion on the accompanying consolidated financial statements.



Key audit matter	How our audit addressed the key audit matter
<i>Revenue recognition – Intelligent Transportation Systems</i>	
<p>The Group's Intelligent Transportation Systems segment sells integrated systems with distinct performance obligations which involve the design, manufacturing and installation, maintenance and warranty of long-term projects that can span over periods beyond one year. Revenues for these fixed-price integrated systems contracts are recognized over the progress towards completion of the performance obligations of the contract using a percentage-of-completion method in reference to costs incurred relative to the total estimated costs.</p> <p>For the year ended December 31, 2020, the Group's Intelligent Systems segment recognized \$66 million of revenue, which includes revenues earned from fixed price integrated systems contracts. The determination of the estimated costs to complete for each integrated system fixed price contract that is open as at the reporting date requires significant judgment in order to determine the amount of revenue to be recognized. The Group's policy for revenue recognition together with the related significant accounting estimates and assumptions is described in note 2 of the consolidated financial statements.</p> <p>We determined that revenue recognition for open contracts for the Intelligent Transportation Systems segment is a matter of most significance to the audit due to the significant judgment made by management in determining the estimated costs to complete for fixed priced contracts and, where applicable, the estimation of any loss on a project. Remaining costs to complete including material, labour and subcontracting costs, among others, are unique to each project, resulting in a high degree of auditor judgment, subjectivity and effort in performing procedures related to testing these estimates as of the reporting date.</p>	<p>For fixed price integrated system contracts that were open as of December 31, 2020, our audit procedures included the following:</p> <ul style="list-style-type: none"> • We inspected contractual arrangements including pricing and billing terms, change orders and terms and conditions impacting revenue recognition; • We performed substantive analytical procedures to compare the gross margin at the project level realized in the year to historical gross margin data; • We compared prior period cost estimates to the actual costs incurred in the current period to assess management's ability to estimate the costs to complete a contract; • We tested the completeness and accuracy of the costs incurred to date by vouching underlying supporting documentation related to payroll, third-party costs and inventory cost of material; • We tested, on a sample basis, the estimated costs to complete by analyzing: (i) direct material and labour incurred to date compared to the project scope; (ii) inspecting quotes provided by third-party subcontractors engaged by the Group; and (iii) held discussions with operational personnel to evaluate project status and appropriateness of estimated cost to complete; and • We considered subsequent events after year-end that may require adjustments to revenue recognized.

Other information

Management is responsible for the other information. The other information comprises:

- Management's Discussion and Analysis; and
- The information, other than the consolidated financial statements and our auditor's report thereon, in the Annual Report.



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

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

We obtained Management's Discussion and Analysis prior to the date of this auditor's report. If, based on the work we have performed, we conclude that there is material misstatement of this other information, we are required to report that fact in this auditor's report. We have nothing to report in this regard.

The Annual Report is expected to be made available to us after the date of the auditor's report. If based on the work we will perform on this other information, we conclude there is a material misstatement of other information, we are required to report that fact to those charged with governance.

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

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

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

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

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

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

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

- Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group's internal control.



- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Group to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the Group audit. We remain solely responsible for our audit opinion.

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

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

From the matters communicated with those charged with governance, we determine those matters that were of most significance in the audit of the consolidated financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

The engagement partner on the audit resulting in this independent auditor's report is Kwan-Ho Song.

Toronto, Canada
March 10, 2021

Ernst & Young LLP

Chartered Professional Accountants
Licensed Public Accountants



Consolidated Statements of Income and Comprehensive Income
(in thousands of Canadian dollars, except share and per share amounts)



CONTINUING OPERATIONS	Note	Year ended December 31,	
		2020	2019
Revenues			
Licensing		\$ 78,260	\$ 106,052
Intelligent Transportation Systems		66,266	66,873
		144,526	172,925
Direct cost of revenues			
Licensing		46,205	53,130
Intelligent Transportation Systems		39,463	42,887
		85,668	96,017
Gross profit		58,858	76,908
Operating expenses			
Depreciation of right-of-use assets	8	979	1,305
Depreciation of property, plant and equipment	9	969	1,296
Amortization of intangible assets	10	18,855	23,305
Selling, general and administrative expenses	17	26,868	26,719
Research and development expenses		2,282	2,874
Impairment losses on intangible assets	10	295	115
Special charges	18	1,227	2,448
		51,475	58,062
Results from operations		7,383	18,846
Finance income		(573)	(1,665)
Finance expense		459	740
Foreign exchange (gain) loss		(88)	324
Other income		(1,680)	(869)
Income before taxes		9,265	20,316
Current income tax expense		2,037	8,117
Deferred income tax expense		2,800	1,106
Income tax expense	19	4,837	9,223
Net income from continuing operations		4,428	11,093
Net income from discontinued operations	4	14,255	1,569
Net income		\$ 18,683	\$ 12,662
Other comprehensive loss that may be reclassified subsequently to net income:			
Foreign currency translation adjustment		(7,355)	(11,176)
Comprehensive income		\$ 11,328	\$ 1,486
Income per share	20		
From continuing operations		0.04	0.09
From discontinued operations		0.12	0.01
Income per share - Basic		\$ 0.16	\$ 0.10
From continuing operations		\$ 0.04	\$ 0.09
From discontinued operations		0.12	0.01
Income per share - Diluted		\$ 0.16	\$ 0.10

See accompanying notes to these consolidated financial statements.

Consolidated Statements of Financial Position
(in thousands of Canadian dollars)



As at	Note	December 31, 2020	December 31, 2019	January 1, 2019
Current assets				
Cash and cash equivalents		\$ 135,700	\$ 87,870	\$ 87,029
Short-term investments		5,550	1,550	1,551
Restricted short-term investments		—	—	2,995
Accounts receivable	22	13,747	42,925	14,719
Other current assets		—	108	124
Unbilled revenue	6	13,549	8,965	5,432
Income taxes recoverable		264	137	270
Inventories (net of obsolescence)	7	9,068	8,570	8,114
Prepaid expenses and deposits		8,264	2,242	2,927
		186,142	152,367	123,161
Non-current assets				
Accounts receivable	22	506	3,846	565
Prepaid expenses and deposits		338	—	—
Right-of-use assets, net	8	3,780	4,502	3,972
Property, plant and equipment, net	9	2,783	2,826	3,614
Intangible assets, net	10	59,261	89,534	119,015
Investment in joint venture	11	6,704	5,233	5,203
Deferred income tax assets	19	28,202	32,737	36,948
Goodwill	12	16,093	32,977	34,446
		117,667	171,655	203,763
TOTAL ASSETS		\$ 303,809	\$ 324,022	\$ 326,924
Liabilities				
Current liabilities				
Bank indebtedness	13	\$ —	\$ 4,026	\$ 3,537
Accounts payable and accrued liabilities	14	20,038	26,264	24,644
Income taxes payable		631	203	—
Current portion of lease liabilities	8	1,012	998	1,120
Contingent liabilities	15	—	—	1,265
Current portion of deferred revenue	6	4,800	8,638	6,357
Current portion of long-term debt		—	59	407
		26,481	40,188	37,330
Non-current liabilities				
Deferred revenue	6	2,573	1,513	1,954
Long-term lease liabilities	8	2,747	3,550	2,604
Long-term debt		—	271	236
Deferred income tax liabilities	19	78	3,297	5,905
		5,398	8,631	10,699
TOTAL LIABILITIES		31,879	48,819	48,029
Shareholders' equity				
Capital stock	16	547,537	570,553	570,553
Contributed surplus		46,250	32,011	31,252
Accumulated other comprehensive income		3,581	10,936	22,112
Deficit		(325,438)	(338,297)	(345,022)
		271,930	275,203	278,895
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY		\$ 303,809	\$ 324,022	\$ 326,924

See accompanying notes to these consolidated financial statements.

On behalf of the Board:

/s/Richard Shorkey, Director

/s/Roxanne Anderson, Director

Consolidated Statements of Cash Flows
(in thousands of Canadian dollars)



	Note	Year ended December 31,	
		2020	2019
Cash generated from (used in) operations			
Net income from continuing operations		\$ 4,428	\$ 11,093
Non-cash items			
Stock-based compensation expense	16	1,015	693
Depreciation of right-of-use assets		979	1,305
Interest expense on lease liabilities		223	231
Depreciation and amortization		19,824	24,601
Foreign exchange gain		(359)	(113)
Equity in earnings from joint venture	11	(1,680)	(873)
(Gain) loss on disposal of intangible assets		(1)	206
Impairment losses on intangible assets		295	115
Loss on disposal of assets		4	746
Deferred income tax expense		2,800	1,106
Long-term accounts receivable		—	(85)
Embedded derivatives		190	11
Contingent consideration adjustment		—	(1,042)
Changes in non-cash working capital balances	24	7,478	(29,368)
Cash generated from continuing operations		35,196	8,626
Net cash flows attributable to discontinuing operations		24	3,247
Net cash generated from operating activities		35,220	11,873
Financing			
Dividends paid		(4,441)	(5,939)
Bank indebtedness		(3,654)	685
Payment of lease liabilities		(1,103)	(1,504)
Repayment of long-term debt		(521)	(265)
Repurchase of shares for cancellation	16	(10,622)	—
Exercise of stock options		830	—
Cash used in continuing operations		(19,511)	(7,023)
Net cash flows attributable to discontinuing operations		32	(32)
Net cash used in financing activities		(19,479)	(7,055)
Investing			
Proceeds from disposition of a subsidiary	4	49,400	—
Cash sold on disposition of a subsidiary		(1,825)	—
Purchase of short-term investments		(4,054)	—
Dividends received from joint venture	11	477	513
Proceeds from sale of restricted short-term investments		—	2,904
Proceeds from sale of property, plant and equipment		32	43
Purchase of property and equipment		(1,255)	(1,301)
Purchase of intangible assets		(1,336)	(1,890)
Cash generated from continuing operations		41,439	269
Net cash flows attributable to discontinuing operations		—	(172)
Net cash generated from investing activities		41,439	97
Foreign exchange loss on cash held in foreign currency		(9,350)	(4,074)
Net increase in cash and cash equivalents		47,830	841
Cash and cash equivalents, beginning of		87,870	87,029
Cash and cash equivalents, end of		\$ 135,700	\$ 87,870

See accompanying notes to these consolidated financial statements.

Consolidated Statements of Shareholders' Equity
(in thousands of Canadian dollars)



	Note	Capital Stock	Contributed Surplus	Accumulated Other Comprehensive Income	Deficit	Total Shareholders' Equity
January 1, 2019		\$ 570,553	\$ 31,252	\$ 22,112	\$ (345,022)	\$ 278,895
Net income		—	—	—	12,662	12,662
Other comprehensive loss		—	—	(11,176)	—	(11,176)
Stock-based compensation expense	16	—	759	—	—	759
Dividends declared		—	—	—	(5,937)	(5,937)
December 31, 2019		\$ 570,553	\$ 32,011	\$ 10,936	\$ (338,297)	\$ 275,203
January 1, 2020		\$ 570,553	\$ 32,011	\$ 10,936	\$ (338,297)	\$ 275,203
Net income		—	—	—	18,683	18,683
Repurchase of shares for cancellation		(24,054)	13,432	—	—	(10,622)
Other comprehensive loss		—	—	(7,355)	—	(7,355)
Exercise of options		1,006	(176)	—	—	830
Stock-based compensation expense	16	—	1,015	—	—	1,015
Common shares issued from performance stock units		32	(32)	—	—	—
Dividends declared		—	—	—	(5,824)	(5,824)
December 31, 2020		\$ 547,537	\$ 46,250	\$ 3,581	\$ (325,438)	\$ 271,930

See accompanying notes to these consolidated financial statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Year ended December 31, 2020 and 2019

(in thousands of Canadian dollars, except share and per share amounts, unless otherwise stated)

1. NATURE OF BUSINESS

Quarterhill Inc. ("Quarterhill" or the "Company"), formerly "Wi-LAN Inc." ("WiLAN"), is a Canadian company incorporated and domiciled in Canada. The address of the Company's registered office is 25 King St. W Suite 1101, Toronto, Ontario, M5L 2A1. The Company's shares are listed under the symbol "QTRH" on the Toronto Stock Exchange (the "TSX") and the United States OTCQX Best Market (the "OTCQX") under the symbol "QTRHF". Quarterhill is focused on the acquisition, management and growth of companies in the intelligent transportation systems ("ITS") and innovation and licensing industries, which correspond with the Company's operating segments identified as Licensing and Intelligent Transportation Systems. On May 15, 2020, the Company sold its investment in VIZIYA Corp., which represented the Enterprise Software segment, and has been presented as a discontinued operation within the Company's consolidated financial statements and further disclosed in Note 4, Discontinued Operations.

2. SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation

Statement of compliance

These consolidated financial statements of the Company were prepared in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB"). These are the Company's first annual consolidated financial statements prepared in accordance with IFRS and IFRS 1, "First-Time Adoption of IFRS." Subject to certain transition elections disclosed in Note 27, the Company has consistently applied the same accounting policies in its opening IFRS consolidated statement of financial position at January 1, 2019, and throughout all periods presented as if these policies had always been in effect.

Until the year ended December 31, 2019, the Company's consolidated financial statements were prepared in accordance with accounting principles generally accepted in the United States of America ("US GAAP"). An explanation of how the transition to IFRS has affected the reported financial position, financial performance and cash flows of the Company is provided in Note 27. This note includes reconciliations of equity and comprehensive income of the comparative periods and of equity at the date of transition reported under US GAAP to IFRS for those periods.

These consolidated financial statements were authorized for issue by the Board of Directors on March 10, 2021.

Basis of measurement

These consolidated financial statements have been prepared on a historical cost basis, except for certain financial instruments that are measured at fair value on a recurring basis, as explained in the accounting policies below, and certain intangible assets (patent licenses) that the Company elected to record at the IFRS transition date of January 1, 2019 at the US GAAP revaluation of its previously impaired patent licenses, adjusted for any subsequent changes to depreciation based on differences between US GAAP and IFRS, as these assets' deemed cost.

Basis of consolidation

These consolidated financial statements include the accounts of the Company and its wholly owned subsidiaries. The Company also holds, through one of its subsidiaries, a 50% joint venture ownership interest in Xuzhou-PAT Control Technologies Limited ("XPCT"), which is accounted for using the equity method and includes only the Company's net investment and equity in earnings of the joint venture. Consolidation of a subsidiary begins when the Company obtains control over the subsidiary and ceases when the Company ceases to control the subsidiary. All intercompany transactions and balances have been eliminated in these consolidated financial statements.

Functional and presentation currency

The consolidated financial statements are presented in Canadian dollars, which differs from the Company's functional currency of US dollars.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Year ended December 31, 2020 and 2019

(in thousands of Canadian dollars, except share and per share amounts, unless otherwise stated)

On January 1, 2020, the Company changed its presentation currency from US dollars to Canadian dollars to facilitate comparisons with its industry peers, and better meet the needs of the Canadian investor. This change was applied retrospectively to all periods presented in these consolidated financial statements.

The Company follows the requirements as prescribed in IAS 21, "The Effects of Changes in Foreign Exchange Rates" to translate to the presentation currency. The assets and liabilities of the consolidated entity are translated to Canadian dollars at the exchange rate as at the reporting date, and the income and expenses are translated to Canadian dollars at the monthly average exchange rates of the reporting period. Foreign currency differences arising from the translation are recognized in other comprehensive income ("OCI").

For the prior year comparative periods assets and liabilities presented and previously reported in US dollars have been translated to Canadian dollars using end exchange rates of 0.7673 (December 31, 2019) and 0.7346 (January 1, 2019). Consolidated statements of income and other comprehensive income previously reported for the year ended December 31, 2019 have been translated using average quarterly exchange rates of 0.7522, 0.7476, 0.7573, and 0.7576 for the three month periods ending March 31, 2019, June 30, 2019, September 30, 2019 and December 31, 2019 respectively. Retained earnings and historical equity transactions existing as at January 1, 2019 were translated at the exchange rate at that date of 0.7346.

Estimates, assumptions, and judgments

The preparation of these consolidated financial statements in conformity with IFRS requires management to make judgments, estimates and assumptions that affect the reported amounts of revenues, expenses, assets, liabilities and the disclosure of contingent assets and liabilities at the reporting date. Uncertainty about these assumptions and estimates could result in adjustments to the carrying amount of an asset or liability or the reported amount of revenue and expense in future periods. Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimates are revised and in any future periods affected.

Key estimates, including judgments and uncertainties

Revenue recognition

Contract revenue, contract costs, contract liabilities and contract assets relating to the Intelligent Transportation Systems segment are based on estimates and judgments used in determining the progress of a contract. Estimates include amounts derived to measure the progress of the contract. Progress towards completion is measured by comparing the actual costs incurred to the total estimated costs for the contract. In determining the estimated costs to complete the contracts, assumptions and estimates are required to evaluate issues related to schedule, material and labour costs, changes in contract scope and subcontractor costs. Due to the nature of project contracts, estimates may change significantly between accounting periods. Changes in estimates are reflected in the period in which the circumstances that gave rise to the change became known and affect the Company's revenue, contract assets, and contract liabilities.

Leases

Management uses judgment in determining whether a contract contains a lease, the interest used to discount the present value of fixed payments in accounting for the lease liability and corresponding right-of-use ("ROU") asset, and in determining whether it is likely that a lease term will be extended.

Asset impairments for non-financial assets and impairment reversals

The Company's estimate of the recoverable amount for the purpose of impairment testing requires management to make assumptions regarding estimates of the present value of future cash flows including growth opportunities, economic risk, and the discount rate. These same assumptions are also used when assessing recoverability of impairments previously recognized.

Income taxes and deferred taxes

The Company is subject to income taxes in Canada and other foreign jurisdictions. The calculation of income taxes in many cases, however, requires significant judgment in interpreting tax rules and regulations. The Company's tax filings are subject to audits which could materially change the amount of current and deferred income taxes and liabilities. Additionally, estimation of the income tax provision includes evaluating the

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Year ended December 31, 2020 and 2019

(in thousands of Canadian dollars, except share and per share amounts, unless otherwise stated)

recoverability of deferred tax assets based on the assessment of the Company's ability to use the underlying future tax deductions before they expire against future taxable income. The assessment is based on existing tax laws, estimates of future profitability and tax planning strategies. If the future taxable results of the Company differ significantly from those expected, the Company would be required to increase or decrease the carrying value of the deferred tax assets with a potentially material impact on the Company's consolidated statements of financial position and consolidated statements of income and comprehensive income. The carrying amount of deferred tax assets is reassessed at each reporting period and reduced to the extent that it is no longer probable that sufficient taxable income will be available to utilize all or part of the deferred tax assets. Unrecognized deferred tax assets are recognized to the extent that it is more likely than not that taxable income will be available against which deferred tax assets can be utilized.

Financial assets

Assessments about the recoverability of financial assets, including accounts receivable and unbilled revenue, require judgment as to whether a loss event has occurred and estimate of the amounts and timing of future cash flows.

Business Combinations

The Company uses the acquisition method of accounting for business combinations. The cost of an acquisition is measured as the consideration transferred at fair value at the acquisition date. The determination of fair values for the acquired intangible assets involves the use of discounted cash flow analyses. Any contingent consideration to be transferred by the Company is recognized at fair value at the acquisition date. The Company determines that a pre-acquisition contingency is probable in nature and estimable as of the acquisition date and records its best estimate for the contingency as part of the purchase price allocation. The Company continues to gather information and evaluates any pre-acquisition contingencies throughout the measurement period and makes adjustments as necessary to the purchase price allocation. Changes in fair value of contingent consideration outside of the measurement period are measured at fair value, with changes in fair value recognized in profit or loss. Acquisition-related costs are expensed as incurred. Any excess of the fair value of the consideration transferred over the fair value of net identifiable assets acquired, at acquisition date, is recorded as goodwill.

Foreign Currency Transactions

Monetary assets and liabilities denominated in foreign currencies are translated into the applicable functional currency of the entity at exchange rates prevailing at the consolidated statement of financial position date. Revenue and expenses are translated at the average rate for the period. The gains and losses from foreign currency denominated transactions are included in foreign exchange gain/loss in the consolidated statement of income and comprehensive income.

Cash and Cash Equivalents

Cash and cash equivalents consist of cash in banks and highly liquid investments with original terms to maturity at the date of acquisition of less than three months.

Short-Term Investments

Short-term investments are accounted for at amortized cost using the effective interest rate method. Short-term investments comprise guaranteed investment certificates with original maturities of one year or less at the date of investment and their carrying value approximates their fair value.

Restricted Short-Term Investments

Restricted short-term investments are amounts held specifically as collateral for bank guarantees that the Company has entered into for security against potential procedural costs pursuant to a court order regarding patent infringement whereby the Company is the plaintiff. As at December 31, 2020, and December 31, 2019, the Company had no bank guarantees outstanding that required collateral.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Year ended December 31, 2020 and 2019

(in thousands of Canadian dollars, except share and per share amounts, unless otherwise stated)

Unbilled Revenue

Unbilled revenue includes unbilled amounts typically resulting from sales under long-term contracts when the cost-to-cost method of revenue recognition is utilized and revenue recognized exceeds the amount billed to the customer accounted for under IFRS 15, "Revenue from Contracts with Customers" ("IFRS 15"). At any given period-end, a large portion of the balance in this account represents the accumulation of labour, materials and other costs that have not been billed due to timing, whereby the accumulation of each month's costs and earnings is administratively billed in subsequent months. Also included in the account are amounts that will become billable according to contract terms, which usually require the consideration of the passage of time, achievement of milestones or completion of the project.

Inventories

Inventories are measured at the lower of cost or net realizable value. The cost of inventories is determined on the weighted average basis. Costs comprises all costs of purchase, costs of conversion and other costs incurred in bringing the inventories to their present location and condition.

Property Plant and Equipment

Property, plant and equipment are measured at cost less accumulated depreciation and accumulated impairment losses, if any. Costs include the purchase price and the directly attributable costs required to bring the asset to the condition necessary for the asset to be capable of operating in the manner intended by management. When components of an item of property, plant and equipment have different useful lives, they are accounted for as separate items of property, plant and equipment and depreciated accordingly. The cost of replacing or repairing a component of an item is recognized in the carrying amount of the item if it is probable that future economic benefits will occur and the cost can be measured reliably. The costs of routine maintenance are recognized in profit or loss as incurred. Depreciation is calculated on the straight-line basis over the estimated useful lives of the assets as follows:

Leasehold improvements	term of the lease
Computer equipment and software	3 years
Furniture and fixtures	5 years
Machinery and equipment	4-7 years
Building	20 years

The Company reviews the residual value, useful lives and depreciation methods used on an annual basis and, where revisions are required, the Company applies such changes in estimates on a prospective basis.

Intangible Assets

Intangible assets consist of finite-lived patents, developed software, customer relationships, brand and backlog.

Patents include patents and patent rights (hereinafter, collectively "patents"), are purchased separately, and are carried at cost less accumulated amortization and impairments.

Developed software, customer relationships, and brand were acquired through business acquisitions and are recognized at fair value as determined on the acquisition date less accumulated amortization and impairments.

Fair value of the developed software and brand is determined based on the present value of expected future cash flows.

Customer relationships represent acquired customer relationships with customers that are capable of being separated from the acquired entity and being sold, transferred, licensed, rented or exchanged. These customer relationships are initially recorded at their fair value based on the present value of expected future cash flows.

Amortization is calculated on a straight-line basis over the estimated useful lives of the intangible assets as follows:

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Patents	up to 20 years
Developed software	5 years
Customer relationships and backlog	7 years
Brand	7 years

The Company continually evaluates the remaining estimated useful life of its finite intangible assets to determine whether events and circumstances warrant a revision to the remaining period of amortization and are accounted for prospectively from the date of the change.

Impairment of Non-Financial Assets

The carrying amounts of non-financial assets, excluding inventories, deferred income tax assets, and contract assets are reviewed for impairment at each reporting date, or whenever events or changes in circumstances indicate the carrying amounts may not be recoverable. If there are indicators of impairment, a review is undertaken to determine whether the carrying amounts are in excess of their recoverable amounts. Goodwill is tested at least annually, at year-end, for impairment. For the purpose of impairment testing, assets that cannot be tested individually are grouped together into the smallest group of assets that generates cash inflows, the cash-generating unit ("CGU"), from continuing use that are largely independent of the cash inflows of other assets or groups of assets.

The recoverable amount of an asset or CGU is the greater of its value in use and its fair value less costs to sell. The value in use is determined by the cash flows expected to arise from the CGU discounted using a pre-tax discount rate that reflects the current market assessments of the time value of money and asset-specific risk. In determining fair value less costs of disposal, an appropriate valuation model is used. These calculations are corroborated by the use of valuation multiples, quoted share prices and other available fair value indicators. An impairment loss is recognized if the carrying amount of an asset or its CGU exceeds its estimated recoverable amount. Impairment losses are recognized in profit and loss. Impairment losses recognized in respect of CGUs are allocated first to reduce the carrying amount of any goodwill allocated to the CGUs, and then to reduce the carrying amount of the other assets in the CGUs.

For non-financial assets that have been previously impaired, excluding goodwill, an assessment is made at each reporting date as to whether there is any indication that previous impairment losses may no longer exist or may have decreased. If such an indication exists, the Company estimates the recoverable amount of the asset or CGU. A previously recognized impairment loss is reversed only if there has been a change in the assumptions used to determine the asset's recoverable amount since the impairment loss was recognized. The impairment loss to be reversed in the consolidated statements of income and comprehensive income is limited to the recoverable amount, but not beyond the carrying amount, net of depreciation or amortization, that would have arisen if the prior impairment loss had not been recognized.

Investment in Joint Venture

The Company's joint arrangement has been determined to be a joint venture based on the Company's assessment of its contractual rights and obligations. Joint ventures are accounted for using the equity method whereby the investments are initially recorded at cost. The investment is increased or decreased to reflect the Company's proportionate share of the post-acquisition earnings or losses and equity movements of the investee, after adjustments to align the accounting policies with those of the Company. When the Company's share of losses exceeds its interest in an equity-accounted investee, the carrying amount of that interest, including any long-term investments, is reduced to nil, and the recognition of further losses is discontinued except to the extent that the Company has an obligation or has made payments on behalf of the investee.

Goodwill

Goodwill represents the excess of the cost of an acquisition over the fair value of the Company's share of the net identifiable assets of the acquired business at the date of acquisition. Goodwill is presented separately on the consolidated statement of financial position and is subsequently measured at cost less any accumulated impairment losses.

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Revenue Recognition

The Company recognizes revenue, at an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services, when control of the promised goods or services is transferred to the customer. Revenue represents the amount that the Company expects to receive for products and services in its contracts with customers, net of sales taxes. The cumulative effects of revisions to contract revenues and estimated completion costs are recorded in the accounting period in which the amounts become evident and can be reasonably estimated. These revisions can include such items as the effects of change orders and claims, warranty claims, liquidated damages or other contractual penalties and adjustments for contract closeout settlements. The Company reports revenue as either Licensing or Intelligent Transportation Systems, which corresponds with its operating segments. The following paragraphs describe the specific revenue recognition policies for each of the Company's significant types of revenue by segment.

Licensing segment

Right-to-use

Patent licenses are considered a promise to provide the right to use specific intellectual property to the customer. Revenue from contracts containing no sales or usage-based royalties is recognized when the patent right is effective, with the exception of certain instances where licensing rights applicable to future portfolio licenses are granted. In these arrangements, revenue on these specific rights would be recognized over the term of the applicable rights. Payment is generally either due immediately or within 30 days.

Sales or usage-based royalty

Revenue from contracts containing a sales or usage-based royalty is recognized only when the associated sale or usage occurs or the performance obligation to which the royalty has been allocated has been satisfied. Customers generally report their royalty obligations one quarter in arrears and, accordingly, the Company estimates the expected royalties to be reported for an accounting period, with an adjustment for actual royalties reported in the following financial reporting period. Payment is due upon submission of the royalty report.

Intelligent Transportation Systems segment

Contracted projects

The majority of sales of integrated systems are delivered as contracted projects with contract terms of less than one year to more than five years. The customer controls all of the work in progress as intelligent transportation systems are being developed and installed. The Company's contract types include fixed price and time and materials contracts. The transaction price includes amounts expected to be received in exchange for the goods or services plus any contract amendments that are expected to be received. Payment terms are based on completion of milestones throughout the project life for fixed price contracts and monthly for time and materials projects.

Many of these projects have distinct performance obligations typically encompassing one or more of installation, maintenance and warranty. A contract's transaction price is allocated to each distinct performance obligation using the best estimate of the standalone selling price of each distinct good or service in the contract. The primary method used to estimate standalone selling price is the expected cost plus margin approach. Revenue is recognized when or as the performance obligation is satisfied.

Installations

Revenue for the installation obligations of fixed price contracts is recognized over time using the input method based on costs incurred relative to the total expected costs to complete each project. Control is transferred to the customer over time as the customer controls the work in progress and revenue earned from the contract is recognized over time based on the extent of progress towards completion of the performance obligation. The Company reviews and updates the contract-related estimates regularly. Determining the contract costs and estimates to complete requires significant judgment. Adjustments are recognized in profit on contracts under the cumulative catch-up method in the period the adjustment is identified. If the Company anticipates the estimated remaining costs to completion will exceed the value allocated to the performance obligation, the resulting loss is recognized immediately.

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Maintenance

The maintenance obligation of contracts with multiple performance obligations is recognized over the term of the contract as control is transferred to the customer. Stand-alone maintenance service contracts are typically time and materials, but some are fixed price, for which revenue is recognized in the same manner as fixed price installations, over time using the input method based on costs incurred relative to the total expected costs to complete each project. For time and materials contracts, labour and material rates are established within the contract. Revenues from time and materials contracts are recognized as control is transferred to the customer based on cost plus margin. These services are billed on a monthly basis and collected shortly thereafter.

Warranty

Revenue from warranty obligations is recognized over time based on time lapsed as this best represents the value transferred to the customer.

Product sales

Product sales revenue is recognized when control transfers under the term of the enforceable contract. Customers are billed when transfer of control occurs and payments are typically due within 30 days.

Financial Instruments

Recognition and initial measurement

Financial assets and liabilities, with the exception of accounts receivable and unbilled revenues that do not have a significant financing component, are initially recognized at fair value plus or minus directly attributable transaction costs as appropriate, except for financial assets at fair value through profit and loss ("FVTPL"), for which transaction costs are expensed. Accounts receivable and unbilled revenues that do not have a significant financing component are initially measured at the transaction price determined in accordance with IFRS 15. Accounts receivable are recognized on the date that they originate and all other financial instruments are recognized when the Company becomes party to the contractual provisions of the instrument.

Financial assets

The classification of financial assets depends on the business model for managing the financial assets and the associated contractual cash flows. A financial asset is measured at amortized cost if it is held within a business model whose objective is to hold assets to collect contractual cash flows, and its contractual terms give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

The Company's financial assets consist of cash and cash equivalents, short-term investments, restricted short-term investments, accounts receivable and unbilled revenue: all are classified as amortized cost.

Financial liabilities

The Company determines the classification of its financial liabilities at initial recognition. The Company's financial liabilities consist of bank indebtedness, accounts payable and accrued liabilities, dividends payable, contingent liabilities and long-term debt. Bank indebtedness, accounts payable and accrued liabilities, dividends payable and long-term debt are classified as amortized cost and contingent liabilities are classified as FVTPL.

Subsequent measurement

Subsequent to initial recognition, financial assets and liabilities classified as amortized cost are measured using the effective interest method, less, in the case of financial assets, any impairment. Interest income and expense, foreign exchange gains and losses, impairment and any gain or loss on de-recognition are recognized in profit and loss. Contingent liabilities are reported at fair value and the gain or loss recognized in profit and loss as a special charge.

De-recognition

The Company de-recognizes a financial asset when the rights to receive cash flows from the financial asset have expired or have been transferred and the Company has transferred substantially all risks and rewards of ownership.

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The Company de-recognizes a financial liability when the contractual obligations are discharged, canceled or expire.

Derivative financial instruments

The Company may use derivative financial instruments to reduce exposure to fluctuation in foreign currency exchange rates. The Company may enter into foreign exchange contracts to hedge anticipated cash flows denominated in a foreign currency. Embedded derivatives are separated from the host contract and accounted for separately if the host contract is not a financial asset and certain criteria are met.

The Company has elected not to apply hedge accounting to derivative contracts; as such, these derivative financial instruments are recorded at fair value upon recognition and on a recurring basis, with subsequent changes in fair value recorded in profit or loss during the period of change. Derivatives are reported as other current assets when they have a positive fair value and as other current liabilities when they have a negative fair value.

Fair Value Measurement of Financial Instruments

The Company uses various valuation techniques and assumptions when measuring fair value of its financial assets and financial liabilities. The Company utilizes market data or assumptions that market participants would use in pricing the asset or liability, including assumptions about risk and the risks inherent in the inputs to the valuation technique.

The Company's fair value hierarchy prioritizes the inputs to valuation techniques used to measure fair value. The three levels of the fair value hierarchy are:

Level 1 – Inputs are based on quoted prices (unadjusted) in active markets that are accessible at the reporting date for identical assets or liabilities;

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

Level 3 – Inputs are based on prices or valuation techniques that are both unobservable and significant to the overall fair value measurement.

The following methods and assumptions were used to estimate the fair value of each class of financial instruments for which it is practicable to estimate that value.

Derivative financial instruments

The fair value of embedded derivatives is measured using a market approach, based on the difference between the quoted forward exchange rate as of the contract date and quoted forward exchange rate as of the reporting date. The fair value of forward exchange contracts is determined using the quoted forward exchange rates at the reporting date.

Contingent liabilities

Contingent liabilities are carried at fair value, which is calculated using management estimates or, where appropriate, a Monte Carlo simulation model.

The carrying amount of the Company's other financial assets and liabilities, including cash and cash equivalents, short-term investments, restricted short-term investments, accounts receivable, unbilled revenue, accounts payable and accrued liabilities, and dividend payable approximate their fair value due to the short-term maturity of these items. The fair value of the bank indebtedness and long-term debt approximates the carrying amount since these debt instruments have floating interest rates.

Impairment of Non-Derivative Financial Assets

The Company applies the IFRS 9, "Financial Instruments" simplified approach to measuring expected credit losses, which uses a lifetime expected loss allowance for all accounts receivable and contract assets. Lifetime expected credit losses are estimated based on factors such as the Company's past experience of collecting

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payments, observable changes in national or local economic conditions that correlate with default on receivables, and financial condition of the borrower. Financial assets are written off when there is no reasonable expectation of recovery.

Research and Development

Research costs are included in the consolidated statement of income and comprehensive income in the periods in which they are incurred, net of earned investment tax credits. Software development costs are deferred and amortized when technological feasibility has been established, or otherwise are expensed as incurred.

Warranties

The Company records the estimated costs of product warranties at the time revenue is recognized. Warranty obligation arises from the Company having to replace goods and/or services that have failed to meet required customer specifications due to breakdown or error related to product or workmanship. The Company's warranty obligations are affected by product failure rates, differences in warranty periods, regulatory developments with respect to warranty obligations in the countries in which the Company carries on business, freight expense and material usage and other related repair costs.

The Company's estimates of costs are based upon historical experience, expectations of future return rates and unit warranty repair costs. If the Company experiences increased or decreased warranty activity or increased or decreased costs associated with servicing those obligations, revisions to the estimated warranty liability are recognized in the reporting period when such revisions are made.

Financing Costs

Financing costs are composed of borrowing costs related to short- and long-term debt and the unwinding of the discount on provisions.

Leases

At inception of a contract, the Company assesses whether a contract is, or contains, a lease based on whether the contract conveys the right to control the use of an identified asset for a period of time in exchange for consideration. The Company recognizes a ROU asset and a lease liability at the lease commencement date, which is the date the leased asset is available for use. The Company has elected not to separate lease and non-lease components and instead treats them all as lease payments and a single lease component.

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 interest rate implicit in the lease or, if that rate cannot be readily determined, the Company's incremental borrowing rate. The incremental borrowing rate is the rate that the Company would have to pay to borrow the funds necessary to obtain an asset of similar value to the ROU asset in a similar economic environment with similar terms, security and conditions. The lease term includes periods covered by an option to extend if the Company is reasonably certain to exercise that option. The lease liability is measured at amortized cost using the effective interest method. The lease liability is remeasured when there is a change in future lease payments arising from a change in the Company's estimate of the amount expected to be payable under a residual value guarantee, or if the Company changes its assessment of whether it will exercise a purchase, extension or termination option. When the lease liability is remeasured, a corresponding adjustment is made to the carrying amount of the ROU asset unless it has been reduced to zero. Any further reduction in the lease liability is then recognized in profit or loss.

The ROU asset is initially measured based on the initial 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 ROU assets are depreciated over the shorter of the lease term and the useful life of the underlying asset using the straight-line method as this most closely reflects the expected pattern of the consumption of the future economic benefits. In addition, the ROU asset can be periodically reduced by impairment losses, if any, and adjusted for certain re-measurements of the lease liability.

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A lease modification will be accounted for as a separate lease if the modification increases the scope of the lease and if the consideration for the lease increases by an amount commensurate with the stand-alone price for the increase in scope. For a modification that is not a separate lease or where the increase in consideration is not commensurate, at the effective date of the lease modification, the Company will remeasure the lease liability using the Company's incremental borrowing rate on the date of modification, when the rate implicit to the lease is not readily available, with a corresponding adjustment to the ROU asset.

The lease payments associated with short-term and low-value leases are recognized as an expense on a straight-line basis over the lease term as the Company has elected the relevant practical expedients. Short-term leases are those with a lease term of 12 months or less. Low-value asset leases are those leases where the asset being leased when new has a value of less than \$10,000 US dollars. .

Segment Reporting

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

Income Taxes, Deferred Taxes and Investment Tax Credits

Income taxes comprise current and deferred income taxes. Income taxes are recognized in the consolidated statements of income and comprehensive income, except to the extent that they relate to items recognized directly in equity or in OCI, in which case, the income taxes are also recognized directly in equity or in OCI.

Current income taxes are the expected taxes payable on the taxable income for the year, using income tax rates enacted or substantively enacted, at the end of the reporting period, and any adjustment to income taxes payable in respect of previous years.

Deferred income tax assets and liabilities are determined based on the difference between the accounting and tax bases of the assets and liabilities and measured using the enacted tax rates that are expected to be in effect when the differences are estimated to be reversed. The realization of deferred income tax assets is dependent upon the generation of sufficient future taxable income during the periods prior to the expiration of the associated tax attributes. The carrying amount of deferred tax assets is reviewed at each reporting date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred tax asset to be used. Unrecognized deferred tax assets are reassessed at each reporting date and are recognized to the extent that it has become probable that future taxable profits will allow the deferred tax asset to be recovered.

The Company is also engaged in scientific research and experimental development giving rise to investment tax credits that may be available to reduce future taxes payable in certain jurisdictions. In calculating income taxes and investment tax credits, consideration is given to factors such as current and future tax rates in the different jurisdictions, non-deductible expenses, qualifying expenditures and changes in tax law. In addition, management makes judgments on the ability of the Company to realize these investment tax credits reported as assets based on its estimations of amounts and timing of future taxable income and future cash flows in the related jurisdiction.

Discontinued Operations

A discontinued operation is a component of the Company's business, the operations and cash flows of which can be clearly distinguished from the rest of the Company, and either (a) represents a separate major line of business or geographic area of operations; (b) is part of a single coordinated plan to dispose of a separate major line of business or geographic area of operations; or (c) is a subsidiary acquired exclusively with a view to resale. 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.

Discontinued operations are presented separately from continuing operations in the consolidated statements of income and comprehensive income and consolidated statements of cash flows for all periods presented.

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Government Grants

The Company recognizes government grants when there is reasonable assurance that the Company will comply with the corresponding conditions attached to the grant and that the grant will be received. Government grants are recognized in the consolidated statements of income and comprehensive income on a systematic basis over the periods in which the Company recognizes as expenses the related costs for which the grants are intended to compensate and are deducted from the related expense.

3. FUTURE ACCOUNTING PRONOUNCEMENTS

Listed below are the standard, amendments, and interpretations that the Company reasonably expects to be applicable at a future date and intends to adopt when they become effective.

Classification of Liabilities as Current or Non-current (Amendments to IAS 1)

In January 2020, the IASB issued amendments to IAS 1, "Presentation of Financial Statements" to clarify that the classification of liabilities as current or non-current should be based on rights that are in existence at the end of the reporting period and is unaffected by expectations about whether or not an entity will exercise their right to defer settlement of a liability. The amendments further clarify requirements for classifying liabilities an entity will or may settle by issuing its own equity instruments. These amendments are effective for annual reporting periods beginning on or after January 1, 2023, with earlier application permitted. The adoption of these amendments is not expected to have a significant impact on the consolidated financial statements.

Onerous Contracts – Cost of Fulfilling a Contract (Amendments to IAS 37)

IAS 37, "Provisions, Contingent Liabilities and Contingent Assets" has been revised to incorporate amendments issued by the IASB in May 2020. The amendments specify which costs an entity includes in determining the costs of fulfilling a contract for the purpose of assessing whether the contract is onerous. The amendments are effective for annual reporting periods beginning on or after January 1, 2022. Earlier application is permitted. The Company is currently assessing the impact of these amendments.

Interest Rate Benchmark Reform – Phase 2 (Amendments to IFRS 9, IAS 39, IFRS 7, IFRS 4 and IFRS 16)

IFRS 9, "Financial Instruments," IAS 39, "Financial Instruments: Disclosure," IFRS 4, "Insurance Contracts," and IFRS 16, "Leases" have been revised to incorporate amendments issued by the IASB in August 2020. The amendments provide relief to accounting for the modifications required by the interest rate benchmark reform and hedge accounting. In addition, the amendments to IFRS 7 require additional disclosure related to interest rate benchmark reform. The amendments are effective for annual periods beginning on or after January 1, 2021. Earlier application is permitted. The Company is currently assessing the impact of these amendments.

4. DISCONTINUED OPERATIONS

On May 15, 2020, the Company sold its investment in VIZIYA Corp. and its related entities ("VIZIYA") for \$49,400. VIZIYA was acquired in May 2017 and represented the Company's Enterprise Software segment. The Company's results for the prior fiscal period reported throughout these consolidated financial statements have been adjusted to reflect continuing operation results and figures with respect to these discontinued operations. As a result of the sale, the Company recognized the following gain on disposition in the consolidated statement of income and comprehensive income.

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Gain on sale of VIZIYA

Gross cash proceeds of sale	\$	49,400
Less, transaction costs		(32)
Net cash proceeds of sale		49,368
Net assets disposed		(32,827)
Cumulative exchange gain on translating foreign operations reclassified from equity		1,172
Gain on disposal, before tax	\$	17,713

The results of the discontinued operations are presented below for the following periods:

	Year ended December 31,	
	2020	2019
Revenues	\$ 6,132	\$ 21,884
Direct cost of revenues	1,211	2,023
Gross profit	4,921	19,861
Operating expenses	7,309	18,981
Results from operations	(2,388)	880
Other expenses	104	49
Income tax recovery	(593)	(738)
(Loss) income from discontinued operations	(1,899)	1,569
Gain on disposal, before tax	17,713	—
Deferred income tax expense	1,559	—
Net income from discontinued operations	\$ 14,255	\$ 1,569

5. FINANCIAL INSTRUMENTS

Derivatives consists of the embedded derivative portion of the unearned revenue of US dollar denominated sales contracts in the Company's Canadian, Chilean and Mexican subsidiaries and foreign exchange forward contracts. The fair value of embedded derivatives is measured using a market approach, based on the difference between quoted forward exchange rates as of the contract date and quoted forward exchange rates as of the reporting date. Contingent liabilities are carried at fair value, which is calculated using management estimates or, where appropriate, a Monte Carlo simulation model. The carrying amount of the Company's other financial assets and liabilities, including cash and cash equivalents, short-term investments, restricted short-term investments, accounts receivable, unbilled revenue, bank indebtedness, accounts payable and accrued liabilities, and long-term debt approximate, their fair value due to the short-term maturity of these items. The fair value of the bank indebtedness and long-term debt approximates the carrying amount since these debt instruments have floating interest rates.

Inputs used to calculate the fair value of derivative financial instruments and long-term debt are classified as Level 2 inputs, inputs used to calculate contingent liabilities are classified as Level 3 inputs, and inputs for all other financial instruments for which fair value approximates carrying value are classified as Level 1 inputs.

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6. UNBILLED REVENUE AND DEFERRED REVENUE

Significant changes in unbilled revenue and deferred revenue balances during the year ended December 31, 2020 are as follows:

As at	December 31, 2020	December 31, 2019	\$ Change	January 1, 2019
Unbilled revenue	\$ 13,549	\$ 8,965	\$ 4,584	\$ 5,432
Deferred revenue - current	(4,800)	(8,638)	3,838	(6,357)
Deferred revenue - non-current	(2,573)	(1,513)	(1,060)	(1,954)
Net contract assets (liabilities)	\$ 6,176	\$ (1,186)	\$ 7,362	\$ (2,879)

Revenue recognized for the year ended December 31, 2020 that was included in deferred revenue at the beginning of the year was \$5,784 (2019 - \$5,226).

7. INVENTORIES

As at	December 31, 2020	December 31, 2019	January 1, 2019
Raw materials	\$ 1,392	\$ 1,182	\$ 992
Original equipment manufacturer materials	4,001	3,948	4,258
Work in process	1,571	1,291	1,108
Finished goods	2,104	2,149	1,756
	\$ 9,068	\$ 8,570	\$ 8,114

During the year, inventories expensed within direct cost of revenues were \$18,126 (2019 - \$18,483). Write-downs of inventory that were included in direct cost of revenues for the year were \$169 (2019 - \$296). Reversals of write-downs recognized during the year were \$101 (2019 - \$nil).

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8. RIGHT-OF-USE ASSETS AND LEASE LIABILITIES

The Company has leases for corporate offices, production facilities, and certain equipment. These leases have remaining lease terms ranging from 6 months to 8.3 years, some of which include options to extend the leases for up to 10 years or to terminate the lease with notice periods of 90 days to 6 months or at predetermined dates as specified within the lease contract. The Company has classified the assets related to these leases as right-of-use assets and the liabilities associated with the future lease payments under these leases as lease liabilities. The weighted average incremental borrowing rate applied to these lease liabilities at initial recognition on January 1, 2019 was 5.45%.

The following table provides details of changes in the Company's lease assets:

	Buildings	Office Equipment	Total
Cost			
Balance, January 1, 2019	\$ 3,939	\$ 33	\$ 3,972
Additions	2,128	—	2,128
Foreign currency translation	(213)	(1)	(214)
Balance, December 31, 2019	5,854	32	5,886
Additions	407	—	407
Disposals	(348)	—	(348)
Foreign currency translation	(14)	(1)	(15)
Balance, December 31, 2020	\$ 5,899	\$ 31	\$ 5,930
Accumulated Depreciation			
Balance, January 1, 2019	\$ —	\$ —	\$ —
Additions	1,408	15	1,423
Foreign currency translation	(39)	—	(39)
Balance, December 31, 2019	1,369	15	1,384
Additions	997	13	1,010
Disposals	(158)	—	(158)
Foreign currency translation	(85)	(1)	(86)
Balance, December 31, 2020	\$ 2,123	\$ 27	\$ 2,150
Net Book Value			
Balance, January 1, 2019	\$ 3,939	\$ 33	\$ 3,972
Balance, December 31, 2019	\$ 4,485	\$ 17	\$ 4,502
Balance, December 31, 2020	\$ 3,776	\$ 4	\$ 3,780

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The following table provides details of changes in the Company's lease liabilities:

Balance, January 1, 2019	\$	3,724
Additions		2,080
Interest		231
Payments		(1,389)
Foreign currency translation		(98)
Balance, December 31, 2019		4,548
Additions		—
Disposal		(201)
Interest		223
Payments		(1,144)
Foreign currency translation		333
Balance, December 31, 2020	\$	3,759

As at	<u>December 31, 2020</u>	
Maturities of lease liabilities:		
2021	\$	1,189
2022		1,183
2023		496
2024		292
2025		277
Thereafter		897
Total lease payments		4,334
Less imputed interest		575
Total	\$	3,759

Comprised of:		
Current portion of lease liabilities	\$	1,012
Long-term lease liabilities		2,747
Lease liabilities as of December 31, 2020	\$	3,759

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Year ended December 31, 2020 and 2019

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9. PROPERTY, PLANT AND EQUIPMENT

	Leasehold Improvements	Computer Equipment & Software	Furniture & Fixtures	Machinery & Equipment	Land & Building	Total
Cost						
Balance, January 1, 2019	\$ 2,167	\$ 3,793	\$ 796	\$ 2,868	\$ 720	\$ 10,344
Additions	264	358	26	826	—	1,474
Disposals	(1,770)	(106)	—	(1,547)	—	(3,423)
Foreign currency translation	(88)	(169)	(53)	(81)	(19)	(410)
Balance, December 31, 2019	573	3,876	769	2,066	701	7,985
Additions	49	718	35	534	—	1,336
Disposals	(177)	(598)	(97)	(314)	—	(1,186)
Foreign currency translation	(7)	(60)	(27)	9	3	(82)
Balance, December 31, 2020	\$ 438	\$ 3,936	\$ 680	\$ 2,295	\$ 704	\$ 8,053
Accumulated Depreciation						
Balance, January 1, 2019	\$ 1,074	\$ 3,387	\$ 704	\$ 1,536	\$ 29	\$ 6,730
Depreciation	172	305	35	950	19	1,481
Disposals	(1,013)	(106)	—	(1,542)	—	(2,661)
Foreign currency translation	(47)	(161)	(51)	(126)	(6)	(391)
Balance, December 31, 2019	186	3,425	688	818	42	5,159
Depreciation	93	349	22	555	18	1,037
Disposals	(111)	(386)	(59)	(287)	—	(843)
Foreign currency translation	(1)	(70)	(24)	11	1	(83)
Balance, December 31, 2020	\$ 167	\$ 3,318	\$ 627	\$ 1,097	\$ 61	\$ 5,270
Net Book Value						
Balance, January 1, 2019	\$ 1,093	\$ 406	\$ 92	\$ 1,332	\$ 691	\$ 3,614
Balance, December 31, 2019	\$ 387	\$ 451	\$ 81	\$ 1,248	\$ 659	\$ 2,826
Balance, December 31, 2020	\$ 271	\$ 618	\$ 53	\$ 1,198	\$ 643	\$ 2,783

Property, plant and equipment cost and accumulated depreciation have been reduced for assets that have been retired during the year ended December 31, 2020. The Company recognized nil impairment during the year ended December 31, 2020 (2019-\$nil).

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10. INTANGIBLE ASSETS

	Patents	Developed Software	Customer Relationships, Brand and Backlog	Total
Cost				
Balance, January 1, 2019	\$ 422,871	\$ 23,934	\$ 30,803	\$ 477,608
Additions	1,890	—	—	1,890
Disposals	(475)	—	—	(475)
Impairment	—	—	—	—
Foreign currency translation	(18,055)	(580)	(439)	(19,074)
Balance, December 31, 2019	406,231	23,354	30,364	459,949
Additions	1,336	—	—	1,336
Disposals	—	(12,750)	(9,180)	(21,930)
Impairment	—	—	—	—
Foreign currency translation	(8,836)	(282)	(180)	(9,298)
Balance, December 31, 2020	\$ 398,731	\$ 10,322	\$ 21,004	\$ 430,057
Accumulated Amortization & Impairment				
Balance, January 1, 2019	\$ 343,790	\$ 7,723	\$ 7,080	\$ 358,593
Amortization	18,452	4,732	4,406	27,590
Disposals	(264)	—	—	(264)
Impairment	115	—	—	115
Foreign currency translation	(15,164)	(283)	(172)	(15,619)
Balance, December 31, 2019	346,929	12,172	11,314	370,415
Amortization	13,795	3,603	3,004	20,402
Disposals	—	(8,248)	(3,498)	(11,746)
Impairment	295	—	—	295
Foreign currency translation	(8,263)	(235)	(72)	(8,570)
Balance, December 31, 2020	\$ 352,756	\$ 7,292	\$ 10,748	\$ 370,796
Net Book Value				
Balance, January 1, 2019	\$ 79,081	\$ 16,211	\$ 23,723	\$ 119,015
Balance, December 31, 2019	\$ 59,302	\$ 11,182	\$ 19,050	\$ 89,534
Balance, December 31, 2020	\$ 45,975	\$ 3,030	\$ 10,256	\$ 59,261

11. INVESTMENT IN JOINT VENTURE

	December 31, 2020	December 31, 2019	January 1, 2019
Balance, beginning of the year	\$ 5,233	\$ 5,203	\$ 4,244
Currency gain (loss) on financial statement translation	268	(330)	145
Company's share of earnings	1,680	873	1,232
Dividend received	(477)	(513)	(418)
Balance, end of year	\$ 6,704	\$ 5,233	\$ 5,203

XPCT is a joint venture in China in which the Company's subsidiary International Road Dynamics ("IRD") holds a 50% interest. XPCT has two business divisions providing products and services to both the ITS industry and construction equipment manufacturers.

As a distributor for the Company's ITS manufactured goods, XPCT provides a strategic advantage to the Company to increase sales in the Chinese market.

IRD had sales to XPCT of \$nil during the year ended December 31, 2020 (2019 -\$38). At December 31, 2020, IRD had amounts owing to XPCT of \$48. As at December 31, 2019 accounts receivable from XPCT was \$33.

As at December 31, 2020, IRD has an outstanding 100% joint and several liability guarantee to XPCT, for a loan in the amount of 15.0 million yuan or \$2.9 million (2019 - \$2.8 million); however, IRD can seek recourse against its joint venture partner for any amount greater than IRD's proportionate share of the liability. The amount owing represents the maximum amount available to be drawn under this facility.

The Company's ownership interest comprises a 50% share of net assets and net earnings of XPCT as well as purchase price adjustments to allocate fair values assigned to certain assets and liabilities at the time of acquisition. Summary financial information for XPCT is as follows:

As at	December 31, 2020	December 31, 2019	January 1, 2019
Cash	\$ 3,840	\$ 442	\$ 1,835
Other current assets	32,697	25,557	21,863
Non-current assets	—	55	103
Current liabilities			
Trade and other	(12,562)	(9,122)	(7,523)
Short-term loans	(9,849)	(5,779)	(4,915)
Non-current liabilities	(718)	(687)	(957)
Net assets - 100%	13,408	10,466	10,406
Net assets attributable to the Company	\$ 6,704	\$ 5,233	\$ 5,203

	Year ended December 31,	
	2020	2019
Revenue	\$ 39,542	\$ 27,080
Direct costs of revenues	(32,258)	(22,308)
Depreciation and amortization	(1,310)	(1,262)
Finance expense	(602)	(428)
Other expense	(1,420)	(1,104)
Income before income taxes	3,952	1,978
Income tax expense	592	232
Net income - 100%	\$ 3,360	\$ 1,746
Net income - attributable to the Company	\$ 1,680	\$ 873

12. GOODWILL

The changes in the carrying amount of goodwill by reporting units are presented in the table below:

	Licensing	Intelligent Transportation Systems	Enterprise Software	Total
Balance at January 1, 2019	\$ 17,184	\$ —	\$ 17,262	\$ 34,446
Currency translation	(733)	—	(736)	(1,469)
Balance at December 31, 2019	16,451	—	16,526	32,977
Disposition	—	—	(16,526)	(16,526)
Currency translation	(358)	—	—	(358)
Balance at December 31, 2020	\$ 16,093	\$ —	\$ —	\$ 16,093

In accordance with the IFRS guidance related to goodwill, the Company is required to assess the carrying amount of its goodwill for potential impairment annually or more frequently if events or a change in circumstances indicate that impairment may have occurred. The Company tests goodwill for impairment annually at year-end using data as of December 31 of that year at the level of the group of CGUs to which the goodwill is allocated, which corresponds with the corresponding operating segment.

The recoverable amount of the CGU to which the goodwill belongs is determined based on a value-in-use calculation that discounts the present value of estimated future cash flows at an appropriate risk-adjusted rate. The Company uses its internal forecasts to estimate future cash flows and includes an estimate of long-term future growth rates based on its most recent views of the long-term outlook for each business for a period of five years and uses a terminal growth rate of 2%. Actual results may differ from those assumed in these forecasts. The Company derives its discount rates using a capital asset pricing model and by analyzing published rates for industries relevant to its reporting units to estimate the cost of equity financing. The Company uses discount rates that are commensurate with the risks and uncertainty inherent in the respective businesses and in its internally developed forecasts. The discount rate used in the Licensing segment valuation, the only segment at December 31, 2020 to which goodwill is allocated, was 13.6% (2019 - 23.5%). The discount rate used in the assessment of recoverable value of the Enterprise Software segment at December 31, 2019 was 20.0%.

The results of the assessments performed at December 31, 2020 and December 31, 2019 indicated that the recoverable amount of these operating segments exceeded their carrying values.

Estimating the fair value of reporting units requires the use of estimates and significant judgments that are based on a number of factors including actual operating results. It is reasonably possible that the judgments and estimates described above could change in future periods.

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13. BANK INDEBTEDNESS

As at	December 31, 2020	December 31, 2019	January 1, 2019
HSBC revolving credit facility of \$9.5 million authorized and secured by a general security agreement:			
HSBC Bank Canada - Borrowing in Canadian dollars with interest at bank prime plus 1.5% (effective rate at December 31, 2020 of 4.5% (2019 - 5.5%))	\$ —	\$ 2,934	\$ 1,973
HSBC Bank Canada demand term loan in Canadian dollars, repayable in quarterly installments of CDN\$32 with interest at bank prime plus 0.5% (effective rate at December 31, 2020 of 3.5% (2019 - 4.5%)). Due September 30, 2021	—	225	354
HSBC Bank Canada demand term loan in Canadian dollars, repayable in quarterly installments of CDN\$75 with interest at bank prime plus 0.5% (effective rate at December 31, 2020 of 4.5% (2019 - 4.5%)). Due May 31, 2022	—	750	1,053
ING Bank, euro revolving credit facility, interest at three-month Euribor rate plus 2.4% (effective rate at December 31, 2020 of 1.9% (2019-2.0%))	—	117	157
	\$ —	\$ 4,026	\$ 3,537

The HSBC Bank Canada credit facility may be borrowed by way of banker's acceptances at prevailing market rates to a maximum of \$9.5 million or by way of US dollar advances to a maximum of US \$7.0 million. Borrowings on this facility are restricted to the lesser of \$9.5 million and the margin total on the following IRD assets: 90% of secured and government accounts receivable less than 120 days, 75% of good quality Canadian or US domiciled accounts receivable less accounts 90 days and over, 90% of foreign accounts receivable backed by letters of credit and 50% of inventory and 25% of works in process inventory to a maximum of \$3.0 million. As at December 31, 2020, approximately \$7.7 million was available to be drawn.

The Company's credit facility and demand term loans with HSBC Bank Canada are secured by a general security agreement on the assets of IRD held in Canada with a carrying value at December 31, 2020 of \$28.6 million. In addition, IRD's subsidiaries in the United States, Chile and Mexico have provided corporate guarantees as security, and the demand term loan is guaranteed by Export Development Canada.

The ING Bank credit facility is secured by the assets of iCOMS Detections S.A., a subsidiary of IRD, to a maximum of \$246 (€157). The carrying value of these assets was \$2.3 million (€1.4 million) as at December 31, 2020.

IRD is subject to covenants on its credit facility and long-term debt with HSBC Bank Canada as follows: current ratio greater than 1.2 to 1 (tested monthly); debt to tangible net worth less than 2.5 to 1 (tested monthly); and debt service coverage ratio greater than 1.25 to 1 (tested annually) based on IRD's financial results. As at December 31, 2020, IRD is in compliance with these covenants.

IRD's Chilean subsidiary also maintains a secured line of credit to support performance guarantees required for selected projects. As at December 31, 2020, the dollar value of these performance guarantees totaled \$706 (2019 - \$612). IRD has also provided a 100% joint and several liability guarantee to XPCT, for a loan in the amount of 15.0 million yuan or \$2.9 million (2019 - \$2.8 million); however IRD can seek recourse against its joint venture partner for any amount greater than IRD's proportionate share of the liability.

The Company also has a revolving credit facility available with the Canadian Imperial Bank of Commerce in the amount of \$8 million or the equivalent in US dollars for general corporate purposes and a further US \$2 million for a foreign exchange facility. Canadian dollar or US dollar amounts advanced under this credit facility are

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payable on demand and bear interest at the bank's Canadian prime rate plus 1.0% per annum or US base rate plus 1.0% per annum. Borrowings under this facility are collateralized by a general security agreement over the Company's cash and cash equivalents, accounts receivable and present and future personal property. As at December 31, 2020 and during the year ended December 31, 2020, the Company had no borrowings under this facility (2019 – \$nil).

14. ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

As at	December 31, 2020	December 31, 2019	January 1, 2019
Trade payables	\$ 10,039	\$ 9,479	\$ 12,419
Accrued compensation	6,202	8,013	4,823
Accrued contingent partner payments & legal fees	433	6,128	2,883
Dividends	1,383	1,471	1,485
Accrued litigation costs	1,578	930	1,277
Customer advances	—	—	1,244
Project losses	321	243	513
Other current liabilities	82	—	—
	\$ 20,038	\$ 26,264	\$ 24,644

15. CONTINGENT LIABILITIES

In connection with Quarterhill's original acquisition of VIZIYA in 2017, the Company agreed to pay VIZIYA's former shareholders up to an additional US\$11,900 in cash and common shares pursuant to the terms of the acquisition agreement if VIZIYA achieved certain targets for its earnings before interest, taxes and amortization ("Eligible Earnings") between at least US\$6,750 and US\$11,850 for the period from April 1, 2017 to July 31, 2019. Additionally, if VIZIYA achieved cumulative Eligible Earnings during that period exceeding US\$11,850, the Company would be required to pay 50% of the amount of those excess Eligible Earnings as additional contingent consideration until that cumulative Eligible Earnings reached a cap of US\$23,700. In 2019, Quarterhill determined that VIZIYA did not achieve the minimum amount of cumulative Eligible Earnings for its former shareholders to be paid any additional amounts. VIZIYA's former shareholders have initiated arbitration of the Eligible Earnings and additional payment calculations as permitted pursuant to the terms of the acquisition agreement, the results of which arbitration may, or may not, result in a determination that the former shareholders are entitled to receive some or all of this earn-out obligation under the acquisition agreement. Quarterhill has defended this arbitration and does not believe that it will ultimately be found liable; however, the outcome of any litigation including this arbitration is inherently uncertain. As at December 31, 2020, it was determined that it is not more likely than not that a legal liability exists and therefore no provision has been made in the Company's consolidated financial statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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16. SHARE CAPITAL

The share capital of the Company consists of the following:

	Authorized	Issued and Outstanding		
		December 31, 2020	December 31, 2019	January 1, 2019
a. common shares, with no par value	unlimited	114,322,032	118,817,466	118,817,466
b. special preferred, redeemable, retractable, non-voting shares	6,350.9	Nil	Nil	Nil
c. preferred shares, issuable in series	unlimited	Nil	Nil	Nil
				Number
January 1, 2019, and December 31, 2019				118,817,466
Conversion of PSU to common shares				47,290
Exercise of stock options				351,893
Shares repurchased under SIB for cancellation				(2,687,981)
Shares repurchased under NCIB for cancellation				(2,206,636)
December 31, 2020				114,322,032

SIB

On May 21, 2020, the Company announced its intention to make a Substantial Issuer Bid ("SIB") to purchase for cancellation up to \$20 million of its outstanding common shares from shareholders for cash by way of modified-Dutch auction with a price range of between \$1.95 and \$2.15 per share. The SIB commenced on June 1, 2020 and expired on July 7, 2020. During the third quarter of 2020, the Company repurchased for cancellation 2,687,981 common shares at an average purchase price of \$2.15 per share, plus transaction costs of \$0.5 million, for a total of \$6.3 million. As purchases were made, the Company reduced share capital for the average book value of the shares repurchased. As the price paid by the Company was less than the average book value, the difference was allocated to contributed surplus. During the year, \$7.1 million was allocated to contributed surplus.

NCIB

On August 6, 2020, the Company received approval from TSX on its notice of intention to make a Normal Course Issuer Bid ("NCIB") to purchase for cancellation up to 11,303,777 of its outstanding common shares. During the year 2020, the Company repurchased for cancellation 2,206,636 common shares at an average purchase price of \$1.95 per share totaling \$4.3 million. As purchases were made, the Company reduced share capital for the average book value of the shares repurchased. As the price paid by the Company was less than the average book value, the difference was allocated to contributed surplus. During the year, \$6.3 million was allocated to contributed surplus.

The Company paid quarterly cash dividends as follows:

	2020		2019	
	Per Share	Total	Per Share	Total
1st quarter	\$ 0.0125	\$ 1,481	\$ 0.0125	\$ 1,500
2nd quarter	0.0125	1,462	0.0125	1,473
3rd quarter	0.0125	1,498	0.0125	1,475
4th quarter	0.0125	1,383	0.0125	1,489
	\$ 0.0500	\$ 5,824	\$ 0.0500	\$ 5,937

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Stock-Based Compensation

At the annual and special meeting of shareholders held on April 18, 2018, Quarterhill's shareholders approved the adoption of the Company's 2018 Equity Incentive Plan (the "Equity Incentive Plan") and the related terminations of the Company's "2001 Share Option Plan" (the "Option Plan") and "Deferred Stock Unit Plan for Directors and Designated Employees" (the "DSU Plan").

As at December 31, 2020, the Company had options to purchase up to 6,810,789 common shares outstanding. Upon adoption of the Equity Incentive Plan, all options outstanding under the Option Plan are now governed by the Equity Incentive Plan. All deferred stock units outstanding under the DSU Plan were exercised for common shares on April 18, 2019 so no deferred stock units remain outstanding.

Quarterhill maintains the newly adopted Equity Incentive Plan (replacing the Option Plan and the DSU Plan) and a Restricted Share Unit ("RSU") Plan for its directors, employees and consultants. The current RSU Plan calls for settlement only in cash.

During the year ended December 31, 2020, the Company granted options to purchase 4,571,757 common shares at exercise prices ranging from \$1.80 to \$2.60 with a weighted average fair value of \$0.69. The Company used the Black-Scholes model for estimating the fair value of options granted with the following weighted average assumptions for the options granted in 2020.

	<u>2020</u>
Risk free rate	0.69 %
Volatility	0.45
Expected option life (in years)	3.6
Expected dividend yield	1.95 %
Forfeiture rate	14.50 %

During the year ended December 31, 2017, the Company granted two sets of performance-based options with grant date at fair value of \$1.106 and \$1.0175, respectively. These performance-based options will vest, if at all, over a three year period. Each tranche of options will vest if at any time after the first, second and third years, certain specified share price targets are achieved for a period of at least 30 consecutive days. The Company estimates the fair value of the performance based options using a Monte Carlo simulation model. The following assumptions were used during the year ended December 31, 2018:

	<u>May Grant</u>	<u>June Grant</u>
Number of options granted	1,299,072	650,000
Stock price	\$2.16	\$1.89
Implied volatility	55%	60%
Risk free rate	1.43%	1.40%

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	Options Outstanding			Exercisable Options	
	Number of Options	Price Range	Weighted Average Exercise Price	Number	Weighted Average Exercise Price
December 31, 2018	6,840,475	\$1.89 — \$4.37	\$2.77	2,231,285	\$3.85
Granted	1,183,918	1.33 — 1.76	1.45		
Forfeited	(3,045,185)	1.33 — 3.93	2.42		
Expired	(1,190,300)	3.37 — 4.37	4.37		
December 31, 2019	3,788,908	\$1.33 — \$4.23	\$2.14	1,508,063	\$2.12
Granted	4,571,757	1.80 — 2.60	2.03		
Forfeited	(1,057,983)	1.33 — 2.38	2.19		
Expired	(140,000)	3.25 — 4.23	3.83		
Exercised	(351,893)	1.33 — 2.38	2.32		
December 31, 2020	6,810,789	\$1.33 — \$4.23	\$2.02	1,570,308	\$2.04

The weighted average fair value per option granted during the year ended December 31, 2020 was \$0.69 (2019 – \$0.69).

The intrinsic value of the exercisable options was \$495 as at December 31, 2020 (2019 – \$nil). The total fair value of options vested was \$468 for the year ended December 31, 2020 (2019 – \$991).

As at December 31, 2020, there was \$3,507 of total unrecognized stock-based compensation cost, net of expected forfeitures, related to unvested stock-based compensation arrangements granted under the stock option plan. This cost is expected to be recognized over a weighted average period of 2.9 years.

Details of the outstanding options at December 31, 2020 are as follows:

Range of Exercise Prices		Outstanding Options at December 31, 2020	Remaining Term of Options in Years	Weighted Average Exercise Price	Exercisable Options at December 31, 2020	Weighted Average Exercise Price
\$ 1.33	\$ 1.79	730,205	4.38	\$ 1.53	247,018	\$ 1.53
1.80	1.99	3,368,424	5.16	1.91	166,667	1.89
2.00	2.50	1,765,683	3.86	2.08	910,146	2.10
2.60	2.84	946,477	4.74	2.66	246,477	2.66
\$ 1.33	\$ 2.84	6,810,789	4.68	\$ 2.02	1,570,308	\$ 2.04

Restricted Share Units

The Company implemented an RSU Plan for certain employees and directors in January 2007. Under the RSU Plan, units are settled in cash based on the market value of Quarterhill's common shares on the dates when the RSUs vest. The accrued liability and related expense for the RSUs are adjusted to reflect the market value of the common shares at each consolidated statement of financial position date. The liability recorded in respect of the vested RSUs was \$250 as at December 31, 2020 (2019 - \$539). The change in the liability is recorded as compensation expense.

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RSU activity for the years ended December 31, 2020 and 2019 was as follows:

	Number
December 31, 2018	2,268,343
Granted	391,609
Settled	(1,700,547)
Forfeited	(88,571)
December 31, 2019	870,834
Granted	—
Settled	(682,739)
Forfeited	(10,977)
December 31, 2020	177,118

During the year ended December 31, 2020, 10,977 RSUs (2019 – 88,571) were forfeited as they related to former employees.

17. EXPENSE BY NATURE

	Year ended December 31,	
	2020	2019
Personnel costs	\$ 30,338	\$ 36,434
Subcontractor fees	7,594	8,759
Direct and indirect materials costs	19,299	19,914
Litigation and licensing costs	38,142	41,813
Professional, patent and outside services	13,956	9,884
Communications and information technology	1,471	1,172
Facilities	1,581	2,724
Travel and entertainment	2,287	3,502
Other administrative expenses	150	1,408
Depreciation of right-of-use assets	979	1,305
Depreciation of property, plant and equipment	969	1,296
Amortization and impairment of intangible assets	19,150	23,420
Special charges	1,227	2,448
Total direct cost of revenues and operating expenses	137,143	154,079
Salaries and wages	26,528	26,091
Employee benefits	4,245	3,654
Stock-based compensation	1,015	683
Bonuses	3,544	5,251
Commissions	172	310
Other personnel costs	572	445
Government grants earned	(5,738)	—
Personnel costs	\$ 30,338	\$ 36,434

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18. SPECIAL CHARGES

Special charges within the consolidated statements of income and comprehensive income include costs and recoveries that relate to certain restructuring initiatives that the Company has undertaken from time to time, acquisition-related costs and recoveries and other charges. During the year ended December 31, 2020, the Company recognized special charges of \$1,227 (2019 - \$2,448). Charges for the year ended December 31, 2020 relate to retirement allowances while costs for the comparative period related to workforce reduction and reduction of operating facilities at the Company's Licensing segment, offset by the contingent consideration adjustment.

19. TAXES

The reconciliation of the expected provision for income tax expense to the actual provision for income tax expense reported in the consolidated statements of income and comprehensive income for the years ended December 31, 2020 and December 31, 2019 is as follows:

	Year ended December 31,	
	2020	2019
Income before taxes	\$ 9,265	\$ 20,316
Canadian statutory income tax rate	26.5 %	26.5 %
Expected income tax expense	2,455	5,384
Permanent differences	251	423
Foreign withholding taxes paid	16	13
Foreign rate differential	(234)	(22)
Return to provision	297	(1,760)
Change in benefit of tax assets not recognized	1,672	4,470
Other	380	715
Income tax expense	\$ 4,837	\$ 9,223

The income tax expense from continuing operations are as follows:

	Year ended December 31,	
	2020	2019
Current income tax expense		
Current period	\$ 2,170	\$ 8,115
Adjustment in respect of prior periods	(133)	2
Deferred income tax expense		
Current period	2,370	2,868
Adjustment in respect of prior periods	430	(1,762)
	\$ 4,837	\$ 9,223

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The effect of temporary differences, tax losses, and tax credits that give rise to significant components of the Company's deferred income tax assets and liabilities, which have been recognized during the year ended December 31, 2020, are as follows:

	<u>December 31, 2020</u>	<u>December 31, 2019</u>
Deferred income tax assets		
Tax loss carryforwards	\$ 18,014	\$ 22,886
Scientific research and experimental development ("SR&ED") carryforwards	8,087	8,399
Lease liabilities	1,800	1,218
Tax credits	1,178	1,001
Difference between tax and book value of capital and intangible assets	409	(3,817)
Tax reserves and accrued liabilities	458	426
Deferred revenue, unbilled revenue & prepaid expenses	170	568
Deferred income tax assets	30,116	30,681
Deferred income tax liabilities		
Right-of-use assets	(1,794)	(1,164)
Investments	(198)	(77)
Deferred income tax liabilities	(1,992)	(1,241)
Deferred income tax assets, net	\$ 28,124	\$ 29,440

The Company is required to assess whether it is probable that it will realize the benefits of its deferred tax assets based on consideration of all available evidence. The factors the Company uses to assess the likelihood of realization are its history of losses, forecasts of future pre-tax income, and tax planning strategies that could be implemented to realize the deferred tax assets. Accordingly, available deferred income tax assets in the amount of \$21,759 were not recognized as it is not probable that future taxable income will be available to the Company to utilize the benefits. Additionally, certain Canadian entities within the licensing segment that incurred losses during the current period have relied on tax planning strategies to support the recognition of their respective deferred tax assets in the amount of \$2,925.

The amount of deductible temporary differences, unused tax losses, and unused tax credits for which no deferred tax asset is recognized in the consolidated statements of financial position for the years ended December 31, 2020 and 2019 are as follows:

	<u>December 31, 2020</u>	<u>December 31, 2019</u>
Tax loss carryforwards	\$ 44,423	\$ 50,625
Fixed assets	21,079	21,651
Tax credits	6,387	6,335
Other deductible temporary differences	713	2,102
	\$ 72,602	\$ 80,713

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(in thousands of Canadian dollars, except share and per share amounts, unless otherwise stated)

As at December 31, 2020, the Company had unused non-capital tax losses of approximately \$109,618 (2019 - \$138,099) that are due to expire as follows:

Expiry	SR&ED pool	Canadian Tax Losses	US Tax Losses	Other Jurisdictions	Consolidated Tax Losses
2021	\$ —	\$ —	\$ —	\$ 292	\$ 292
2022	—	—	—	349	349
2023	—	—	—	18	18
2024	—	—	—	277	277
2025	—	—	—	70	70
2026	—	—	—	—	—
2027	—	—	—	563	563
2028	—	—	—	412	412
2029	—	—	—	—	—
2030	—	—	1,095	—	1,095
2031	—	—	2,657	—	2,657
2032	—	—	6,129	—	6,129
2033	—	8,366	9,726	—	18,092
2034	—	3,385	5,296	—	8,681
2035	—	1,638	1,496	—	3,134
2036	—	17,237	10,581	—	27,818
2037	—	3,852	—	—	3,852
2038	—	31,707	—	—	31,707
2039	—	374	—	—	374
2040	—	192	—	—	192
Indefinite	31,412	—	2,567	1,339	3,906
	\$ 31,412	\$ 66,751	\$ 39,547	\$ 3,320	\$ 109,618

The Company has investment tax credits of \$2,726 that expire in various amounts from 2022 to 2040. Investment tax credits, which are earned as a result of qualifying SR&ED expenditures, are recognized and applied to reduce income tax expense in the year in which the expenditures are made and their realization is reasonably assured. The Company also has unused foreign tax credits of approximately \$5,002 that expire in various amount from 2026 to 2030.

As at December 31, 2020, the Company had temporary differences of \$3,546 (2019 - \$13,191) associated with investments in subsidiaries for which no deferred tax liabilities have been recognized, as the Company is able to control the timing of the reversal of these temporary differences and it is not probable that these differences will reverse in the foreseeable future.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Year ended December 31, 2020 and 2019

(in thousands of Canadian dollars, except share and per share amounts, unless otherwise stated)

20. INCOME PER SHARE

Basic income per share is calculated by dividing net income by the weighted average number of common shares outstanding during the year.

Diluted income per share is calculated by adjusting the weighted average number of common shares outstanding to assume conversion of all potential dilutive stock options to common shares

	Year ended December 31,	
	2020	2019
Numerator:		
Net income from continuing operations	4,428	11,093
Net income from discontinued operations	14,255	1,569
Net income	18,683	12,662
Denominator:		
Weighted average number of common shares outstanding for basic EPS	116,939,833	118,817,466
Adjustment for stock options	70,082	—
Weighted average number of common shares outstanding for diluted EPS	117,009,915	118,817,466
From continuing operations	0.04	0.09
From discontinued operations	0.12	0.01
Basic income per share	0.16	0.10
From continuing operations	0.04	0.09
From discontinued operations	0.12	0.01
Diluted income per share	0.16	0.10

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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(in thousands of Canadian dollars, except share and per share amounts, unless otherwise stated)

21. SEGMENT REPORTING

An operating segment is a component of the Company that engages in business activities from which it may earn revenues and incur expenses, including revenues and expenses that relate to transactions with any of the Company's other components, and for which discrete financial information is available. The operating results of all operating segments are reviewed regularly by the Company's CODM to make decisions about resources to be allocated to the segment and assess their performance. The Company's CODM is the Chief Executive Officer. The Company's operating segments are organized on the basis of products and services provided and also represent its reportable segments. The Company's reportable segments, identified as Licensing and Intelligent Systems, follow the same accounting policies as those described in the summary of significant accounting policies, and are further described below. The Company divested its Enterprise Software segment on May 15, 2020.

Licensing – The Licensing segment includes companies that count licensing as their principal business activity. The Company's investment in this segment consists of WiLAN and its wholly owned subsidiaries. Current WiLAN patent portfolios include patents relating to memory interface technologies, semiconductor manufacturing and packaging technologies, medical, industrial and automotive applications, computer gaming, intelligent personal assistant technologies, enhanced image processing, streaming video technologies, non-volatile Flash memory, DRAM and other memory technologies, semiconductor analog circuitry technologies and several other technologies.

Intelligent Transportation Systems – The Intelligent Transportation Systems segment includes companies that provide integrated systems and solutions to the ITS industry and its adjacent markets. The Company's investment in this segment consists of IRD and its wholly owned subsidiaries. The ITS industry is focused on improving the intelligent systems, enhancing the safety, increasing the efficiency and reducing the environmental impact of highway and roadway transportation systems.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Year ended December 31, 2020 and 2019

(in thousands of Canadian dollars, except share and per share amounts, unless otherwise stated)

Segmented statements of income for the years ended December 31, 2020 and 2019 are included below:

CONTINUING OPERATIONS	For the year ended December 31, 2020			
	Licensing	Intelligent Transportation Systems	Corporate	Total
Revenues	\$ 78,260	\$ 66,266	\$ —	\$ 144,526
Direct cost of revenues	46,205	39,463	—	85,668
Gross profit	32,055	26,803	—	58,858
Depreciation of right-of-use assets	238	646	95	979
Depreciation of property, plant and equipment	59	889	21	969
Amortization of intangible assets	13,785	5,070	—	18,855
Selling, general and administrative expenses	3,386	11,393	12,089	26,868
Research and development expenses	—	2,282	—	2,282
Impairment losses of intangible assets	295	—	—	295
Special charges	—	883	344	1,227
Results from operations	14,292	5,640	(12,549)	7,383
Finance income	(200)	(10)	(363)	(573)
Finance expense	139	293	27	459
Foreign exchange (gain) loss	647	27	(762)	(88)
Other income	—	(1,680)	—	(1,680)
Income before taxes	13,706	7,010	(11,451)	9,265
Current income tax expense	1,834	203	—	2,037
Deferred income tax (recovery) expense	(2,159)	1,661	3,298	2,800
Income tax expense	(325)	1,864	3,298	4,837
Net income (loss) from continuing operations	\$ 14,031	\$ 5,146	\$ (14,749)	\$ 4,428

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Year ended December 31, 2020 and 2019

(in thousands of Canadian dollars, except share and per share amounts, unless otherwise stated)

CONTINUING OPERATIONS	For the year ended December 31, 2019			
	Licensing	Intelligent Transportation Systems	Corporate	Total
Revenues	\$ 106,052	\$ 66,873	\$ —	\$ 172,925
Direct cost of revenues	53,130	42,887	—	96,017
Gross profit	52,922	23,986	—	76,908
Depreciation of right-of-use assets	534	711	60	1,305
Depreciation of property, plant and equipment	123	1,153	20	1,296
Amortization of intangible assets	18,275	5,030	—	23,305
Selling, general and administrative expenses	2,849	13,477	10,393	26,719
Research and development expenses	—	2,874	—	2,874
Impairment losses of intangible assets	115	—	—	115
Special charges	2,464	509	(525)	2,448
Results from operations	28,562	232	(9,948)	18,846
Finance income	(433)	(23)	(1,209)	(1,665)
Finance expense	69	657	14	740
Foreign exchange (gain) loss	(968)	276	1,016	324
Other income	4	(873)	—	(869)
Income before taxes	29,890	195	(9,769)	20,316
Current income tax expense	7,660	457	—	8,117
Deferred income tax expense (recovery)	2,898	(1,628)	(164)	1,106
Income tax expense (recovery)	10,558	(1,171)	(164)	9,223
Net income (loss) from continuing operations	\$ 19,332	\$ 1,366	\$ (9,605)	\$ 11,093

The following table includes revenue by contracts disaggregated by the timing of revenue recognition:

	Year ended December 31,	
	2020	2019
Revenue recognized at a point in time	129,909	156,789
Revenue recognized over time	14,617	16,136
	144,526	172,925

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Year ended December 31, 2020 and 2019

(in thousands of Canadian dollars, except share and per share amounts, unless otherwise stated)

Revenue by geography for the years ending December 31, 2020 and 2019 are as follows:

Revenues	Year ended December 31,	
	2020	2019
United States	\$ 115,412	\$ 78,297
Canada	2,509	7,287
Chile	2,791	4,056
China	179	9,505
Korea	1,825	54,018
Singapore	570	—
Taiwan	9,094	5,942
Thailand	2,876	1,552
Ukraine	2,151	2,846
Rest of the world	7,119	9,422
Total revenues	\$ 144,526	\$ 172,925

Segment assets as at December 31, 2020 and December 31, 2019 are as follows:

As at	December 31, 2020	December 31, 2019	January 1, 2019
Licensing	\$ 107,852	\$ 103,658	\$ 126,911
Intelligent Transportation Systems	65,888	60,852	61,877
Total segment assets	173,740	164,510	188,788
Total corporate assets	130,069	159,512	138,136
Total assets	\$ 303,809	\$ 324,022	\$ 326,924

As at	December 31, 2020	December 31, 2019	January 1, 2019
Non-current assets			
United States	\$ 17,230	\$ 18,458	\$ 18,109
Canada	63,295	109,645	140,887
Belgium	567	417	909
Chile	825	1,319	1,142
Total non-current assets	\$ 81,917	\$ 129,839	\$ 161,047

Non-current assets for this purpose consist of property, plant and equipment, right-of-use assets, intangible assets, and goodwill.

Major Customers

A major customer is defined as an external customer whose transactions within a segment of the Company amount to 10% or greater of the respective segment's revenue. Two major customers of the Licensing segment represented \$66,295 of the segment's total revenues for the year ended December 31, 2020, whereas for the year ended December 31, 2019, three major customers totaled \$85,537 of the segment's total revenues. One major customer of the Intelligent Transportation Systems segment represented \$8,877 for the year ended December 31, 2020. There were no major customers for the Intelligent Transportation Systems segment for the year ended December 31, 2019.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Year ended December 31, 2020 and 2019

(in thousands of Canadian dollars, except share and per share amounts, unless otherwise stated)

Remaining performance obligations

As at December 31, 2020, the amount of transaction price allocated to remaining performance obligations was \$30,734. The Company expects to recognize approximately 75% of this balance as revenue in 2021, 10% in 2022 and 15% thereafter.

22. FINANCIAL RISK MANAGEMENT

Credit Risk

Credit risk is the risk of financial loss to the Company if a licensee or counter party to a financial instrument fails to meet its contractual obligations. Financial instruments that potentially subject the Company to concentrations of credit risk consist primarily of cash and cash equivalents, short-term investments, accounts receivable, and foreign exchange forward contracts.

The Company's cash and cash equivalents and short-term investments consist primarily of deposit investments that are held primarily with Canadian chartered banks. Management does not expect any counter-parties to fail to meet their obligations.

The Company recognizes a loss allowance provision using the simplified approach based on lifetime expected credit losses ("ECLs"). The Company's exposure to credit risk with its accounts receivable from customers is influenced mainly by the individual characteristics of each customer. The Company's customers are for the most part, large multinational companies or government organizations which do not have a history of non-payment. Credit risk from accounts receivable encompasses the default risk of the Company's customers. Prior to entering into transactions with new customers, the Company assesses the risk of default associated with the particular customer. In addition, on an ongoing basis, management monitors the level of accounts receivable attributable to each customer and the length of time taken for amounts to be settled and, where necessary, takes appropriate action to follow up on those balances considered overdue. The Company has had no significant bad debts for any periods presented.

The following table provides an aging analysis of trade accounts receivable. The age of an invoice does not necessarily indicate an account is past due as many contracts for system revenue require the successful completion of system testing and acceptance.

As at	December 31, 2020	December 31, 2019	January 1, 2019
Current	\$ 178	\$ 32,133	\$ 1,047
1 - 30 days	7,494	6,065	3,927
31 - 60 days	2,083	2,087	2,921
61 - 90 days	1,549	768	4,347
91 days and over	3,044	3,018	3,645
Less expected credit loss	(601)	(1,146)	(1,168)
Accounts receivable	13,747	42,925	14,719
Long-term accounts receivable	506	3,846	565
Total accounts receivable	\$ 14,253	\$ 46,771	\$ 15,284

None of the amounts outstanding have been challenged by the respective counterparties and the Company continues to conduct business with them on an ongoing basis. Accordingly, management has no reason to believe that these balances are not fully collectable in the future.

The Company reviews financial assets on an ongoing basis with the objective of identifying potential matters that could delay the collection of funds at an early stage. Once items are identified as being past due, contact is made with the respective customer to determine the reason for the delay in payment and to establish an agreement to rectify the breach of contractual terms.

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Liquidity Risk

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they fall due. The Company's objective in managing liquidity risk is to ensure that it has sufficient liquidity available to meet its liabilities when due. The Company manages its liquidity needs through various sources including cash generated through operations, cash reserves, various revolving credit facilities, and the issuance of common shares. At December 31, 2020, the Company had cash and cash equivalents and short-term investments of \$141,250.

The table below presents a maturity analysis of the Company's financial liabilities:

	Total	Less than 1 year	2 - 3 years	4 - 5 years	Thereafter
Accounts payable and accrued liabilities	20,038	20,038	—	—	—
	\$ 20,038	\$ 20,038	—	—	—

See Note 8 for maturity of lease liabilities.

Market Risk

Market risk is the risk to the Company that the fair value of future cash flows from its financial instruments will fluctuate due to changes in interest rates and foreign currency exchange rates. Market risk arises as a result of the Company generating revenues in foreign currencies.

Interest Rate Risk

The financial instruments that expose the Company to interest rate risk are its cash and cash equivalents, short-term investments, bank indebtedness and long-term debt. The Company's objectives of managing its cash and cash equivalents and short-term investments are to ensure sufficient funds are maintained on hand at all times to meet day-to-day requirements and to place any amounts that are considered in excess of day-to-day requirements on short-term deposit with the Company's banks so that they earn interest. When placing amounts of cash and cash equivalents into short-term investments, the Company only places investments with Canadian chartered banks and ensures that access to the amounts placed can be obtained on short notice. A one percent increase/decrease in interest rates would not have resulted in a material increase/decrease in interest income/expense during the year ended December 31, 2020.

Currency Risk

A portion of Quarterhill's revenues and operating expenses are denominated in Canadian dollars, Indian rupees, Chilean pesos, euros, Australian dollars and Chinese yuan. Because the parent company's functional currency is in US dollars, Quarterhill's operating results are subject to changes in the exchange rate of the foreign currencies (primarily Canadian dollar) relative to the US dollar. Any decrease in the value of the Canadian dollar relative to the US dollar has an unfavourable impact on Canadian dollar denominated revenues and a favourable impact on Canadian dollar denominated operating expenses. Approximately 5.2% of the Company's cash and cash equivalents and short-term investments are denominated in Canadian dollars and are subject to changes in the exchange rate of the Canadian dollar relative to the US dollar.

The following table illustrates the Company's exposure to exchange risk and the pre-tax effects on earnings and other comprehensive income ("OCI") of a 5% decrease in the US dollar in comparison to other relevant foreign currency. This analysis assumes all other variables remain constant.

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	Foreign Currency Exposure	Foreign Currency Exchange Risk In US\$	5% Decrease OCI
	December 31, 2020	Income	
Net asset:			
Canadian dollar	(372)	14	5
Chilean peso	876	—	(44)
Mexican Peso	266	—	(13)
Euro	(153)	6	2
Chinese yuan	6,704	—	(335)
Other	(317)	17	(1)

The Company may manage the risk associated with foreign exchange rate fluctuations by, from time to time, entering into foreign exchange forward contracts and engaging in other hedging strategies. To the extent that Quarterhill engages in risk management activities related to foreign exchange rates, it may be subject to credit risks associated with the counterparties with whom it contracts.

The Company's objective in obtaining foreign exchange forward contracts is to manage its risk and exposure to currency rate fluctuations related primarily to future cash inflows and outflows of Canadian dollars. The Company does not use foreign exchange forward contracts for speculative or trading purposes. For the year ended December 31, 2020 the Company did not hold any foreign exchange forward contracts.

The COVID-19 Pandemic

While the Company is not immune to the impacts of the pandemic, the majority of the work performed within each portfolio company remains ongoing, and in the case of the Intelligent Transportation Systems segment, certain of its work has been deemed "essential" by governing authorities. However, there remains some risk that certain project work or license sales will be deferred or restricted and new orders delayed, in particular, in international jurisdictions.

23. RELATED-PARTY TRANSACTIONS

These consolidated financial statements include the accounts of Quarterhill Inc. and its wholly owned subsidiaries. Balances and transactions between the Company and its subsidiaries, which are related parties, have been eliminated on consolidation and are not disclosed in this note. Transactions and balances with XPCT, a joint venture in China in which the Company's subsidiary IRD holds a 50% interest, which is also a related party, are disclosed in Note 11.

Key management personnel are Quarterhill Inc.'s President & Chief Executive Officer, Chief Financial Officer and Senior Vice-President, General Counsel & Corporate Secretary and the Chief Executive Officers of each of IRD and WiLAN. Other related parties are close family members of the key management personnel and entities controlled by key management personnel.

The executive compensation expense to the five key management personnel is as follows:

	Year ended December 31,	
	2020	2019
Salaries and benefits	\$ 2,658	\$ 2,723
Board fees	717	704
Stock-based compensation	601	588
	\$ 3,976	\$ 4,015

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24. CHANGES IN NON-CASH WORKING CAPITAL BALANCES

	Year ended December 31,	
	2020	2019
Accounts receivable	\$ 23,962	\$ (27,179)
Unbilled revenue	(5,287)	(3,967)
Income taxes recoverable	(139)	122
Inventories	(829)	(840)
Prepaid expenses and deposits	(6,861)	716
Deferred revenue	1,713	362
Accounts payable and accrued liabilities	(5,547)	1,238
Income taxes payable	466	180
	7,478	(29,368)

Supplemental Cash Flow Information

	Year ended December 31,	
	2020	2019
Net interest received in cash, included in operations	\$ (553)	\$ (1,424)
Taxes paid	2,099	2,933

25. CAPITAL MANAGEMENT

The Company's capital management objectives are to maintain financial flexibility in order to pursue its strategy of organic acquisitional growth, pay dividends, and, from time to time, return capital to shareholders, while maintaining an adequate return for shareholders. The Company defines its capital as cash, the aggregate of cash and cash equivalents, short-term investments, restricted short-term investments, bank indebtedness, current and long-term debt, and shareholders' equity.

	December 31, 2020	December 31, 2019	January 1, 2019
Current portion of long-term debt	\$ —	\$ 59	\$ 407
Non-current portion of long-term debt	—	271	236
Long-term debt	—	330	643
Bank indebtedness	—	4,026	3,537
Less:			
Cash and cash equivalents	(135,700)	(87,870)	(87,029)
Short-term investments	(5,550)	(1,550)	(1,551)
Restricted short-term investments	—	—	(2,995)
Net debt	(141,250)	(85,064)	(87,395)
Shareholders' equity	271,930	275,203	278,895
Total capital management	\$ 130,680	\$ 190,139	\$ 191,500

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Year ended December 31, 2020 and 2019

(in thousands of Canadian dollars, except share and per share amounts, unless otherwise stated)

The Company manages its capital structure in accordance with changes in economic conditions. To maintain or adjust its capital structure, the Company may purchase shares for cancellation pursuant to an NCIB or SIB, issue new shares, or raise or retire the debt. In the current year, the Company took advantage of its surplus of cash by settling all of its long-term debt and bank indebtedness to reduce interest expense.

The Company is subject to covenants and restrictions related to its credit facilities as further described in Note 13 Bank Indebtedness. The Company was in compliance with the covenants as at and throughout the year ended December 31, 2020.

26. SUBSEQUENT EVENTS

On January 5, 2021, the Company acquired all of the issued and outstanding shares of Sensor Line GmbH ("Sensor Line"), a German-based ITS provider of fiber optic traffic sensors for road and rail markets for cash consideration of €3.8 million (approximately \$6.0 million). Sensor Line will be integrated into Quarterhill's wholly owned subsidiary, IRD. Annual gross revenues of Sensor Line for 2020 were approximately €2.4 million and total tangible assets at December 31, 2020 were approximately €2.3 million. The assessment of the purchase price and the accounting for this acquisition has not yet been finalized and certain IFRS 3 disclosures have not been included due to the timing of the acquisition.

27. EXPLANATION OF TRANSITION TO IFRS

As stated in Note 2, these are the Company's first consolidated financial statements prepared in accordance with IFRS as issued by the IASB.

The accounting policies set out in Note 2 have been applied in preparing these consolidated financial statements for the year ended and as at December 31, 2020, the comparative information for the year ended and as at December 31, 2019, and in the opening IFRS statement of financial position as at January 1, 2019 (the Company's date of transition).

In preparing its opening IFRS statement of financial position, the Company has adjusted amounts reported previously in financial statements prepared in accordance with US GAAP.

An explanation of the effect of the Company's transition to IFRS is summarized in this note:

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Year ended December 31, 2020 and 2019

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Reconciliation of Statements of Financial Position to IFRS as at December 31, 2019 and January 1, 2019

As at	December 31, 2019					January 1, 2019		
	US GAAP	IFRS adj.	IFRS	IFRS	Immaterial Corrections	IFRS	US GAAP	IFRS
	US\$	US\$	US\$	CAD\$	CAD\$	CAD\$	US\$	CAD\$
Current assets								
Cash and cash equivalents	\$ 67,422	\$ —	\$ 67,422	\$ 87,870	\$ —	\$ 87,870	\$ 63,929	\$ 87,029
Short-term investments	1,189	—	1,189	1,550	—	1,550	1,139	1,551
Restricted short-term investments	—	—	—	—	—	—	2,200	2,995
Accounts receivable	32,936	—	32,936	42,925	—	42,925	10,812	14,719
Other current assets	83	—	83	108	—	108	91	124
Unbilled revenue	6,879	—	6,879	8,965	—	8,965	3,990	5,432
Income taxes recoverable	105	—	105	137	—	137	198	270
Inventories (net of obsolescence)	6,576	—	6,576	8,570	—	8,570	5,960	8,114
Prepaid expenses and deposits	1,720	—	1,720	2,242	—	2,242	2,150	2,927
	116,910	—	116,910	152,367	—	152,367	90,469	123,161
Non-current assets								
Accounts receivable	2,951	—	2,951	3,846	—	3,846	415	565
Right-of-use assets, net	3,570	(116)	3,454	4,502	—	4,502	2,918	3,972
Property, plant and equipment, net	2,168	—	2,168	2,826	—	2,826	2,655	3,614
Intangible assets, net	68,699	—	68,699	89,534	—	89,534	87,425	119,015
Investment in joint venture	4,015	—	4,015	5,233	—	5,233	3,822	5,203
Deferred income tax assets	25,497	31	25,528	33,270	(533)	32,737	27,141	36,948
Goodwill	25,303	—	25,303	32,977	—	32,977	25,303	34,446
	132,203	(85)	132,118	172,188	(533)	171,655	149,679	203,763
TOTAL ASSETS	\$ 249,113	\$ (85)	\$ 249,028	\$ 324,555	\$ (533)	\$ 324,022	\$ 240,148	\$ 326,924
Liabilities								
Current liabilities								
Bank indebtedness	\$ 3,089	\$ —	\$ 3,089	\$ 4,026	\$ —	\$ 4,026	\$ 2,598	\$ 3,537
Accounts payable and accrued liabilities	19,762	—	19,762	25,755	509	26,264	18,103	24,644
Income taxes payable	156	—	156	203	—	203	—	—
Current portion of lease liabilities	766	—	766	998	—	998	823	1,120
Contingent liabilities	—	—	—	—	—	—	929	1,265
Current portion of deferred revenue	6,628	—	6,628	8,638	—	8,638	4,670	6,357
Current portion of long-term debt	45	—	45	59	—	59	299	407
	30,446	—	30,446	39,679	509	40,188	27,422	37,330
Non-current liabilities								
Deferred revenue	1,161	—	1,161	1,513	—	1,513	1,435	1,954
Long-term lease liabilities	2,724	—	2,724	3,550	—	3,550	1,913	2,604
Long-term debt	208	—	208	271	—	271	173	236
Deferred income tax liabilities	2,530	—	2,530	3,297	—	3,297	4,337	5,905
	6,623	—	6,623	8,631	—	8,631	7,858	10,699
TOTAL LIABILITIES	37,069	—	37,069	48,310	509	48,819	35,280	48,029
Shareholders' equity								
Capital stock	419,111	—	419,111	570,553	—	570,553	419,111	570,553
Contributed surplus	23,527	—	23,527	32,011	—	32,011	22,957	31,252
Accumulated other comprehensive income	16,797	—	16,797	10,936	—	10,936	16,243	22,112
Deficit	(247,391)	(85)	(247,476)	(337,255)	(1,042)	(338,297)	(253,443)	(345,022)
	212,044	(85)	211,959	276,245	(1,042)	275,203	204,868	278,895
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	\$ 249,113	\$ (85)	\$ 249,028	\$ 324,555	\$ (533)	\$ 324,022	\$ 240,148	\$ 326,924

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Year ended December 31, 2020 and 2019

(in thousands of Canadian dollars, except share and per share amounts, unless otherwise stated)

Reconciliation of Statement of Income (loss) to IFRS for the year ended December 31, 2019

	US GAAP	IFRS adj.	IFRS	IFRS	Immaterial Corrections	Viziya Disc. Ops.	IFRS
	US\$	US\$	US\$	CAD\$	CAD\$	CAD\$	CAD\$
Revenues							
Licensing	\$ 88,214	\$ —	\$ 88,214	\$ 117,174	\$ —	\$ 11,122	\$ 106,052
Intelligent Transportation Systems	58,506	—	58,506	77,635	—	10,762	66,873
	146,720	—	146,720	194,809	—	21,884	172,925
Direct cost of revenues							
Licensing	40,012	—	40,012	53,153	—	23	53,130
Intelligent Transportation Systems	33,821	—	33,821	44,887	—	2,000	42,887
	73,833	—	73,833	98,040	—	2,023	96,017
Gross profit	72,887	—	72,887	96,769	—	19,861	76,908
Operating expenses							
Depreciation of right-of-use assets	—	1,072	1,072	1,423	—	118	1,305
Depreciation of property, plant and equipment	1,112	—	1,112	1,478	—	182	1,296
Amortization of intangible assets	20,592	—	20,592	27,325	—	4,020	23,305
Selling, general and administrative expenses	28,722	(1,132)	27,590	36,595	—	9,876	26,719
Research and development expenses	5,133	(215)	4,918	6,525	—	3,651	2,874
Impairment losses on intangible assets	87	—	87	115	—	—	115
Special charges	2,173	—	2,173	3,073	509	1,134	2,448
	57,819	(275)	57,544	76,534	509	18,981	58,062
Results from operations	15,068	275	15,343	20,235	(509)	880	18,846
Finance income	(1,256)	—	(1,256)	(1,665)	—	—	(1,665)
Finance expense	394	178	572	761	—	21	740
Foreign exchange loss	266	—	266	355	—	31	324
Other income	(658)	—	(658)	(872)	—	(3)	(869)
Income before taxes	16,322	97	16,419	21,656	(509)	831	20,316
Current income tax expense	5,991	215	6,206	8,232	—	115	8,117
Deferred income tax (recovery) expense	(197)	(31)	(228)	(280)	533	(853)	1,106
Income tax expense	5,794	184	5,978	7,952	533	(738)	9,223
Net income from continuing operations	10,528	(87)	10,441	13,704	(1,042)	1,569	11,093
Net income from discontinued operations							\$ 1,569
Net income							\$ 12,662
Other comprehensive income (loss) that may be reclassified subsequently to net income:							
Foreign currency translation adjustment							(11,176)
Comprehensive income							\$ 1,486
Net income per share							
From continuing operations	\$ 0.09	\$ —	\$ 0.09	\$ 0.12	\$ —	\$ 0.01	\$ 0.09
From discontinued operations							0.01
Net income per share - Basic							\$ 0.10
From continuing operations	\$ 0.09	\$ —	\$ 0.09	\$ 0.12	\$ —	\$ 0.01	\$ 0.09
From discontinued operations							0.01
Net income per share - Diluted							\$ 0.10

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Year ended December 31, 2020 and 2019

(in thousands of Canadian dollars, except share and per share amounts, unless otherwise stated)

Reconciliation of Statement of Cash Flows to IFRS for the year ended December 31, 2019

	US GAAP	IFRS adj.	IFRS	IFRS	Immaterial Corrections	IFRS - Restated
	US\$	US\$	US\$	CAD\$	CAD\$	CAD\$
Cash generated from (used in) operations						
Net income from continuing operations	\$ 10,528	\$ (87)	\$ 10,441	\$ 13,704	\$ (1,042)	\$ 11,093
Non-cash items						
Stock-based compensation expense	570	—	570	758	—	693
Depreciation of right-of-use assets	—	1,072	1,072	1,365	—	1,305
Interest expense on lease liabilities	—	178	178	231	—	231
Depreciation and amortization	21,704	—	21,704	28,807	—	24,601
Foreign exchange gain	(85)	—	(85)	(113)	—	(113)
Equity in earnings from joint venture	(659)	—	(659)	(873)	—	(873)
Loss on disposal of intangible assets	156	—	156	206	—	206
Impairment losses on intangible assets	87	—	87	115	—	115
Loss on disposal of assets	557	—	557	746	—	746
Deferred income tax expense (recovery)	(198)	(31)	(229)	(277)	533	1,106
Long-term accounts receivable	(2,600)	—	(2,600)	(3,433)	—	(85)
Embedded derivatives	8	—	8	11	—	11
Contingent consideration adjustment	(929)	—	(929)	(1,042)	—	(1,042)
Changes in non-cash working capital balances	(21,605)		(21,605)	(28,332)	509	(29,368)
Cash generated from continuing operations	7,534	1,132	8,666	11,873	—	8,626
Net cash flows attributable to discontinuing operations						3,247
Net cash generated from operating activities						11,873
Financing						
Dividends paid	(4,476)	—	(4,476)	(5,939)	—	(5,939)
Bank indebtedness	491	—	491	682	—	685
Payment of lease liabilities	—	(1,132)	(1,132)	(1,504)	—	(1,504)
Repayment of long-term debt	(219)	—	(219)	(294)	—	(265)
Cash used in continuing operations	(4,204)	(1,132)	(5,336)	(7,055)	—	(7,023)
Net cash flows attributable to discontinuing operations	—	—	—	—	—	(32)
Net cash used in financing activities	(4,204)	(1,132)	(5,336)	(7,055)	—	(7,055)
Investing						
Dividends received from joint venture	389	—	389	513	—	513
Proceeds from sale of restricted short-term investments	2,200	—	2,200	2,904	—	2,904
Proceeds from sale of property, plant and equipment	33	—	33	43	—	43
Purchase of property and equipment	(1,111)	—	(1,111)	(1,474)	—	(1,301)
Purchase of intangible assets	(1,429)	—	(1,429)	(1,889)	—	(1,890)
Cash used in continuing operations	82	—	82	97	—	269
Net cash flows attributable to discontinuing operations	—	—	—	—	—	(172)
Net cash used in investing activities	82	—	82	97	—	97
FX gain (loss) on cash held in foreign currency	80	—	80	(4,074)	—	(4,074)
Net increase in cash and cash equivalents	\$ 3,492	\$ —	\$ 3,492	\$ 841	\$ —	\$ 841
Cash and cash equivalents, beginning of	63,929	—	63,929	87,029	—	87,029
Cash and cash equivalents, end of	\$ 67,421	\$ —	\$ 67,421	\$ 87,870	\$ —	\$ 87,870

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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Notes to Reconciliations

Leases

Under US GAAP, all leases recognized by the Company were classified as operating leases and subsequently accounted for as a straight-line expense over the lease term. This expense consists of interest on the accretion of the lease liabilities, calculated using the effective interest rate method, and depreciation of the ROU assets, which is calculated based on the difference in the interest expense and the total straight-line lease expense.

IFRS does not distinguish between operating and finance leases for lessees. A single recognition and measurement model is applied to all leases where the reporting entity acts in the capacity as the lessee. While the effective interest rate method is used to subsequently measure the accretion of the lease liability (the interest expense), similar to US GAAP, the subsequent measurement for the ROU asset differs. Under IFRS, the Company will depreciate the ROU assets at the shorter of the estimated useful life and the lease term, on a straight-line basis. Additionally, while all costs relating to leases are recognized as operating expenses under US GAAP, under IFRS the interest expense is classified as a finance expense outside of the line, "Results from operations" whereas depreciation expense continues to be recognized within operating expenses. These classification differences also resulted in corresponding changes to the statement of cash flows.

IFRS 1 "First-time adoption of International Financial Reporting Standards"

IFRS 1 "First-time adoption of International Financial Reporting Standards" sets out the reporting requirements when IFRS is adopted for the first time. The Company is required to establish its IFRS accounting policies for the period ended December 31, 2020 and apply those policies retrospectively to determine the Company's consolidated statement of financial position at the date of transition, January 1, 2019. IFRS 1 provides for a number of mandatory exceptions from full retrospective application of IFRS standards effective as of the end of the Company's first IFRS reporting period. None of these mandatory exceptions had a material impact on the Company's transition to IFRS. Also, in accordance with IFRS 1, the Company tested goodwill for impairment at the date of transition to IFRS. There was no impairment recognized on goodwill at January 1, 2019.

IFRS 1 also provides certain optional exemptions from full retrospective application, that may be elected by first-time adopters of IFRS. As part of the transition, the Company elected the following optional exemptions:

Business Combinations

The Company has elected to apply IFRS 3, "Business Combinations", prospectively from January 1, 2019. As such, US GAAP balances relating to business combinations entered into before that date, including goodwill, have been carried forward without adjustment.

US GAAP revaluation for impaired assets as deemed cost

The Company has elected to record certain of its intangible assets (patent licenses) in the opening statement of financial position on the transition date at its US GAAP revaluation of its previously impaired patent licenses, adjusted for any subsequent changes to amortization based on differences between US GAAP and IFRS, as these assets' deemed cost at the date of transition.

Revenue from contracts with customers

The Company elected to apply select transition provisions per IFRS 15, "Revenue From Contracts with Customers" upon transition to IFRS. In doing so, the Company will:

- not restate contracts that were completed upon transition to IFRS; completed contracts are determined to be contracts for which the Company has transferred all of the goods or services identified in accordance with the Company's previous US GAAP;
- for contracts that were modified before the Company's IFRS transition date, the Company has considered the aggregate effect of all modifications when identifying the satisfied and unsatisfied

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Year ended December 31, 2020 and 2019

(in thousands of Canadian dollars, except share and per share amounts, unless otherwise stated)

performance obligations, determining the transaction price, and allocating the transaction price to satisfied and unsatisfied performance obligations; and

- for all reporting periods presented before the Company's IFRS transition date, not disclose the amount of the transaction price allocated to the remaining performance obligations and an explanation of when the entity expects to recognize that amount as revenue.

Leases

The Company elected to apply select transition provisions per IFRS 16, "Leases" upon transition to IFRS. In doing so, the Company has elected to:

- measure the lease liability at January 1, 2019 at the present value of remaining lease payments, discounted using the Company's incremental borrowing rate at January 1, 2019;
- measure the ROU asset at January 1, 2019 at an amount equal to the corresponding lease liability, adjusted by the amount of any prepaid or accrued lease payments relating to that lease recognized in the statement of financial position immediately before January 1, 2019;
- apply IAS 36 to ROU assets at January 1, 2019;
- not recognize ROU assets and lease liabilities for short-term leases that have a lease term of 12 months or less and leases of low-value assets;
- exclude initial direct costs from the measurement of the ROU asset at January 1, 2019; and
- use hindsight in determining if the lease term of the contract contains options to extend or terminate the lease.

Share-based payments

The Company has elected not to retrospectively apply IFRS 2, "Share-based Payments" to equity instruments that were granted and had vested before the transition date. As a result of applying this exemption, the Company applied the provision of IFRS 2 to any outstanding equity instruments that are unvested as at the date of transition to IFRS.

Foreign currency transactions and advance consideration

The Company has elected not to apply IFRIC 22, "Foreign Currency Transactions and Advance Consideration" to assets, expenses and income recognized before the date of transition to IFRS.