

Consolidated Financial Statements
(In Canadian dollars)

TERRA FIRMA CAPITAL CORPORATION

Years ended December 31, 2014 and 2013



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INDEPENDENT AUDITORS' REPORT

To the Shareholders of Terra Firma Capital Corporation

We have audited the accompanying consolidated financial statements of Terra Firma Capital Corporation, which comprise the consolidated statements of financial position as at December 31, 2014 and 2013, the consolidated statements of income and comprehensive income, changes in equity and cash flows for the years then ended, and notes, comprising a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards, 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.

Auditors' Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements 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 entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

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

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the consolidated financial position of Terra Firma Capital Corporation as at December 31, 2014 and 2013, and its consolidated financial performance and its consolidated cash flows for the years then ended in accordance with International Financial Reporting Standards.

Chartered Professional Accountants, Licensed Public Accountants

March 25, 2015
Toronto, Canada

TERRA FIRMA CAPITAL CORPORATION

Consolidated Statements of Financial Position
(In Canadian dollars)

December 31, 2014 and 2013

	2014	2013
Assets		
Cash and cash equivalents	\$ 1,083,745	\$ 7,721,115
Funds held in trust	834,065	383,526
Amounts receivable and prepaid expenses (note 4)	2,058,846	1,661,352
Loan and mortgage investments (note 5)	78,635,796	55,278,303
Investment properties held in joint operations (note 6)	2,062,661	7,671,452
Portfolio investments (note 7)	1,620,828	954,073
Deferred income tax asset	48,381	–
	<u>\$ 86,344,322</u>	<u>\$ 73,669,821</u>

Liabilities and Equity

Liabilities:

Accounts payable and accrued liabilities (note 8)	\$ 2,227,308	\$ 1,366,708
Provision for discontinued operations (note 9)	27,500	321,490
Unearned income	639,307	472,924
Income taxes payable	341,432	82,375
Deferred income tax liability	–	6,348
Short-term unsecured loans payable (note 10)	1,500,000	–
Loan and mortgage syndications (note 5)	45,390,821	42,889,374
Mortgages payable (note 6)	1,151,118	3,680,547
Convertible debentures (note 11)	10,514,431	10,125,074
Total liabilities	<u>61,791,917</u>	<u>58,944,840</u>

Equity:

Share capital (note 13(a))	16,654,718	10,795,790
Equity component of convertible debentures (note 11)	284,490	–
Contributed surplus (notes 13(b) and 14)	1,049,585	603,962
Retained earnings	6,352,957	3,125,229
Total shareholders' equity	<u>24,341,750</u>	<u>14,524,981</u>
Non-controlling interest	210,655	200,000
Total equity	<u>24,552,405</u>	<u>14,724,981</u>

Commitments and contingencies (note 12)

	<u>\$ 86,344,322</u>	<u>\$ 73,669,821</u>
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See accompanying notes to consolidated financial statements.

The consolidated financial statements were approved
by the Board on March 25, 2015 and signed on its behalf by:

"John Kaplan" _____ Director

"Seymour Temkin" _____ Director

TERRA FIRMA CAPITAL CORPORATION

Consolidated Statements of Income and Comprehensive Income
(In Canadian dollars)

Years ended December 31, 2014 and 2013

	2014	2013
Revenue:		
Interest and fees	\$ 12,127,716	\$ 8,454,163
Rental (note 6)	257,595	451,335
	<u>12,385,311</u>	<u>8,905,498</u>
Expenses (income):		
Property operating costs (note 6)	87,751	287,078
General and administrative	1,996,205	1,476,156
Share-based compensation (note 13(b))	809,109	39,208
Interest (note 17)	6,054,690	4,742,023
Gain on conversion of interest in joint operation (note 6)	(487,000)	—
Fair value adjustment - investment properties (note 6)	(147,950)	78,287
Fair value adjustment - portfolio investment (note 7)	(66,755)	—
	<u>8,246,050</u>	<u>6,622,752</u>
Income from operations before income taxes	4,139,261	2,282,746
Income taxes (note 18)	1,052,522	582,919
Income from continuing operations	3,086,739	1,699,827
Income from discontinued operations (note 9)	151,644	—
Net income and comprehensive income	\$ 3,238,383	\$ 1,699,827
Net income and comprehensive income attributable to:		
Common shareholders	\$ 3,227,728	\$ 1,699,827
Non-controlling interest	10,655	—
	<u>\$ 3,238,383</u>	<u>\$ 1,699,827</u>
Earnings per share (note 15):		
Continuing operations:		
Basic	\$ 0.10	\$ 0.06
Diluted	0.08	0.05
Discontinued operations:		
Basic	—	—
Diluted	—	—

See accompanying notes to consolidated financial statements.

TERRA FIRMA CAPITAL CORPORATION

Consolidated Statements of Changes in Equity
(In Canadian dollars)

Years ended December 31, 2014 and 2013

	Share capital		Equity component of convertible debentures (note 11)	Contributed surplus (notes 13(b) and 14)	Retained earnings	Total shareholders' equity	Non- controlling interest	Total equity
	Number of shares (note 13(a))	Amount						
Balance, December 31, 2012	30,695,000	\$ 10,757,405	\$ —	\$ 573,139	\$ 1,425,402	\$ 12,755,946	\$ 200,000	\$ 12,955,946
Issuance of shares pursuant to share option plan	150,000	38,385	—	(8,385)	—	30,000	—	30,000
Share-based compensation	—	—	—	39,208	—	39,208	—	39,208
Net income and comprehensive income	—	—	—	—	1,699,827	1,699,827	—	1,699,827
Balance, December 31, 2013	30,845,000	10,795,790	—	603,962	3,125,229	14,524,981	200,000	14,724,981
Issuance of shares pursuant to Offering, net of share issue costs	9,587,300	5,190,543	—	106,235	—	5,296,778	—	5,296,778
Issuance of shares pursuant to private placement	1,000,000	630,000	—	—	—	630,000	—	630,000
Issuance of shares pursuant to share option plan	150,000	38,385	—	(8,385)	—	30,000	—	30,000
Share-based compensation	—	—	—	347,773	—	347,773	—	347,773
Issuance of convertible debentures, equity component	—	—	284,490	—	—	284,490	—	284,490
Net income and comprehensive income	—	—	—	—	3,227,728	3,227,728	10,655	3,238,383
Balance, December 31, 2014	41,582,300	\$ 16,654,718	\$ 284,490	\$ 1,049,585	\$ 6,352,957	\$ 24,341,750	\$ 210,655	\$ 24,552,405

See accompanying notes to consolidated financial statements.

TERRA FIRMA CAPITAL CORPORATION

Consolidated Statements of Cash Flows
(In Canadian dollars)

Years ended December 31, 2014 and 2013

	2014	2013
Cash provided by (used in):		
Operating activities:		
Income from continuing operations	\$ 3,086,739	\$ 1,699,827
Interest and fees earned	(12,127,716)	(8,454,163)
Interest expense	6,054,690	4,742,023
Non-cash items:		
Share-based compensation (note 13(b))	809,109	39,208
Gain on conversion of interest in joint operation	(487,000)	-
Fair value adjustment - investment properties	(147,950)	78,287
Fair value adjustment - portfolio investment	(66,755)	-
Income tax provision	1,052,522	582,919
Change in non-cash operating items:		
Decrease (increase) in other receivables	(119,611)	1,343,610
Increase in prepaid expenses and deposits	(136,156)	(88,678)
Increase (decrease) in accounts payable and accrued liabilities	524,490	(299,001)
Interest and fees received	8,913,755	6,650,694
Interest paid	(7,462,690)	(4,390,886)
Income taxes paid	(902,869)	(984,095)
Cash provided by (used in) operating activities - continuing operations	(1,009,442)	919,745
Cash used in operating activities - discontinued operations (note 9)	(87,671)	(124,467)
Cash provided by (used in) operating activities	(1,097,113)	795,278
Financing activities:		
Proceeds from loan and mortgage syndications	25,740,188	35,493,200
Repayments of loan and mortgage syndications	(23,628,514)	(10,249,514)
Repayments of mortgages payable	(29,429)	(79,835)
Proceeds from short-term loans payable	5,120,000	-
Repayment of short-term loans payable	(3,620,000)	-
Proceeds from issuance of convertible debentures, net of issue costs	4,545,950	-
Repayment of convertible debentures	(3,925,000)	-
Proceeds from issuance of shares pursuant to the Offering, net of issue costs (note 13(a))	5,296,778	-
Proceeds from issuance of shares pursuant to private placement (note 13(a))	630,000	-
Proceeds from issuance of shares pursuant to share options plan	30,000	30,000
Cash provided by financing activities	10,159,973	25,193,851
Investing activities:		
Funding of loan and mortgage investments	(40,192,633)	(40,276,867)
Repayments of loan and mortgage investments	25,619,567	19,292,248
Capital additions to investment properties (note 6)	(76,625)	(119,087)
Increase in funds held in trust	(450,539)	(383,526)
Portfolio investment	(600,000)	(4,073)
Cash used in investing activities	(15,700,230)	(21,491,305)
Increase (decrease) in cash and cash equivalents	(6,637,370)	4,497,824
Cash and cash equivalents, beginning of year	7,721,115	3,223,291
Cash and cash equivalents, end of year	\$ 1,083,745	\$ 7,721,115

See accompanying notes to consolidated financial statements.

TERRA FIRMA CAPITAL CORPORATION

Notes to Consolidated Financial Statements
(In Canadian dollars)

Years ended December 31, 2014 and 2013

1. Reporting entity:

Terra Firma Capital Corporation (the "Company") was incorporated under the Business Corporations Act (Ontario) on July 26, 2007. The common shares of the Company ("Shares") trade on the TSX Venture Exchange (the "Exchange") under the symbol TII. The registered office of the Company is located at 5000 Yonge Street, Suite 1502, Toronto, Ontario, M2N 7E9. The principal business of the Company is to provide real estate financings secured by investment properties and real estate developments throughout Canada and the United States. These financings are made to real estate developers and owners who require shorter-term loans to bridge a transitional period of one to five years where they require capital at various stages of development or redevelopment property, for such development or redevelopment, property repairs or the purchase of investment property.

2. Basis of presentation:

(a) Statement of compliance:

These consolidated financial statements of the Company have been prepared by management in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB") as well as Interpretations of the International Financial Reporting Interpretations Committee ("IFRIC").

(b) Basis of presentation:

The Company holds its interests in certain joint operations and portfolio investment in its wholly owned subsidiaries which are controlled by the Company. For accounting purposes, control is established by an investor when it is exposed to, or has rights to, variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity. The Company's principal subsidiaries are Terra Firma MA Ltd. (100% owned), Terra Firma Queen Developments Inc. (100% owned), Terra Firma Capital (Hill) Corporation (the "Hill") (78.95% owned), and TFCC LanQueen Ltd. (100% owned). The financial statements of these subsidiaries and the Company's proportionate share in joint operations are consolidated with those of the Company and all intercompany transactions and balances between the Company and its subsidiary entities and joint operations have been eliminated upon consolidation.

Non-controlling interest represents equity interest in the Hill owned by an outside party. The share of net assets of the Hill attributable to non-controlling interest is presented as a component of equity.

TERRA FIRMA CAPITAL CORPORATION

Notes to Consolidated Financial Statements (continued)
(In Canadian dollars)

Years ended December 31, 2014 and 2013

2. Basis of presentation (continued):

(c) Basis of measurement:

These consolidated financial statements have been prepared on a historical cost basis, except for investment properties held in joint operations, portfolio investments, financial instruments classified at fair value through profit or loss and non-controlling interests, which are stated at their fair values.

(d) Functional and presentation currency:

These consolidated financial statements have been presented in Canadian dollars, which is the Company's functional currency.

(e) Critical judgments and estimates:

The preparation of the consolidated financial statements requires management to make estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, the disclosure of contingent assets and liabilities at the dates of the consolidated financial statements and the reported amounts of income and expenses during the year. Actual results may differ from these estimates.

In making estimates, the Company relies on external information and observable conditions where possible, supplemented by internal analysis as required. Those estimates and judgments have been applied in a manner consistent with the prior period and there are no known trends, commitments, events or uncertainties that the Company believes will materially affect the methodology or assumptions utilized in making those estimates and judgments in these consolidated financial statements. The areas involving a higher degree of judgment or complexity, or areas where assumptions and estimates are significant to the consolidated financial statements are disclosed separately in notes 3(c), 6, 7 and 13.

Changes to estimates and assumptions may affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the dates of these consolidated financial statements and the reported amounts of revenue and expenses during the years. Actual results could also differ from those estimates under different assumptions and conditions.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the year in which the estimates are revised and in any future years affected.

TERRA FIRMA CAPITAL CORPORATION

Notes to Consolidated Financial Statements (continued)
(In Canadian dollars)

Years ended December 31, 2014 and 2013

3. Significant accounting policies:

The Company's accounting policies and its standards of financial disclosure set out below are in accordance with IFRS and have been applied consistently to all periods presented in these consolidated financial statements, unless otherwise stated.

(a) Cash and cash equivalents:

Cash and cash equivalents include unrestricted cash and short-term investments. Short-term investments, comprising money market instruments, have a maturity of 90 days or less at their date of purchase and are stated at cost, which approximates net realizable value.

(b) Funds held in trust:

Funds held in trust are comprised of cash balances that are deposited and held in trust within a wholly owned subsidiary of the Company that administers loan and mortgage investments. The restricted deposits are subject to future loan and mortgage contractual obligations and are therefore restricted in access until all the contractual payout conditions are met. Funds held in trust are carried at amortized cost which approximates their fair value. The corresponding liability is included in accounts payable and accrued liabilities.

(c) Loan and mortgage investments:

The loan and mortgage investments are recognized initially at fair value plus any directly attributable transaction costs. Subsequent to initial recognition, the loan and mortgage investments are measured at amortized cost using the effective interest rate method (the "EIM"). The loan and mortgage investments are derecognized when the contractual rights to receive cash flows and benefits expire, or where they have been transferred and the Company also transfers the control or substantially all the risks and rewards of ownership.

The loan and mortgage investments are assessed each reporting period to determine whether there is any objective evidence of impairment and are considered to be impaired if one or more loss events that have occurred after its initial recognition, have a negative effect on the estimated future cash flows of the financial asset and the loss can be reliably measured.

TERRA FIRMA CAPITAL CORPORATION

Notes to Consolidated Financial Statements (continued)
(In Canadian dollars)

Years ended December 31, 2014 and 2013

3. Significant accounting policies (continued):

If there is objective evidence of an impairment loss, the loss is based on the difference between the carrying amount of the loan and mortgage investment, and the respective estimated future cash flows discounted at the loan and mortgage investment's original effective interest rate and is recorded as an allowance for losses and recognized in the consolidated statements of income and comprehensive income. If, in a subsequent period, the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognized, the previously recognized impairment is reversed to the extent of the impairment amount.

(d) Joint arrangements:

A joint arrangement is a contractual arrangement pursuant to which the Company and other parties undertake an economic activity that is subject to joint control whereby the strategic financial and operating policy decisions relating to the activities of the activities of the joint arrangement require the unanimous consent of the parties sharing control. Joint arrangements are of two types - joint ventures and joint operations.

The Company's significant joint arrangements consist of joint operations, which are structured through a direct interest in the joint venture's assets, rather than through the establishment of a separate entity, the arrangement is referred to as joint operations and the Company's proportionate share of joint venture assets, liabilities, revenues and expenses are recognized in the consolidated financial statements and classified according to their nature. When the Company transacts with its joint operations, unrealized profits and losses are eliminated to the extent of the Company's interest in the joint operations. Balances outstanding between the Company and joint operations in which it has an interest are eliminated in the consolidated statements of financial position.

(e) Investments properties:

Investment properties include properties held to earn rental income or for capital appreciation, or for both, and properties that are being constructed or developed for future use as investment properties. On acquisition, investment properties are initially recorded at cost. Subsequent to initial recognition, investment properties are carried at fair value. Gains or losses arising from changes in fair values are recognized in the consolidated statements of income and comprehensive income during the period in which they arise.

TERRA FIRMA CAPITAL CORPORATION

Notes to Consolidated Financial Statements (continued)
(In Canadian dollars)

Years ended December 31, 2014 and 2013

3. Significant accounting policies (continued):

(f) Financial instruments:

Financial assets and liabilities are recognized when the Company becomes a party to the contractual provisions of the financial instrument. Financial assets are derecognized when the contractual rights to receive cash flows and benefits related to the financial asset expire, or if the Company transfers the control or substantially all the risks and rewards of ownership of the financial asset or transfers the significant risks and rewards, along with the unconditional ability to sell or pledge the asset to another party. Financial liabilities are derecognized when obligations under the contract expire, are discharged or cancelled.

Financial assets and liabilities are offset and the net amount is reported in the consolidated statements of financial position when there is a legally enforceable right to offset the recognized amounts and there is an intention to settle on a net basis, or realize the asset and settle the liability simultaneously.

Upon initial recognition, financial instruments are measured at fair value and classified as either financial assets or financial liabilities at fair value through profit or loss, held-to-maturity investments, available-for-sale assets, loans and receivables, other financial liabilities or as derivatives designated as hedging instruments in an effective hedge.

Financial instruments are included on the consolidated statements of financial position and measured at fair value, except for loans and receivables, held-to-maturity financial assets and other financial liabilities, which are measured at amortized cost using the EIM, less any impairment. Directly attributable transaction costs other than those related to financial instruments classified as fair value through profit or loss, which are expensed as incurred, are capitalized to the carrying amount of the instrument and amortized using the EIM.

Under the EIM, interest income and expense are calculated and recorded using the effective interest rate which is the rate that exactly discounts estimated future cash receipts or payments throughout the expected life of the financial instrument to the fair value at initial recognition.

The Company's financial assets include cash and cash equivalents, funds held in trust, amounts receivable, portfolio investments and loan and mortgage investments. All of the Company's financial assets other than the portfolio investment which is classified as fair value through profit or loss are classified as loans and receivables.

TERRA FIRMA CAPITAL CORPORATION

Notes to Consolidated Financial Statements (continued)
(In Canadian dollars)

Years ended December 31, 2014 and 2013

3. Significant accounting policies (continued):

The Company's financial liabilities include the accounts payable and accrued liabilities, provision for discontinued operations, income taxes payable, loan and mortgage syndications, short-term loans payable, mortgages payable and liability component of convertible debentures. All of the Company's financial liabilities are classified as other liabilities.

The Company had neither available-for-sale, nor held-to-maturity instruments as at December 31, 2014 and 2013.

(g) Compound financial instruments:

Compound financial instruments issued by the Company comprise convertible debentures that can be converted to Shares of the Company at the option of the holder, and the number of shares to be issued does not vary with changes in their fair value. The liability component of a compound financial instrument is recognized initially at the fair value of a similar liability that does not have an equity conversion option. The equity component is recognized initially as the difference between the fair value of the compound financial instrument as a whole and the fair value of the liability component. All transaction costs directly attributable to the issuance of the compound financial instrument are allocated to the liability and equity components in proportion to their initial carrying amounts.

Subsequent to initial recognition, the liability component of a compound financial instrument is measured at amortized cost using the EIM. The equity component of a compound financial instrument is not re-measured subsequent to initial recognition. Interest, losses and gains relating to the financial liability are recognized in the consolidated statements of income and comprehensive income.

(h) Impairment of financial instruments:

An assessment of whether there is objective evidence that a financial asset or a group of financial assets is impaired is performed at each reporting period. A financial asset is considered to be impaired if one or more loss events have occurred that have a negative impact on the future cash flows of the financial asset after initial recognition of the financial asset and the loss can be reliably measured. These assumptions are limited by the availability of reliable comparable market data, economic uncertainty and the uncertainty of future events. Accordingly, by their nature, estimates of impairment are subjective and may not necessarily be comparable to the actual outcome. Should the underlying assumptions change, the estimated future cash flows could vary.

TERRA FIRMA CAPITAL CORPORATION

Notes to Consolidated Financial Statements (continued)
(In Canadian dollars)

Years ended December 31, 2014 and 2013

3. Significant accounting policies (continued):

If there is objective evidence that an impairment loss on loans and receivables carried at amortized cost has occurred, the loss is based on the difference between the carrying amount of the financial asset, and the respective estimated future cash flows discounted at the financial instrument's original effective interest rate and is recorded as an allowance for losses and recognized in the consolidated statements of income and comprehensive income. If, in a subsequent period, the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognized, the previously recognized impairment is reversed up to the extent of the original impairment amount.

In the determination of impairment, the Company assesses the existence of certain factors, including; non-payment of interest and or principal or other material default by the borrower, financial difficulty of the underlying secured asset, financial difficulty of the borrower and or guarantor, the Company granting certain concessions favorable to the borrower and observable data that there is a measurable decrease in the estimated future cash flows.

(i) De-recognition of financial instruments:

A financial asset is de-recognized if substantially all risks and rewards of ownership and, in certain circumstances, control of the financial asset are transferred. A financial liability is de-recognized when it is extinguished, with any gain or loss on extinguishment to be recognized in other items in the consolidated statements of income and comprehensive income.

(j) Unearned income:

Unearned income includes commitment fees received from borrowers, which are amortized over the contractual terms of the respective loan and mortgage investments.

(k) Share capital:

Common shares are classified as equity. Incremental costs directly attributable to the issuance of common shares are recognized as a deduction from equity.

TERRA FIRMA CAPITAL CORPORATION

Notes to Consolidated Financial Statements (continued)
(In Canadian dollars)

Years ended December 31, 2014 and 2013

3. Significant accounting policies (continued):

(l) Revenue recognition:

(i) Interest and fees earned:

Interest and fees earned is recognized in the consolidated statements of income and comprehensive income using the EIM. The EIM discounts the estimated future cash receipts through the expected life of the loan and mortgage to its carrying amount. When estimating future cash flows, the contractual terms of the mortgage are considered including origination revenue, interest receipts, principal receipts and contractual end of term participation receipts where applicable. Participation receipts that are contingent upon future events such as the profitability of the underlying security are not included in the estimated cash flows. Such amounts are recorded in income when management is reasonably assured of their collection.

(ii) Rental income:

The Company has retained substantially all of the risks and benefits of ownership of its investment properties and, therefore, accounts for its leases with tenants as operating leases. Rental income from these leases is recognized in the consolidated statements of income and comprehensive income on a straight-line basis over the term of the relevant leases.

(m) Share-based compensation:

The Company has a share option plan for grants to eligible directors, officers, senior management and consultants under its share option plan. No awards have been issued to consultants. The expense of the equity-settled incentive option plan is measured based on fair value of the options granted of each tranche at the grant date. The expense is recognized in proportion to the vesting features of each tranche of the grant and is reflected in equity. When share options are exercised, any consideration paid, together with the amount recorded in equity, are recorded in share capital.

(n) Deferred share unit plan:

In May 2014, the Company established and adopted a cash-settled Deferred Share Unit Plan (the "DSU Plan") for employees and directors whereby the Company's Board of Directors may award Deferred Share Units (the "DSUs") as compensation for services rendered.

TERRA FIRMA CAPITAL CORPORATION

Notes to Consolidated Financial Statements (continued)
(In Canadian dollars)

Years ended December 31, 2014 and 2013

3. Significant accounting policies (continued):

The fair value of DSUs granted is measured at the grant date based on the five day volume weighted average trading price of the Company's Shares, and compensation expense is recognized in proportion to the vesting features over the vesting period with the recognition of a corresponding liability that is included in accounts payable and accrued liabilities. The liability is re-measured at each reporting date at fair value with changes in fair value recognized on the consolidated statements of income and comprehensive income.

(o) Provisions:

Provisions for legal claims, where applicable, are recognized in other liabilities when the Company has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources will be required to settle the obligation, and the amount can be reliably estimated. Provisions are measured at management's best estimate of the expenditure required to settle the obligation at the end of the reporting period, and are discounted to present value where the effect is material.

(p) Income taxes:

Income tax comprises current and deferred tax. Income tax is recognized in the consolidated statements of income and comprehensive income except to the extent that it relates to items recognized directly in equity, in which case the income tax is also recognized directly in equity.

Current tax is the expected tax payable on the taxable income for the reporting period, using tax rates enacted, or substantively enacted, at the end of the reporting period.

Deferred tax is determined based on the temporary differences between the carrying value and the tax basis of the assets and liabilities. Any change in the net amount of deferred income tax assets and liabilities is included in income. Deferred income tax assets and liabilities are determined based on enacted or substantially enacted tax rates and laws which are expected to apply to the Company's taxable income for the period in which the assets and liabilities will be recovered or settled. Deferred income tax assets are recognized when it is probable that there will be sufficient taxable income against which to utilize the benefits of the temporary differences.

Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realized.

TERRA FIRMA CAPITAL CORPORATION

Notes to Consolidated Financial Statements (continued)
(In Canadian dollars)

Years ended December 31, 2014 and 2013

3. Significant accounting policies (continued):

(q) Foreign currency translation:

Investment transactions and income and expenses in foreign currencies have been translated into Canadian dollars at the rates of exchange prevailing at the time of the transactions. The fair value of mortgages and cash denominated in foreign currencies has been translated into Canadian dollars at the rates of exchange prevailing at year end. Foreign exchange gains and losses on the receipts of payments on mortgage investments are included in interest and fees on the consolidated statements of income and comprehensive income.

(r) Earnings per share:

Basic earnings per share is calculated by dividing the net income attributable to shareholders of the Company by the weighted average number of Shares outstanding during the period.

Diluted earnings per share is calculated using the "if converted method" and is determined by adjusting the net income attributable to shareholders and the weighted average number of Shares outstanding, adjusted for the dilutive effects of all convertible debentures and granted share options and broker warrants.

(s) Adoption of recent accounting pronouncements:

The Company has adopted the following new and revised standards, along with any consequential amendments, effective January 1, 2014. These changes were made in accordance with the applicable transitional provisions.

- (i) IFRIC 21 - Levies, addresses accounting for a liability to pay a levy within the scope of International Accounting Standard ("IAS") 37, Provisions, Contingent liabilities and Contingent Assets. A levy is an outflow of resources embodying economic benefits that is imposed by governments on entities in accordance with legislation, other than income taxes within the scope of IAS 12, Income Taxes, and fines or other penalties imposed for breaches of the legislation. The standard is applied retrospectively. The implementation of this standard had no impact on these consolidated financial statements.

TERRA FIRMA CAPITAL CORPORATION

Notes to Consolidated Financial Statements (continued)
(In Canadian dollars)

Years ended December 31, 2014 and 2013

3. Significant accounting policies (continued):

- (ii) IAS 32, Financial Instruments - Presentation ("IAS 32"), updates the application guidance in IAS 32, to clarify that the right to offset financial assets and financial liabilities must be available on the current date and cannot be contingent on a future event. The amendments to IAS 32 are effective for fiscal periods beginning on or after January 1, 2014. The adoption of this amendment did not result in any changes to the consolidated financial statements.

(t) New standards not yet adopted:

Certain new standards, amendments and interpretations have been published that are mandatory for the Company's accounting periods beginning on or after January 1, 2015 that the Company has decided not to early adopt. The following are standards, amendments and interpretations that may be relevant to the Company in preparing its consolidated financial statements in future periods:

- (i) IFRS 9, Financial Instruments ("IFRS 9"), was issued to replace IAS 39, Financial Instruments - Recognition and Measurement. IFRS 9 has two measurement categories: amortized cost and fair value. The basis of classification depends on the entity's business model and the contractual cash flow characteristics of the financial asset. All equity instruments are measured at fair value. A debt instrument is measured at amortized cost only if the entity is holding it to collect contractual cash flows and the cash flows represent principal and interest. Otherwise, it is measured at fair value through profit and loss. This standard is effective for years beginning on or after January 1, 2018. The extent of impact of adoption of IFRS 9 has not been determined.
- (ii) IFRS 15, Revenue from Contracts with Customers ("IFRS 15"), provides a comprehensive framework for recognition, measurement and disclosure of revenue from contracts with customers, excluding contracts within the scope of the standard on leases, insurance contracts and financial instruments. IFRS 15 becomes effective for annual periods beginning on or after January 1, 2017 and is to be applied retrospectively. Early adoption is permitted. The Company is currently assessing the impact of the new standard on its consolidated financial statements.

TERRA FIRMA CAPITAL CORPORATION

Notes to Consolidated Financial Statements (continued)
(In Canadian dollars)

Years ended December 31, 2014 and 2013

4. Amounts receivable and prepaid expenses:

The following table presents details of the amounts receivable and prepaid expenses as at December 31, 2014 and 2013:

	2014	2013
Interest receivable	\$ 1,762,120	\$ 1,498,359
Other receivables	196,162	61,116
Prepaid expenses and deposits	100,564	101,877
Amounts receivable and prepaid expenses	\$ 2,058,846	\$ 1,661,352

Included in interest receivable are non-current balances of \$562,871 (2013 - \$74,769). The remaining interest and other receivables are current and due in the current fiscal year in accordance with contract terms.

During the year ended December 31, 2014, the Company converted \$1,666,000 (2013 - nil) of interest receivable to loan and mortgage investments (note 5).

5. Loan and mortgage investments and loan and mortgage syndications:

As at December 31, 2014 and 2013, the Company had principal balance of loan and mortgage investments of \$78,635,796 and \$55,278,303, respectively. The loan and mortgage investments carry a weighted average effective interest rate of 19.6% (2013 - 18.6%) and a weighted average term to maturity of 0.86 years (2013 - 1.21 years).

The loans are on most major real estate property types, but predominantly within the residential and commercial asset groups. In some cases land loans will subsequently be subordinated to construction financing as the project progresses through its development period. The loan and mortgage investments are secured by mortgages registered on title and/or other forms of security including, but not limited to floating charge debentures, general security agreements, postponement of specific claims and joint and several guarantees.

(a) Residential housing developments:

These loans pertain to projects at various stages of development in Toronto, Ontario, Kitchener, Ontario, Markham, Ontario and London, Ontario. 18 of the loans have been syndicated to private investors.

TERRA FIRMA CAPITAL CORPORATION

Notes to Consolidated Financial Statements (continued)
(In Canadian dollars)

Years ended December 31, 2014 and 2013

5. Loan and mortgage investments and loan and mortgage syndications (continued):

(b) Commercial retail development:

The loan represents a first mortgage secured by a retail development located in Kitchener, Ontario.

(c) Residential income properties:

The loans represent second mortgages secured by an apartment building located in Toronto, Ontario and two apartment buildings located in Ottawa, Ontario and an unregistered loan relating to an apartment building located in Ottawa, Ontario.

(d) Student housing:

The equity loan secured by a limited partnership interest in an entity that has an interest in a portfolio of student housing buildings located in the USA.

(e) Land:

The loan secured by a parcel of land located in Ottawa, Ontario and a 1.8 acre parcel of land located in Mississauga, Ontario.

The Company syndicates certain of its loan and mortgage investments to private investors or to financial institutions, each participating in a prescribed manner per agreement and on an investment by investment basis. In these investments the investors assume the same risks associated with the specific investment transaction as the Company. Each syndicated loan and mortgage investment has a designated rate of return that the syndicated investors expect to earn from that loan and mortgage investment.

The principal balance of loan and mortgage syndications at December 31, 2014 and 2013 were \$45,390,821 and \$42,889,374, respectively. The loan and mortgage syndications carry a weighted average effective interest rate of 11.9% (2013 - 12.6%) and a weighted average term to maturity of 0.67 years (2013 - 1.30 years).

TERRA FIRMA CAPITAL CORPORATION

Notes to Consolidated Financial Statements (continued)
(In Canadian dollars)

Years ended December 31, 2014 and 2013

5. Loan and mortgage investments and loan and mortgage syndications (continued):

The following table presents details of the loan and mortgage investments and loan and mortgage syndications as at December 31, 2014:

	Loan and mortgage investments	Loan and mortgage syndications	Net investments	% of net investments
Residential housing developments	\$ 71,355,076	\$ 40,914,961	\$ 30,440,115	91.5
Commercial retail development	600,000	500,000	100,000	0.3
Residential income properties	4,591,720	2,945,860	1,645,860	5.0
Land	2,089,000	1,030,000	1,059,000	3.2
	\$ 78,635,796	\$ 45,390,821	\$ 33,244,975	100.0

The following table presents details of the loan and mortgage investments and loan and mortgage syndications as at December 31, 2013:

	Loan and mortgage investments	Loan and mortgage syndications	Net investments	% of net investments
Residential housing developments	\$ 40,121,019	\$ 28,279,132	\$ 11,841,887	95.6
Commercial retail development	600,000	500,000	100,000	0.8
Residential income properties	1,794,084	1,347,042	447,042	3.6
Student housing	12,763,200	12,763,200	–	–
	\$ 55,278,303	\$ 42,889,374	\$ 12,388,929	100.0

In August 2014, a borrower of a student housing portfolio elected to repay the loan ahead of its maturity date with a prepayment penalty of \$104,876 on the loan. As a result, the Company recognized a gain of \$342,222, included in interest income in the consolidated statements of income and comprehensive income.

TERRA FIRMA CAPITAL CORPORATION

Notes to Consolidated Financial Statements (continued)
(In Canadian dollars)

Years ended December 31, 2014 and 2013

5. Loan and mortgage investments and loan and mortgage syndications (continued):

In November 2013, a borrower of a residential housing development elected to repay the loan ahead of its maturity date with a prepayment penalty of \$67,263 on the loan. As a result, the Company recognized a gain of \$91,861, included in interest income in the consolidated statements of income and comprehensive income.

The Company's loan and mortgage investments generally take the form of:

- land loans registered in first or second position at the earlier stages of real estate development;
- term mortgages for the purposes of acquiring or re-financing income-producing properties; or
- mezzanine or subordinated debt financings or real estate developments that have either progressed to the construction phase or are in the process of approaching the construction phase.

The following table presents details of the Company's loan categories as at December 31, 2014:

	Loan and mortgage investments	Loan and mortgage syndications	Net investments	% of net investments
Mortgages	\$ 59,671,635	\$ 32,468,934	\$ 27,202,701	81.8
Unregistered loans	18,964,161	12,921,887	6,042,274	18.2
	\$ 78,635,796	\$ 45,390,821	\$ 33,244,975	100.0

The following table presents details of the Company's loan categories as at December 31, 2013:

	Loan and mortgage investments	Loan and mortgage syndications	Net investments	% of net investments
Mortgages	\$ 44,078,303	\$ 35,150,242	\$ 8,928,061	72.1
Unregistered loans	11,200,000	7,739,132	3,460,868	27.9
	\$ 55,278,303	\$ 42,889,374	\$ 12,388,929	100.0

TERRA FIRMA CAPITAL CORPORATION

Notes to Consolidated Financial Statements (continued)
(In Canadian dollars)

Years ended December 31, 2014 and 2013

5. Loan and mortgage investments and loan and mortgage syndications (continued):

Mortgages are loans that are secured by real estate assets and may include other forms of securities. Unregistered loans are not secured by real estate asset, but are secured by other forms of securities, such as personal guarantees, or pledge of shares of the borrowing entity.

Principal repayments and loan and mortgage investments maturing in the next three years are as follows:

	Scheduled principal payments	Investments maturing during the year	Total loans and mortgages investments
2015	\$ 1,750	\$ 52,409,514	\$ 52,411,264
2016	–	19,360,297	19,360,297
2017	–	6,864,235	6,864,235
	<u>\$ 1,750</u>	<u>\$ 78,634,046</u>	<u>\$ 78,635,796</u>

Certain of the loan and mortgage investments have early repayment rights and, if exercised, would result in repayments in advance of their contractual maturity dates.

Pursuant to certain lending agreements, the Company is committed to fund additional loan advances. The unfunded loan commitments under the existing loan and mortgage investments at December 31, 2014 were \$4,010,043 including \$2,298,304 of capitalization of future interest relating to the existing loan and mortgage investments (2013 - \$1,529,552, \$866,202 of capitalization of future interest relating to the existing loan and mortgage investments).

During the years ended December 31, 2014 and 2013, the Company capitalized interest income of \$2,800,427 and \$2,296,952, respectively, which is included in the loan and mortgage investments.

During the year ended December 31, 2014, the Company converted \$1,666,000 (2013 - nil) of interest receivable to loan and mortgage investments (note 4).

TERRA FIRMA CAPITAL CORPORATION

Notes to Consolidated Financial Statements (continued)
(In Canadian dollars)

Years ended December 31, 2014 and 2013

5. Loan and mortgage investments and loan and mortgage syndications (continued):

Scheduled principal repayments and maturity amounts loan and mortgage syndications at December 31, 2014 are as follows:

	Scheduled principal payments	Loans maturing during the year	Total loan and mortgage syndications
2015	\$ 875	\$ 34,176,644	\$ 34,177,519
2016	–	11,213,302	11,213,302
	\$ 875	\$ 45,389,946	\$ 45,390,821

6. Joint arrangements:

(a) Interests in joint operations:

Where the Company's interests in the following properties are subject to joint control, the Company records its proportionate share of the related assets, liabilities, revenue and expenses of the properties using the proportionate consolidation method.

(i) Montreal Street JV:

In July 2009, the Company entered into a co-tenancy agreement (the "Montreal Street JV") with a development partner to develop a store for a national pharmacy chain in Ottawa, Ontario. The land on which the store was developed is subject to a 20-year land lease, with five renewal options of five years each. The Montreal Street JV carries a loan of \$2,092,943, bearing interest at 4.2% per annum, is amortized over 25 years and matures June 1, 2016. The Company's ownership interest in the Montreal Street JV is 52.5%.

TERRA FIRMA CAPITAL CORPORATION

Notes to Consolidated Financial Statements (continued)
(In Canadian dollars)

Years ended December 31, 2014 and 2013

6. Joint arrangements (continued):

(ii) Queen Street West JV:

In April 2012, the Company entered into a co-owners' agreement (the "Queen Street West JV") and acquired a land parcel with a development partner to develop a mid-rise residential condominium building in Toronto, Ontario, having a development potential of approximately 100,000 square feet of gross floor area. Under the terms of the co-owners agreement, the Company has agreed to contribute 75% of the capital required during the course of the development, for a 50% ownership interest.

On April 1, 2014, the Company and the co-owner of the joint operation entered into an agreement whereby the Company converted its interest in the joint operation into a loan receivable of \$2,818,000 (the Company's original investment in the joint operation), secured by the property. The carrying value of the Company's interest in joint operation at the time of conversion was \$2,331,000 (after recognizing operating losses from the joint operation during prior periods), resulting in a gain on conversion of interest in joint operation of \$487,000.

The following table presents the carrying value of assets in joint operations transferred on conversion:

Investment property	\$ 5,771,041
Other receivables	46,890
Prepaid expenses and deposits	137,469
Accounts payable and accrued liabilities	(124,400)
Loan and mortgage investment	(1,000,000)
Mortgage payable	(2,500,000)
Value of assets transferred on conversion	\$ 2,331,000

TERRA FIRMA CAPITAL CORPORATION

Notes to Consolidated Financial Statements (continued)
(In Canadian dollars)

Years ended December 31, 2014 and 2013

6. Joint arrangements (continued):

The financial information in respect of the Company's proportionate share of investments in joint operations is as follows:

	2014	2013
Assets	\$ 3,416	\$ 5,465
Cash and cash equivalents	11,643	101,669
Investment properties	2,062,661	7,671,452
	2,077,720	7,778,586
Liabilities		
Accounts payable and prepaid expenses	41,182	24,134
Mortgages payable	1,151,118	3,680,547
	1,192,300	3,704,681
Net assets	\$ 885,420	\$ 4,073,905

The table below details the results of operations for the years ended December 31, 2014 and 2013, attributable to the Company from its joint operations activities:

	2014	2013
Rental revenue	\$ 257,595	\$ 451,335
Interest revenue	–	58,310
	257,595	509,645
Property operating costs	87,751	287,078
General and administrative expenses	1,466	2,732
Interest expense	118,766	400,835
Fair value adjustment - investment properties	(147,950)	78,287
	60,033	768,932
Net income (loss)	\$ 197,562	\$ (259,287)

TERRA FIRMA CAPITAL CORPORATION

Notes to Consolidated Financial Statements (continued)
(In Canadian dollars)

Years ended December 31, 2014 and 2013

6. Joint arrangements (continued):

(b) Investment properties:

The Company has interests in investment properties that are subject to joint control and accordingly, the Company has recorded its proportionate share of the related assets, liabilities, revenue and expenses of the properties.

The following table summarizes the changes in the Company's proportionate share of the investment properties for the years ended December 31, 2014 and 2013:

	2014	2013
Balance, beginning of year	\$ 7,671,452	\$ 7,834,576
Change in amount receivable from joint operating partners	(62,325)	(203,924)
Additions, capital expenditures	76,625	119,087
Sale of investment property	(5,771,041)	–
Fair value adjustment	147,950	(78,287)
Balance, end of year	\$ 2,062,661	\$ 7,671,452

The Company determined the fair value of investment property in the Montreal Street JV using the direct capitalization method. Under the direct capitalization method, fair values were determined by capitalizing the estimated future net operating income at the market capitalization rates. The proportionate share of investment property in the Montreal Street JV with an aggregate value of \$2,062,661 was valued by the Company's management. The capitalization rate used in the valuation of investment property was 6.50% (2013 - 7.00%).

As at December 31, 2014, a 25-basis-point decrease in the overall capitalization rate would increase the Company's proportionate share of value of investment property in the Montreal Street JV by \$82,500 (2013 - \$71,159) and a 25-basis-point increase in the overall capitalization rate would decrease the Company's proportionate share of the value of investment property in the Montreal Street JV by \$76,450 (2013 - \$66,251).

On April 1, 2014, the Company converted its interest in the investment property in the Queen Street West JV into a loan receivable. On that date, the carrying value of investment property in the Queen Street West JV approximates its fair value.

TERRA FIRMA CAPITAL CORPORATION

Notes to Consolidated Financial Statements (continued)
(In Canadian dollars)

Years ended December 31, 2014 and 2013

6. Joint arrangements (continued):

(c) Mortgages payable:

The details of the mortgages payable in respect of the Company's proportionate share of the joint operations at December 31, 2014 and 2013 is as follows:

	2014		2013	
	Amount	% of loans payable	Amount	% of loans payable
Montreal Street JV	\$ 1,151,118	100.0	\$ 1,180,547	32.1
Queen Street West JV	–	–	2,500,000	67.9
	<u>\$ 1,151,118</u>	<u>100.0</u>	<u>\$ 3,680,547</u>	<u>100.0</u>

Scheduled principal repayments and maturity amounts of mortgages payable at December 31, 2014 are as follows:

	Loans Scheduled principal payments	Total maturing during the year	loans and mortgages payable
2015	\$ 30,804	\$ –	\$ 30,804
2016	13,224	1,107,090	1,120,314
	<u>\$ 44,028</u>	<u>\$ 1,107,090</u>	<u>\$ 1,151,118</u>

TERRA FIRMA CAPITAL CORPORATION

Notes to Consolidated Financial Statements (continued)
(In Canadian dollars)

Years ended December 31, 2014 and 2013

7. Portfolio investments:

The Company has invested through the Hill, in a partnership interest in a 94 unit mid-rise condominium development project located in Toronto, Ontario. The Company does not have significant influence in the partnership and is accounting for this investment as a financial asset at fair value through profit and loss. The carrying value of the investment is \$954,073 (2013 - \$954,073). At December 31, 2014, the fair values were determined by the management, using the direct comparison method. The fair value of investment at December 31, 2014 was \$1,020,828.

On December 4, 2014, TFCC LanQueen entered into a partnership agreement (the "Agreement"), whereby TFCC LanQueen is committed to invest up to \$1,326,400 in redevelopment project located in Toronto, Ontario. The Agreement allows TFCC LanQueen to receive a 3% fee at the time of commitment and an amount by way of a preferred return equal to 10% per annum calculated and compounded annually on the amount of its investment in the partnership. As at December 31, 2014, TFCC LanQueen contributed \$600,000 to the partnership and received \$39,792 in fees and accrued \$4,767 of preferred return. The fees and preferred return are recognized as interest and fees in the consolidated statements of income and comprehensive income.

The following table summarizes the changes in the portfolio investments for the years ended December 31, 2014 and 2013:

	2014	2013
Balance, beginning of year	\$ 954,073	\$ 950,000
Investment made	600,000	4,073
Fair value adjustment	66,755	—
Balance, end of year	\$ 1,620,828	\$ 954,073

TERRA FIRMA CAPITAL CORPORATION

Notes to Consolidated Financial Statements (continued)
(In Canadian dollars)

Years ended December 31, 2014 and 2013

8. Accounts payable and accrued liabilities:

The following table presents details of the accounts payable and accrued liabilities as at December 31, 2014 and 2013:

	2014	2013
Interest payable	\$ 728,439	\$ 772,735
Interest reserve	310,483	353,705
Accounts payable and accrued liabilities	727,050	240,268
Share-based compensation payable	461,336	–
	<u>\$ 2,227,308</u>	<u>\$ 1,366,708</u>

Accounts payable and accrued liabilities are current and payable in the current fiscal year.

9. Provision for discontinued operations:

The Company's discontinued operations consist of the assets, liabilities and operations of a sold property located at 870 Red River Road, Thunder Bay, Ontario. The Company has agreed to indemnify rents with respect to a tenant's lease of a unit in the property from the date of sale until its lease expiry of July 2016, to the extent that the tenant fails to make rent payments (the "indemnified tenancy"). The tenant entered into a court appointed receivership process and the receiver was unable to sell the underlying business and as a result, the receiver disclaimed the lease subject to the indemnified tenancy.

Effective July 1, 2014, the unit was leased on subsidized basis to a third party tenant for the remainder of the lease term. Consequently, the rent provision of \$206,319 before applicable taxes was reversed. The balance of the provision as at December 31, 2014 and 2013 was \$27,500 and \$321,490, respectively. The current portion of the provision is \$27,500.

The following table summarizes the changes in the provision for discontinued operations for the years ended December 31, 2014 and 2013:

	2014	2013
Balance, beginning of year	\$ 321,490	\$ 445,957
Lease payments made	(87,671)	(124,467)
Reversal of rent obligation	(206,319)	–
Balance, end of year	<u>\$ 27,500</u>	<u>\$ 321,490</u>

TERRA FIRMA CAPITAL CORPORATION

Notes to Consolidated Financial Statements (continued)
(In Canadian dollars)

Years ended December 31, 2014 and 2013

10. Short-term unsecured loans payable:

In August 2014, the Company entered into formal short-term loan agreements with three lenders to borrow \$5,120,000, of which an agreement for \$1,000,000 is with the Chairman of the Board of the Company (the "Chairman"). The interest rate is 10% annum, payable monthly. These loans are repayable by the Company anytime, without penalty. Proceeds from these loans were used to fund certain loan and mortgage investments.

In September 2014, the Company repaid the loan received from the Chairman in full with interest of \$6,849 (note 16).

For the year ended December 31, 2014, interest expense of \$118,039 was recorded (2013 - nil). As at December 31, 2014, \$1,500,000 of short-term loans payable remains unpaid.

11. Convertible debentures:

On September 29, 2014, the Company refinanced, by way of a private placement, the unsecured subordinated convertible debentures in the principal amount of \$10,150,000 with an original maturity date of September 27, 2014 (the "2011 Debentures"), with the issuance of new unsecured subordinated convertible debentures (the "2014 Debentures") in the principal amount of \$10,850,000.

The 2014 Debentures bear interest at an annual rate of 7%, payable quarterly on the last business day of each calendar quarter commencing December 31, 2014, and mature on September 27, 2017. The 2014 Debentures are convertible into Shares of the Company in whole or in part, at the option of the holder at any time up to maturity at a conversion price of \$0.72 per Share. The Company may, at any time prior to the maturity date and upon giving notice, prepay the 2014 Debentures in full or in part, by paying the holders thereof the outstanding principal amount plus all accrued and unpaid interest, provided that the market price per Share on the date on which the redemption notice is provided is at least 125% of the conversion price.

The 2011 Debentures bore interest at an annual rate of 7.0%, paid on the last business day of each calendar quarter and were convertible into Shares of the Company in whole or in part, at the option of the holder at any time up to maturity at a conversion price of \$0.70 per Share. The 2011 Debentures were not redeemable or convertible at the option of the Company prior to maturity.

TERRA FIRMA CAPITAL CORPORATION

Notes to Consolidated Financial Statements (continued)
(In Canadian dollars)

Years ended December 31, 2014 and 2013

11. Convertible debentures (continued):

The fair value of the liability component of the 2014 Debentures was calculated by discounting the stream of future principal and interest payments at the rate of 8.0% which represents the rate of interest prevailing at the date of issue for instruments of similar terms and risks. The debt component was assigned a value of \$10,486,460 (net of transaction costs of \$76,962) and the equity component was assigned a value of \$284,490 (net of transaction costs of \$2,088). The effective interest rate of the 2014 Debentures is 8.53%.

The fair value of the liability component of the 2011 Debentures was determined to be the fair value of the Debenture as a whole. Issue costs directly attributable to the issuance of the 2011 Debentures were deducted from the liability component of the 2011 Debentures resulting in an effective interest rate of 7.35%.

A portion of the 2014 Debentures were issued to related parties (note 16). Certain directors and officers held 2011 Debentures in an aggregate principal amount of \$800,000.

The following table summarizes the changes in the convertible debentures for the years ended December 31, 2014 and 2013:

	2011 Debentures	2014 Debentures	Total
Liability component of debentures, December 31, 2012	\$ 10,093,325	\$ —	\$ 10,093,325
Interest expensed as EIR of 7.35%	742,249	—	742,249
Interest paid	(710,500)	—	(710,500)
Liability component of debentures, December 31, 2013	10,125,074	—	10,125,074
Interest expensed as EIR of 7.35% for 2011 debentures and at 8.43% for 2014 debentures	549,226	223,434	772,660
Interest paid	(524,300)	(195,463)	(719,763)
Insurance of debentures	—	10,850,000	10,850,000
Repayment of debentures	(10,150,000)	—	(10,150,000)
Transaction costs	—	(79,050)	(79,050)
Amount classified as equity	—	(284,490)	(284,490)
Liability component of debentures, December 31, 2014	\$ —	\$ 10,514,431	\$ 10,514,431

Holders of an aggregate \$6,225,000 principal amount of the 2011 Debentures elected to subscribe to 2014 Debentures.

TERRA FIRMA CAPITAL CORPORATION

Notes to Consolidated Financial Statements (continued)
(In Canadian dollars)

Years ended December 31, 2014 and 2013

12. Commitments and contingencies:

Pursuant to certain lending agreements, the Company is committed to fund additional loan advances. The unfunded loan commitments under the existing lending agreements at December 31, 2014 were \$4,010,043 (2013 - \$1,529,552). The unfunded capital commitments under the Agreement at December 31, 2014 was \$726,400 (2013 - nil).

The Company is also committed to provide additional capital to joint operations in accordance with contractual agreements.

The Company has a lease commitment on its head office premises located at 5000 Yonge Street, Toronto, Ontario. The minimum rental amount is \$30,693 per annum extending to March 31, 2017. Additional maintenance and utility costs and realty taxes are payable as incurred.

The Company, from time to time, may be involved in various claims, legal and tax proceedings and complaints arising in the ordinary course of business. The Company is not aware of any pending or threatened proceedings that would have a material adverse effect on the financial condition or future results of the Company.

13. Shareholders' equity:

(a) Shares issued and outstanding:

The following table summarizes the changes in Shares for the years ended December 31, 2014 and 2013:

	Shares	Amount
Outstanding, December 31, 2012	30,695,000	\$ 10,757,405
Issuance of Shares pursuant to share option plan	150,000	30,000
Transferred from contributed surplus upon exercise of options	–	8,385
Outstanding, December 31, 2013	30,845,000	10,795,790
Issuance of Shares pursuant to the Offering	9,587,300	5,190,543
Issuance of Shares pursuant to the Private Placement	1,000,000	630,000
Issuance of shares pursuant to share option plan	150,000	30,000
Transferred from contributed surplus upon exercise of options	–	8,385
Outstanding, December 31, 2014	41,582,300	\$ 16,654,718

TERRA FIRMA CAPITAL CORPORATION

Notes to Consolidated Financial Statements (continued)
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Years ended December 31, 2014 and 2013

13. Shareholders' equity (continued):

On October 15, 2014, the Company completed a bought deal offering (the "Offering") of 8,000,000 Shares at a price of \$0.63 per Share, for gross proceeds of \$5,040,000. As part of the Offering, the Company issued 560,000 broker warrants to underwriters as additional compensation. Each broker warrant entitles the holder to purchase one Share of the Company at an exercise price of \$0.63 per Share, until October 15, 2015. Share issuance costs amounted to \$849,456, consisting of cash costs of \$743,221 and non-cash costs of \$106,235 relating to the value attributable to broker warrants issued to underwriters. Concurrently with the Offering, the Company issued 1,587,300 Shares through private placement at a price of \$0.63 per Share to the Chairman and the Chief Executive Officer of the Company, for gross proceeds of \$999,999 (note 16).

On November 24, 2014, the Company issued 1,000,000 Shares at \$0.63 per Share to the President and Chief Operating Officer of the Company, for gross proceeds of \$630,000 (note 16).

(b) Share-based payments:

The share-based payments that have been recognized in these consolidated financial statements are as follows:

	2014	2013
Share option Plan	\$ 347,773	\$ 39,208
DSU Plan	461,336	—
	<u>\$ 809,109</u>	<u>\$ 39,208</u>

(i) Share option plan:

The Company has a share option plan (the "Plan") to grant eligible directors, officers, senior management and consultants to grant options to purchase Shares. The exercise price of an option each option shall be determined by the board of directors and in accordance with the Plan and the policies of the Exchange. Subject to the policies of the Exchange, the board of directors may determine the time during which options shall vest and the method of vesting, or that no vesting restriction shall exist, provided that no option shall be exercisable after five years from the date on which it is granted.

TERRA FIRMA CAPITAL CORPORATION

Notes to Consolidated Financial Statements (continued)
(In Canadian dollars)

Years ended December 31, 2014 and 2013

13. Shareholders' equity (continued):

On November 28, 2014, the Company granted share options to certain officers and a consultant of the Company to purchase an aggregate of 1,050,000 Shares at \$0.79 per share and an aggregate of 599,115 Shares at \$0.68 per share. Except for the 1,000,000 options granted to an officer, which shall vest in equal instalments on a quarterly basis over the three-year period, the options vest in four instalments, with the first 25% of the share options vested immediately upon grant, with an additional 25% vesting each 90-day period thereafter.

On May 20, 2014, the Company granted share options to directors, officers and employees of the Company to purchase an aggregate of 565,000 Shares at \$0.50 per share. Except for the 210,000 options granted to employees, which vested immediately, the options vest in four instalments, with the first 25% of the share options vested immediately upon grant, with an additional 25% vesting each 90-day period thereafter.

On February 24, 2014, the Company granted share options to consultants of the Company to purchase an aggregate of 100,000 Shares at \$0.50 per Share. 25% of the share options vested immediately upon grant, with an additional 25% vesting each 90-day period thereafter.

On April 17, 2013, the Company granted share options to directors and officers to purchase an aggregate of 245,334 Shares at \$0.30 per Share. 25% of the share options vested immediately upon grant, with an additional 25% vesting each 90-day period thereafter.

The fair value of the share options granted was estimated on each of the dates of grant, using the Black-Scholes option pricing model, with the following assumptions:

	November 28, 2014	May 20, 2014	February 24, 2014	April 17, 2013
Average expected life	3.06 years	2.62 years	2.68 years	5.00 years
Average risk-free interest rate	1.20%	1.05%	0.98%	1.21%
Average expected volatility	90.00%	96.00%	98.29%	104.00%
Average dividend yield	—	—	—	—

TERRA FIRMA CAPITAL CORPORATION

Notes to Consolidated Financial Statements (continued)
(In Canadian dollars)

Years ended December 31, 2014 and 2013

13. Shareholders' equity (continued):

The fair value of options granted during the years ended December 31, 2014 and 2013 were \$1,029,949 and \$39,209, respectively.

The following is the summary of changes in share options for the years ended December 31, 2014 and 2013:

	2014		2013	
	Number of options	Weighted average exercise price	Number of options	Weighted average exercise price
Outstanding, beginning of year	1,932,334	\$ 0.37	2,442,667	\$ 0.37
Granted	2,314,115	0.68	245,334	0.30
Exercised	(150,000)	0.20	(150,000)	0.20
Cancelled	(25,000)	–	(605,667)	0.42
Outstanding, end of year	4,071,449	0.55	1,932,334	0.37
Number of options exercisable	2,495,863	\$ 0.43	1,897,667	\$ 0.38

The following summarizes the Company's outstanding share options as at December 31, 2014:

Number of options outstanding	Expiry date	Number of options exercisable	Exercise price	Market price at date of grant
895,000	January 24, 2016	895,000	\$ 0.30	\$ 0.28
138,667	December 19, 2016	138,667	0.50	0.40
585,000	April 16, 2017	585,000	0.50	0.30
138,667	April 17, 2018	138,667	0.30	0.25
100,000	February 23, 2019	100,000	0.50	0.42
565,000	May 20, 2019	476,250	0.50	0.47
599,115	November 28, 2019	149,779	0.68	0.85
1,050,000	November 28, 2019	12,500	0.79	0.85
4,071,449		2,495,863		

TERRA FIRMA CAPITAL CORPORATION

Notes to Consolidated Financial Statements (continued)
(In Canadian dollars)

Years ended December 31, 2014 and 2013

13. Shareholders' equity (continued):

(ii) Deferred Share Unit Plan:

In May 2014, the Company established and adopted the DSU Plan to promote a greater alignment of interests between directors, officers and employees and the shareholders of the Company by linking a portion of the annual director retainer and annual bonus to officers or employees to the future value of the Company's Shares.

The Board determines the amount, timing, and vesting conditions associated with each award of DSUs. Directors may elect to receive, on the last day of each quarter, a minimum of 50% and up to 100% of their annual retainer in DSUs and employees may elect to receive up to 100% of their annual bonus in DSUs. DSUs granted pursuant to such an election are fully vested on the date of grant. In addition, when the Directors or employees elect to receive 50% or more of their fees or annual bonus in DSUs, the Company will grant additional DSUs of up to 50% of the value of the DSUs granted to them. 50% of the additional DSUs granted by the Company vest in six months from the date of grant and 50% of the additional DSUs vest in twelve months from the date of grant.

Each DSU has the same value as one Share (based on the five day volume weighted average trading price). DSUs must be retained until the director leaves the Board of Directors or termination of employment of officers or employees, at which time the redemption payment equal to the value of the DSUs, calculated as the volume weighted average closing price of the Shares for the last five days preceding the redemption date, net of applicable taxes are paid out.

The following is the summary of changes in DSUs for the years ended December 31, 2014 and 2013:

	2014	2013
DSUs outstanding, beginning of year	–	–
Granted	747,705	–
Settled	–	–
DSUs outstanding, end of year	747,705	–
Number of DSUs vested	670,642	–

TERRA FIRMA CAPITAL CORPORATION

Notes to Consolidated Financial Statements (continued)
(In Canadian dollars)

Years ended December 31, 2014 and 2013

13. Shareholders' equity (continued):

The total cost recognized with respect to DSUs, including the change in fair value of DSUs during the years ended December 31, 2014 and 2013, were \$461,336 and nil, respectively.

The carrying amount of the liability, included in accounts payable and accrued liabilities relating to the DSUs at December 31, 2014 is \$461,336 (2013 - nil).

(c) Broker warrants:

As part of the Offering completed on October 15, 2014, the Company granted 560,000 broker warrants to underwriters as partial consideration for their services associated with the Offering. Each broker warrant entitles the holder to acquire one Share of the Company at an exercise price of \$0.63 per Share, with an expiry date of October 15, 2015.

The following is the summary of changes in broker warrants for years ended December 31, 2013 and 2014:

	Number of broker warrants outstanding	Fair value	Exercise price
Outstanding, December 31, 2012	–	\$ –	\$ –
Granted	–	–	–
Outstanding, December 31, 2013	–	–	–
Granted	560,000	106,235	0.63
Outstanding, December 31, 2014	560,000	\$ 106,235	\$ 0.63

The fair value of broker warrants was estimated at the grant date using the Black-Scholes option-pricing model with the following assumptions:

	October 15, 2014
Average expected life	1.00 year
Average risk-free interest rate	1.13%
Average expected volatility	73.5%
Average dividend yield	–

TERRA FIRMA CAPITAL CORPORATION

Notes to Consolidated Financial Statements (continued)
(In Canadian dollars)

Years ended December 31, 2014 and 2013

14. Contributed surplus:

The following table presents the details of the contributed surplus balances as at December 31, 2014 and 2013:

	2014	2013
Balance, beginning of year	\$ 603,962	\$ 573,139
Fair value of share-based compensation	347,773	39,208
Transferred to share capital - exercise of options	(8,385)	(8,385)
Fair value of broker warrants	106,235	–
Balance, end of year	\$ 1,049,585	\$ 603,962

15. Earnings per share:

The calculation of earnings per share of the years ended December 31, 2014 and 2013 is as follows:

	2014	2013
Numerator for basic and diluted earnings per share:		
Income attributable to common shareholders	\$ 3,227,728	\$ 1,699,827
Interest savings on debentures, net of taxes	567,906	545,553
Diluted income attributable to common shareholders	\$ 3,795,634	\$ 2,245,380
Denominator basic and diluted earnings per share:		
Weighted average number of Shares outstanding	33,072,348	30,737,486
Dilutive effect of share based payments	821,546	42,487
Dilutive effect of broker warrants	8,992	–
Assumed conversion of debentures	14,646,251	14,500,000
Weighted average number of diluted Shares outstanding	48,549,137	45,279,973
Earnings per share:		
Basic	\$ 0.10	\$ 0.06
Diluted	0.08	0.05

TERRA FIRMA CAPITAL CORPORATION

Notes to Consolidated Financial Statements (continued)
(In Canadian dollars)

Years ended December 31, 2014 and 2013

16. Transactions with related parties:

Except as disclosed elsewhere in the consolidated financial statements, the following are the related party transactions.

At December 31, 2014 and 2013, the Chairman, indirectly through a wholly owned subsidiary, owned approximately 20% of the issued and outstanding Shares of the Company.

(a) Key management personnel compensation:

Aggregate compensation for key management personnel was as follows:

	2014	2013
Short-term employee benefits	\$ 1,135,434	\$ 713,762
Share-based compensation	763,638	39,208
	<u>\$ 1,899,072</u>	<u>\$ 752,970</u>

The key management personnel of the Company include the Chief Executive Officer, President and Chief Operating Officer, Chief Financial Officer, Vice President, Operations and the Board of Directors.

During the years ended December 31, 2014 and 2013, no key management personnel were indebted to the Company.

(b) Loan and mortgages syndications, short-term unsecured loans payable and convertible debentures:

Several of the Company's loan and mortgage investments are syndicated with other investors of the Company, may include officers or directors of the Company. The Company ranks equally with other members of the syndicate as to payment of principal and interest.

In August 2014, the Company borrowed \$1,000,000 of short-term unsecured loan from the Chairman. The loan was repaid in September 2014 with interest of \$6,849 (note 11).

In connection with the financing of the 2014 Debentures, (note 11), certain directors and officers of the Company subscribed for an aggregate principal amount of \$1,330,000. The terms offered to related parties for the 2014 Debentures are identical to those offered to non-related 2014 Debenture holders.

TERRA FIRMA CAPITAL CORPORATION

Notes to Consolidated Financial Statements (continued)
(In Canadian dollars)

Years ended December 31, 2014 and 2013

16. Transactions with related parties (continued):

At December 31, 2014 and 2013, the loan and mortgage investments and debentures syndicated by officers and directors were \$1,844,848 and \$2,276,088, respectively. No loans or investments were issued to borrowers controlled by or related to officers or directors of the Company.

(c) Shareholders' equity:

On October 15, 2014, the Company issued 1,587,300 Shares through private placement at a price of \$0.63 per Share to the Chairman and the Chief Executive Officer of the Company, for gross proceeds of \$999,999 (note 13).

On November 24, 2014, the Company issued 1,000,000 Shares at \$0.63 per Share to the President and Chief Operating Officer of the Company, for gross proceeds of \$630,000 (note 13).

17. Interest expense:

The following table presents the interest incurred for the years ended December, 2014 and 2013:

	2014	2013
Interest on loans and mortgages syndications	\$ 5,202,603	\$ 3,717,266
Interest on Debentures	772,661	742,249
Montreal Street JV	47,091	48,830
Queen Street West JV	32,335	233,678
	<u>\$ 6,054,690</u>	<u>\$ 4,742,023</u>

18. Income taxes:

The following table specifies the current and deferred tax components of income taxes on continuing operations in the consolidated statements of income and comprehensive income:

	2014	2013
Current income tax provision	\$ 1,107,251	\$ 592,173
Deferred income tax	(54,729)	(9,254)
Total tax provision	<u>\$ 1,052,522</u>	<u>\$ 582,919</u>

TERRA FIRMA CAPITAL CORPORATION

Notes to Consolidated Financial Statements (continued)
(In Canadian dollars)

Years ended December 31, 2014 and 2013

18. Income taxes (continued):

Income tax expense is different from the amount that would result from applying the combined federal and provincial income tax rates to income before continuing operations before income taxes. These differences result from the following items:

	2014	2013
Income from continuing operations before income taxes	\$ 4,139,261	\$ 2,282,746
Combined federal and provincial statutory income taxes	26.50%	26.50%
Income tax provision based on statutory income taxes	\$ 1,096,904	\$ 604,928
Increase (decrease) in income tax due to:		
Non-taxable items	(108,133)	(26,056)
Non-deductible stock-based compensation	92,160	10,390
Change in deferred tax asset not previously recognized	(28,409)	(5,230)
Tax rate differential on temporary differences	–	(1,113)
Total tax provision	\$ 1,052,522	\$ 582,919

The composition of the Company's recognized deferred income tax assets and liabilities for the year ended December 31, 2014 is as follows:

	Opening balance	Recognized in income	Closing balance
Investment property	\$ (15,466)	\$ (123,345)	\$ (138,811)
Portfolio investment	–	(8,845)	(8,845)
Incorporation costs	700	(49)	651
Debenture and share issue costs	8,418	64,714	73,132
Deferred Share Units	–	122,254	122,254
	\$ (6,348)	\$ 54,729	\$ 48,381

TERRA FIRMA CAPITAL CORPORATION

Notes to Consolidated Financial Statements (continued)
(In Canadian dollars)

Years ended December 31, 2014 and 2013

18. Income taxes (continued):

The composition of the Company's recognized deferred income tax assets and liabilities for the year ended December 31, 2013 is as follows:

	Opening balance	Recognized in income	Closing balance
Investment property	\$ (25,838)	\$ 10,372	\$ (15,466)
Incorporation costs	753	(53)	700
Debenture and share issue costs	9,483	(1,065)	8,418
	\$ (15,602)	\$ 9,254	\$ (6,348)

19. Capital management:

The Company defines its capital as the aggregate of shareholders' equity, non-controlling interest, convertible debentures, loan and mortgage syndications, short-term loans payable and mortgages payable. The Company's capital management is designed to ensure that the Company has sufficient financial flexibility, short-term and long-term and to grow cash flow and solidify the Company's long-term creditworthiness, as well as a good return for the shareholders.

The following table presents the capital of the Company as at December, 2014 and 2013:

	2014	2013
Short-term loans payable	\$ 1,500,000	\$ –
Loan and mortgage syndications	45,390,821	42,889,374
Mortgage payable	1,151,118	3,680,547
Convertible debentures	10,514,431	10,125,074
Non-controlling interest	210,655	200,000
Shareholders' equity	24,341,750	14,524,981
Total capital	\$ 83,108,775	\$ 71,419,976

The Company is free to determine the appropriate level of capital in context with the cash flow requirements, overall business risks and potential opportunities. As a result, the Company will make adjustments to its capital structure in response to lending opportunities, the availability of capital and anticipated changes in general economic conditions. The Company's overall strategy with respect to capital remained unchanged during the years ended December 31, 2014 and 2013.

TERRA FIRMA CAPITAL CORPORATION

Notes to Consolidated Financial Statements (continued)
(In Canadian dollars)

Years ended December 31, 2014 and 2013

19. Capital management (continued):

During the years ended December 31, 2014 and 2013, the Company had no externally-imposed capital requirements.

20. Fair value measurement:

The Company, as part of its operations, carries a number of financial instruments. The Company's financial instruments consist of cash and cash equivalents, funds held in trust, interest and other receivables, loan and mortgage investments, portfolio investments, accounts payable and accrued liabilities, loan and mortgage syndications, mortgages payable, short-term loans payable and convertible debentures.

The fair value of interest and other receivables, funds held in trust and accounts payable and accrued liabilities approximate their carrying values due to their short-term maturities.

The fair value of loan and mortgage investments, loan and mortgage syndications, mortgages payable, short-term loans payable and Debentures approximate their carrying value as they are short-term in nature. There is no quoted price in an active market for the loans and mortgage investments, mortgage syndication liabilities, mortgages payable, short-term loans payable or Debentures. The Company makes its determinations of fair value based on its assessment of the current lending market for these instruments of same or similar terms. As a result, the fair value is based on Level 3 on the fair value hierarchy.

The Company uses various methods in estimating the fair values recognized in the consolidated financial statements. The fair value hierarchy reflects the significance of inputs used in determining the fair values.

- Level 1 - quoted prices in active markets;
- Level 2 - inputs other than quoted prices in active markets or valuation techniques where significant inputs are based on observable market data; and
- Level 3 - valuation technique for which significant inputs are not based on observable market data.

The fair value of the Company's investment properties, portfolio investments and non-controlling interests are determined using Level 3 inputs at December 31, 2014 and 2013 and no amounts were transferred between fair value levels during 2014 or 2013. Notes 6(b) and 7 outlines the key assumptions used by the Company in determining fair value of its investment properties and portfolio investment.

TERRA FIRMA CAPITAL CORPORATION

Notes to Consolidated Financial Statements (continued)
(In Canadian dollars)

Years ended December 31, 2014 and 2013

21. Risk management:

In the normal course of business, the Company is exposed to a number of risks that can affect its operating performance. These risks and the actions taken to manage them are as follows:

(a) Market risk:

Market risk is the risk that the value of an investment will fluctuate as a result of changes in market price whether the changes are caused by factors specific to the investment or factors affecting all securities in the market.

The Company's objective of managing this risk is to minimise the volatility of earnings. The Company mitigates this risk by charging interest rates which are significantly above normal banking rates.

(b) Credit risk:

Credit risk is the risk of financial loss from the failure of a borrower, for any reason, to fully honour its financial or contractual obligations to the Company, primarily arising from the Company's loan and mortgage investment activities. Fluctuations in real estate values may increase the risk of default and may also reduce the net realizable value of the collateral property to the Company. Credit losses occur when a borrower fails to meet its obligations to the Company and the value realized on the sale of the underlying security deteriorates below the carrying amount of the exposure.

The Company is exposed to credit risk on all financial assets and its exposure is generally limited to the carrying amount on the consolidated statements of financial position.

The Company mitigates the risk of credit losses on its loan and mortgage investments by maintaining strict credit policies and conducting thorough investment due diligence, ensuring loans and mortgages have risk-adjusted loan to value, together with personal guarantees by the borrowers and parties related to the borrowers, review and approval of new loans and mortgages and continued monitoring of change in value of underlying securities.

The Company regularly reviews the loan and mortgage investments and interest receivable listing for balances in arrears and follows up with clients as needed regarding payment. For individual accounts in arrears where discussion with the client has not succeeded, foreclosure proceedings commence. Balances receivable include accrued interest and legal and other costs related to attempts at collection. Where loan investments are collateralized by real property and losses are recognized to the extent that recovery of the balance through sale of the underlying property is not reasonably assured.

TERRA FIRMA CAPITAL CORPORATION

Notes to Consolidated Financial Statements (continued)
(In Canadian dollars)

Years ended December 31, 2014 and 2013

21. Risk management (continued):

As at December 31, 2014, \$124,131 of interest receivable are in arrears over 60 days and \$3,923,438 of the loan and mortgage investments are in arrears over 30 days. Based on the most recent property appraisals the Company has not identified any specific loans for which a loss provision should be made (2013 - nil).

(c) Currency risk:

Currency risk is the risk that the fair value or future cash flows of the Company's foreign currency denominated loan and mortgage investments, loans and mortgages payable and cash and cash equivalents will fluctuate based on changes in foreign currency exchange rates. Approximately \$211,115 (2013 - 985,907) of the Company's cash and cash equivalents at year end are denominated in United States dollars. None of the loan and mortgage investments or loan and mortgage syndications are denominated in United States dollars. At December 31, 2013, \$12,763,200 of the of the loan and mortgage investments and loan and mortgage syndications are denominated in United States dollars and secured primarily by charges on real estate located in United States. Consequently, the Company is subject to currency fluctuations that may impact its financial position and results. The Company manages its currency risk on loan and mortgage investments by syndicating in the same currency.

A change in exchange rate of the Canadian dollar against the U.S. dollar by 5% would not have a significant impact on the net income and comprehensive income and equity for the year.

(d) Interest rate risk:

Interest rate risk arises due to exposure to the effects of future changes in the prevailing level of interest rates.

The Company is exposed to interest rate risk arising from fluctuations in interest rates primarily on its loan and mortgage investments, convertible debentures, short-term loans payable, loan and mortgage syndications and mortgages payable.

The Company mitigates its exposure to this risk by entering into contracts having either fixed interest rates or interest rates pegged to prime for its loan and mortgage investments and loans and mortgages payable and asset liability matching. Such risk is further mitigated by the general short-term nature of loan and mortgage investments.

TERRA FIRMA CAPITAL CORPORATION

Notes to Consolidated Financial Statements (continued)
(In Canadian dollars)

Years ended December 31, 2014 and 2013

21. Risk management (continued):

The Company has no floating rate financial liabilities. At December 31, 2014, if interest rates had been 100-basis-points lower or higher, with all other variables held constant, net income and comprehensive income and equity for the year would be affected as follows:

	Lower 100 bps	Higher 100 bps
Interest and fees	\$ (786,358)	\$ 786,358

(e) Liquidity risk:

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

The Company manages liquidity risk by forecasting cash flows from operations and anticipated investing and financing activities.

If the Company is unable to continue to have access to its loans and mortgages payable and convertible debentures, the size of the Company's loan and mortgage investments will decrease and the income historically generated through holding larger investments by utilizing leverage will not be earned.

Contractual obligations as at December 31, 2014, are due as follows:

	Less than 1 year	2 years	3 years	Total
Accounts payable and accrued liabilities	\$ 2,227,308	\$ –	\$ –	\$ 2,227,308
Provision for discontinued operations	27,500	–	–	27,500
Income taxes payable	341,432	–	–	341,432
Short-term unsecured loans payable	1,500,000	–	–	1,500,000
Mortgages payable	77,748	1,143,252	–	1,221,000
Convertible debentures	759,501	761,582	11,073,680	12,594,763
Total liabilities and contractual obligations	\$ 4,933,489	\$ 1,904,834	\$ 11,073,680	\$ 17,912,003