

SIR Royalty Income Fund

Consolidated Financial Statements
December 31, 2017 and 2016

March 14, 2018

Independent Auditor's Report

To the Unitholders of SIR Royalty Income Fund

We have audited the accompanying consolidated financial statements of SIR Royalty Income Fund and its subsidiaries, which comprise the consolidated statements of financial position as at December 31, 2017 and December 31, 2016 and the consolidated statements of earnings and comprehensive income, changes in unitholders' equity and cash flows for the years then ended, and the related notes, which comprise 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.

Auditor's 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 the auditor's 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, the auditor considers 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 financial position of SIR Royalty Income Fund and its subsidiaries as at December 31, 2017 and December 31, 2016 and their financial performance and their cash flows for the years then ended in accordance with International Financial Reporting Standards.

(signed) PricewaterhouseCoopers LLP

Chartered Professional Accountants, Licensed Public Accountants
Oakville, Ontario

SIR Royalty Income Fund

Consolidated Statements of Financial Position

As at December 31, 2017 and 2016

	December 31, 2017 \$	December 31, 2016 \$
Assets		
Current assets		
Cash	373,651	340,896
Prepaid expenses and other assets	31,587	31,674
Amounts due from related parties (note 10)	3,927,558	3,712,400
	4,332,796	4,084,970
Loan receivable from SIR Corp. (note 5)	40,000,000	40,000,000
Investment in SIR Royalty Limited Partnership (note 6)	50,984,321	50,984,321
	95,317,117	95,069,291
Liabilities		
Current liabilities		
Accounts payable and accrued liabilities	121,788	101,294
Income taxes payable	499,904	188,836
Amounts due to related parties (note 10)	2,521,071	2,759,268
	3,142,763	3,049,398
Deferred income taxes (note 14)	1,841,000	1,785,000
	4,983,763	4,834,398
Fund units (note 8)	96,169,787	96,169,787
Deficit	(5,836,433)	(5,934,894)
Total unitholders' equity	90,333,354	90,234,893
	95,317,117	95,069,291
Subsequent events (notes 8 and 10)		

Approved by the Board of Trustees

(Signed) Peter Luit
Peter Luit, Director

(Signed) Peter Fowler
Peter Fowler, Director

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

SIR Royalty Income Fund

Consolidated Statements of Earnings and Comprehensive Income For the years ended December 31, 2017 and 2016

	Year ended December 31, 2017 \$	Year ended December 31, 2016 \$
Investment income		
Equity income from SIR Royalty Limited Partnership (notes 6 and 10)	11,051,459	9,738,618
Interest income (note 5)	3,000,000	3,000,000
	<hr/> 14,051,459	<hr/> 12,738,618
General and administrative expenses (note 10)	<hr/> 439,323	<hr/> 410,045
Earnings before income taxes	13,612,136	12,328,573
Income tax expense (note 14)	<hr/> 3,798,017	<hr/> 3,450,896
Net earnings and comprehensive income for the year	<hr/> 9,814,119	<hr/> 8,877,677
Basic and diluted earnings per Fund unit (note 9)	<hr/> \$ 1.17	<hr/> \$ 1.13

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

SIR Royalty Income Fund

Consolidated Statements of Changes in Unitholders' Equity

For the years ended December 31, 2017 and 2016

	Year ended December 31, 2017			
	Number of Fund units	Amount \$	Deficit \$	Total \$
Balance - Beginning of year	8,375,567	96,169,787	(5,934,894)	90,234,893
Net earnings for the year	-	-	9,814,119	9,814,119
Distributions declared and paid (note 8)	-	-	(9,715,658)	(9,715,658)
Balance - End of year	8,375,567	96,169,787	(5,836,433)	90,333,354

	Year ended December 31, 2016			
	Number of Fund units	Amount \$	Deficit \$	Total \$
Balance - Beginning of year	7,625,567	85,557,287	(5,834,425)	79,722,862
Net earnings for the year	-	-	8,877,677	8,877,677
Distributions declared and paid (note 8)	-	-	(8,978,146)	(8,978,146)
Issuance of Fund units (note 8)	750,000	10,612,500	-	10,612,500
Balance - End of year	8,375,567	96,169,787	(5,934,894)	90,234,893

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

SIR Royalty Income Fund
Consolidated Statements of Cash Flows
For the years ended December 31, 2017 and 2016

	Year ended December 31, 2017 \$	Year ended December 31, 2016 \$
Cash provided by (used in)		
Operating activities		
Net earnings for the year	9,814,119	8,877,677
Items not affecting cash		
Current income taxes (note 14)	3,742,017	3,266,896
Deferred income taxes (note 14)	56,000	184,000
Equity income from SIR Royalty Limited Partnership	(11,051,459)	(9,738,618)
Distributions received from SIR Royalty Limited Partnership (note 10)	10,835,529	9,544,729
Income taxes paid	(3,430,949)	(3,551,633)
Net change in non-cash working capital items (note 12)	(216,844)	59,532
	<u>9,748,413</u>	<u>8,642,583</u>
Financing activities		
Distributions paid to unitholders	(9,715,658)	(8,978,146)
	<u>32,755</u>	<u>(335,563)</u>
Change in cash during the year		
Cash - Beginning of year	<u>340,896</u>	<u>676,459</u>
Cash - End of year	<u>373,651</u>	<u>340,896</u>

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

SIR Royalty Income Fund

Notes to Consolidated Financial Statements
December 31, 2017 and December 31, 2016

1 Nature of operations and seasonality

Nature of operations

SIR Royalty Income Fund (the Fund) is a trust established on August 23, 2004 under the laws of the Province of Ontario, Canada.

On October 1, 2004, the Fund filed a final prospectus for a public offering of units of the Fund. The net proceeds of the offering to the Fund of \$51,166,670 were used by the Fund to acquire, directly, certain bank debt of SIR Corp. (the SIR Loan) and, indirectly, through SIR Holdings Trust (the Trust), all of the Ordinary LP Units of SIR Royalty Limited Partnership (the Partnership). The Partnership owns the Canadian trademarks (the SIR Rights) formerly owned or licensed by SIR Corp. (SIR) or its subsidiaries and used in connection with the operation of the majority of SIR's restaurants in Canada (the SIR Restaurants). The Partnership has granted SIR a 99-year licence to use the SIR Rights in most of Canada in consideration for a Royalty, payable by SIR to the Partnership, equal to 6% of the revenues of the restaurants included in the Royalty Pooled Restaurants (the Licence and Royalty Agreement). The Fund indirectly participates in the revenues generated under the Licence and Royalty Agreement through its Investment in the Partnership (note 6).

The address of the registered office of the Fund is 5360 South Service Road, Suite 200, Burlington, Ontario. The consolidated financial statements were approved by the Board of Trustees on March 13, 2018.

Seasonality

The full-service restaurant sector of the Canadian food-service industry, in which SIR operates, experiences seasonal fluctuations in revenues. Favourable summer weather generally results in increased revenues during SIR's fourth quarter (ending the last Sunday in August) when patios can be open. Additionally, certain holidays and observances also affect dining patterns both favourably and unfavourably. Accordingly, equity income from the Partnership recognized by the Fund will vary in conjunction with the seasonality in revenues experienced by SIR.

2 Basis of presentation

The Fund prepares its consolidated financial statements in accordance with International Financial Reporting Standards (IFRS), as issued by the International Accounting Standards Board (IASB).

3 Summary of significant accounting policies

The significant accounting policies used in the preparation of the consolidated financial statements are as follows:

Basis of measurement

The consolidated financial statements have been prepared under the historical cost convention.

SIR Royalty Income Fund

Notes to Consolidated Financial Statements
December 31, 2017 and December 31, 2016

Consolidation

The Fund prepares its consolidated financial statements in accordance with IFRS and include the accounts of the Fund and its subsidiaries, namely the Trust and SIR GP Inc. All intercompany accounts and transactions have been eliminated.

The Fund consolidates an investee when it is exposed to or has rights to variable returns from its involvement with the investee and has the ability to affect these returns through its power over the investee. Subsidiaries are fully consolidated from the date on which control is obtained by the Fund and are deconsolidated from the date control ceases.

Use of estimates

The preparation of these consolidated financial statements requires management to make estimates and assumptions that affect income and expenses during the reporting periods, in addition to the reported amounts of assets and liabilities and the disclosure of contingent liabilities at the date of the consolidated financial statements. Actual results could differ materially from those estimates in the near term.

Financial instruments

Financial assets and liabilities are recognized when the Fund becomes a party to the contractual provisions of the instrument. Financial assets are derecognized when the rights to receive cash flows from the assets have expired or have been transferred and the Fund has transferred substantially all risks and rewards of ownership.

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.

At initial recognition, the Fund classifies its financial instruments in the following categories, depending on the purpose for which the instruments were acquired:

- i) **Loans and receivables:** Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. The Fund's loans and receivables comprise cash and amounts due from related parties, which are included in current assets due to their short-term nature, and the SIR Loan, which is classified as non-current. Loans and receivables are initially recognized at the amount expected to be received less, when material, a discount to reduce the loans and receivables to fair value. Subsequently, loans and receivables are measured at amortized cost using the effective interest method less a provision for impairment.
- ii) **Financial liabilities at amortized cost:** Financial liabilities at amortized cost comprise accounts payable and accrued liabilities and amounts due to related parties. Accounts payable and accrued liabilities, and amounts due to related parties are initially recognized at the amount required to be paid less, when material, a discount to reduce the financial liabilities to fair value. Subsequently, accounts payable and accrued liabilities, and amounts due to related parties are measured at amortized cost using the effective interest method.

Financial liabilities are classified as current liabilities if payment is due within 12 months, otherwise, they are presented as non-current liabilities.

SIR Royalty Income Fund

Notes to Consolidated Financial Statements
December 31, 2017 and December 31, 2016

Impairment of financial assets

At each reporting date, the Fund assesses whether there is objective evidence that a financial asset at amortized cost is impaired. If such evidence exists, the Fund recognizes an impairment loss as the difference between the amortized cost of the loan or receivable and the present value of the estimated future cash flows, discounted using the instrument's original effective interest rate. The carrying amount of the asset is reduced by this amount either directly or indirectly through the use of an allowance account.

Impairment losses on financial assets carried at amortized cost are reversed in subsequent periods if the amount of the loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognized.

Investments in associates and unconsolidated structured entities

Associates are entities over which the Fund has significant influence, but not control, and include the investment in the Partnership.

A structured entity is an entity that has been designed so that voting or similar rights are not the dominant factor in deciding who controls the entity, such as when any voting rights relate to administrative tasks only, and the relevant activities are directed by means of contractual arrangements. The Fund has determined that its investment in the Partnership is an investment in a structured entity.

The Partnership is a structured entity established to own the Canadian trademarks used in connection with the operations of the SIR Restaurants. SIR consolidates the Partnership, as the sale of Canadian trademarks to the Partnership had no impact on SIR's use of the Canadian trademarks. The Fund has voting control of SIR GP Inc., the managing general partner for the Partnership, with an 80% ownership of SIR GP Inc.'s common shares; however, the Fund does not have the ability to affect the returns on the investment in the Partnership through its power over the Partnership. Accordingly, since the Fund is able to significantly influence the Partnership, it is accounted for as an investment in an associate.

The financial results of the Fund's investments in associates are included in the Fund's consolidated results according to the equity method. Subsequent to the acquisition date, the Fund's share of profits or losses of associates is recognized in the consolidated statements of earnings and its share of other comprehensive income of associates is included in other comprehensive income.

Unrealized gains on transactions between the Fund and an associate are eliminated to the extent of the Fund's interest in the associate. Unrealized losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred. Dilution gains and losses arising from changes in interests in investments in associates are recognized in the consolidated statements of earnings.

The Fund assesses whether there is any objective evidence that its interest in its associate is impaired. If impaired, the carrying value of the Fund's share of the underlying assets of the associate is written down to its estimated recoverable amount (being the higher of fair value less cost to sell and value in use) and charged to the consolidated statements of earnings.

SIR Royalty Income Fund

Notes to Consolidated Financial Statements
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Earnings per Fund unit

Earnings per Fund unit are based on the weighted average number of Fund units outstanding during the period. Diluted earnings per Fund unit are calculated to reflect the dilutive effect, if any, of SIR exercising its right to exchange its Class A GP units into Fund units at the beginning of the period.

Distributions

Distributions to unitholders are intended to be made monthly in arrears and are recorded when declared by the Trustees of the Fund. Distributions to unitholders are recorded as a financing activity in the consolidated statements of cash flows.

Income taxes

Income taxes comprise current and deferred taxes and are recognized in the consolidated statements of earnings and comprehensive income.

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

In general, deferred income taxes are recognized in respect of temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements. Deferred income taxes are determined on a non-discounted basis using tax rates and laws that have been enacted, or substantively enacted, at the consolidated statements of financial position date and are expected to apply when the deferred income tax asset or liability is settled. Deferred income tax assets are recognized to the extent it is probable that the assets can be recovered.

IFRS issued but not yet effective

IFRS 9, Financial Instruments - Classification and Measurement

In July 2014, the IASB issued the final version of IFRS 9, Financial Instruments, bringing together the classification and measurement, impairment and hedge accounting phases of the IASB's project to replace IAS 39 Financial Instruments: Recognition and Measurement. The Fund will adopt IFRS 9 on January 1, 2018 using the modified retrospective method. IFRS 9 will require the Fund to record a provision for the expected credit losses on its amounts due from related parties which management has determined is not material to the consolidated financial statements.

Due to the ability of SIR to exchange the SIR Loan with its Class C GP Units of the Partnership, the SIR Loan will not meet the solely principal and interest requirement. Accordingly, under IFRS 9, the SIR Loan will be recognized at fair value with changes in fair value being recorded in the consolidated statement of earnings. As at January 1, 2018, the estimated fair value of the SIR Loan is approximately \$42,500,000. The difference between the fair value and the carrying value of \$40,000,000 will be recorded in the deficit.

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IFRS 7, Financial Instruments - Disclosure

IFRS 7, Financial Instruments: Disclosure has been amended to require additional disclosures on transition from IAS 39 to IFRS 9. This amendment is effective January 1, 2018.

IFRS 15, Revenue from Contracts with Customers

IFRS 15, Revenue from Contracts with Customers specifies how and when to recognize revenue as well as requiring entities to provide users of financial statements with more informative, relevant disclosures. The standard supersedes IAS 18, Revenue, IAS 11, Construction Contracts, and a number of revenue-related interpretations. IFRS 15 will be adopted by the Partnership on January 1, 2018. Management has evaluated this standard and has determined there will be no impact on the financial statements.

4 Critical accounting estimates and judgments

The Fund makes estimates and assumptions concerning the future that will by definition seldom equal actual results. The following are estimates and judgments that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year:

Investment in the Partnership/consolidation of structured entities

The Partnership receives royalties on the SIR Rights, which are licensed to SIR for use in Royalty Pooled Restaurants. The Fund and SIR each hold an investment in the Partnership. Generally, the Partnership units have no voting rights, except in certain specified conditions.

The determination of the entity having the ability to affect the returns on their investment in the Partnership required significant judgment. Based on an evaluation of the activities of the Partnership and the Partnership Agreement, management concluded the substance of the relationships between the Partnership, SIR and the Fund indicates the Partnership is controlled by SIR. In addition, the evaluation of whether or not the Fund has significant influence over the Partnership is a matter of significant judgment. Based on a review of the operating and financing activities of the Partnership, management has concluded that the Fund is able to significantly influence these activities.

Valuation of the SIR Loan and investment in the Partnership

Management reviews for objective evidence whether there may be an impairment of the SIR Loan or the investment in the Partnership. The review includes a review of the earnings, cash flows and available cash of SIR on a prospective basis to assess SIR's ability to meet its obligations to the Fund for interest payments on the SIR Loan and to the Partnership for the Royalty. Based on the analysis completed during the years ended December 31, 2017 and 2016, no impairments have been recorded in the consolidated financial statements.

SIR Royalty Income Fund

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Fair value of SIR Loan

The fair value of the SIR Loan is estimated by discounting the expected cash flows using a current market interest rate adjusted for SIR's credit risk. Management has used a discount rate of 7% to discount the expected cash flows. In determining the appropriate discount rate, management considered available market information as well as the credit risk for SIR. The fair value of the SIR Loan is sensitive to changes in the discount rate. A 0.25% increase or decrease in the discount rate will result in a \$1,250,000 decrease or increase in the fair value of the SIR Loan.

5 Loan receivable from SIR Corp.

The SIR Loan of \$40,000,000 bears interest at 7.5% per annum, is due October 12, 2044 and is collateralized by a general security agreement covering substantially all of the assets of SIR and its subsidiaries in Canada. Interest income of \$3,000,000 was earned during the year ended December 31, 2017 (2016 – \$3,000,000).

SIR has a credit agreement (Credit Agreement) with a Schedule I Canadian chartered bank (the Lender). The Credit Agreement between SIR and the Lender provides for a three-year facility for a maximum principal amount of \$30,000,000 consisting of a \$20,000,000 revolving term credit facility (Credit Facility 1), and a \$10,000,000 revolving term loan (Credit Facility 2). SIR and the Lender have also entered into a purchase card agreement providing credit of up to an additional \$5,000,000. On December 8, 2017, SIR extended the Credit Agreement from July 6, 2018 to July 6, 2020 under substantially the same terms and conditions. The Credit Agreement as amended provides for a new \$2,200,000 leasing facility.

Credit Facility 1 is for general corporate and operating purposes, bearing interest at the prime rate plus 2.25% and/or the bankers' acceptance rate plus 3.25%, principal repaid in one bullet repayment on July 6, 2020. A standby fee of 0.65% is charged on the undrawn balance of Credit Facility 1. Provided SIR is in compliance with the Credit Agreement, the principal amount of Credit Facility 1 can be repaid and reborrowed at any time during the term of the agreement. Credit Facility 2 bears interest at the prime rate plus 2.25% and/or the bankers' acceptance rate plus 3.25%. The initial advance on Credit Facility 2 is repayable in quarterly instalments of \$500,000.

Under the amended Credit Agreement, subsequent advances on Credit Facility 2 may be requested annually (subject to availability and lender approval), in minimum multiples of \$1,000,000, to finance capital spending on new and renovated restaurants. Each subsequent advance will be repayable in equal quarterly instalments based on a five year amortization, with the remaining outstanding principal balance due on July 6, 2020.

On December 15, 2017, SIR drew an additional \$4,500,000 on Credit Facility 2. This advance is repayable in quarterly instalments of \$225,000, with the remaining outstanding principal balance due on July 6, 2020.

The Credit Agreement is secured by substantially all of the assets of SIR and most of its subsidiaries, which are also guarantors. The Partnership and the Fund have not guaranteed the Credit Agreement. The Credit Agreement qualifies as "permitted indebtedness" within the meaning of the agreements between the Fund, the Partnership and SIR, and as a result the Fund and the Partnership have, as contemplated in the existing agreements, subordinated and postponed their claims against SIR to the claims of the Lender. The terms of the subordination are as contemplated in the previous agreements between the Fund, the Partnership and SIR. This subordination includes a subordination of the Partnership's rights under the License and Royalty Agreement between the Partnership and SIR whereby the Partnership licenses to SIR the right to use

SIR Royalty Income Fund

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December 31, 2017 and December 31, 2016

trademarks and related intellectual property in return for royalty payments based on revenues and will be effected pursuant to the terms of an Intercreditor Agreement.

Under the Intercreditor Agreement, absent a default or event of default under the Credit Agreement, ordinary payments to the Fund and the Partnership can continue and the Partnership can exercise any and all of its rights to preserve the trademarks and related intellectual property governed by the License and Royalty Agreement. However, if a default or an event of default were to occur, the Fund and the Partnership agree not to take actions on their security until the Lender has been repaid in full. However, payments by SIR, to the Fund and the Partnership, will be permitted for such amounts as are required to fund their monthly operating expenses, up to an annual limit. In addition, the Fund, the Partnership and SIR will have the right, acting cooperatively, to reduce payments of Royalties and/or interest on the SIR Loan by up to 50% without triggering a cross default under the Credit Agreement for a period of up to nine consecutive months. SIR and each obligor provided an undertaking to cooperate and explore all options with the Fund to maximize value to the Fund's unitholders and SIR and its shareholders in exchange for the subordinating parties not demanding repayment or enforcing security as a result of any such related party obligation default. The Intercreditor Agreement also contains various other typical covenants of the Fund and the Partnership.

SIR has the right to require the Fund to, indirectly, purchase the Class C GP Units and assume a portion of the SIR Loan as consideration for the acquisition of the Class C GP Units.

6 Investment in SIR Royalty Limited Partnership

On October 12, 2004, the Fund, indirectly through the Trust and SIR GP Inc., respectively, acquired all of the Ordinary LP Units and 99 Ordinary GP Units. The holders of the Ordinary LP Units are entitled to receive a pro rata share of distributions and the holders of the Ordinary GP Units receive a fixed monthly distribution of \$5 in aggregate.

During the year ended December 31, 2016, SIR converted 750,000 of its Class A GP Units in the Partnership into 750,000 Fund units and sold these Fund units. In accordance with the exchange agreement, the Fund converted the 750,000 Class A GP Units received into 750,000 Class A LP Units. The 750,000 Class A LP Units were issued by the Partnership to the Trust at a fair value of \$10,612,500.

The holders of the Class A LP Units are entitled to receive a pro rata share of all residual distributions of the Partnership. As at December 31, 2017, the Fund's interest in the residual earnings of the Partnership was 80.9% (December 31, 2016 – 80.3%). Generally, the Partnership units have no voting rights, except in certain specified conditions.

The Partnership makes cash distributions to its partners in the following order of priority: i) First, to the holders of the Class C GP Units and the Class C LP Units, ii) second, to the holders of the Class B GP Units, iii) third, to the holders of the Ordinary GP Units, and iv) thereafter, to the holders of the Class A GP Units, the Class A LP Units, and the Ordinary LP Units.

SIR Royalty Income Fund

Notes to Consolidated Financial Statements
December 31, 2017 and December 31, 2016

The continuity of the Investment in the Partnership is as follows:

	Year ended December 31, 2017 \$	Year ended December 31, 2016 \$
Balance - Beginning of year	50,984,321	40,371,821
Acquisition of Class A LP units (note 8)	-	10,612,500
Equity income	11,051,459	9,738,618
Distributions declared	(11,051,459)	(9,738,618)
	<hr/>	<hr/>
Balance - End of year	50,984,321	50,984,321

The summarized financial information of the Partnership is as follows:

	As at December 31, 2017 \$	As at December 31, 2016 \$
Cash	267,087	-
Other current assets	5,043,307	5,076,464
Intangible assets	97,585,372	97,569,544
	<hr/>	<hr/>
Total assets	102,895,766	102,646,008
	<hr/>	<hr/>
Current liabilities and total liabilities	5,310,384	5,076,454
	<hr/>	<hr/>
Partners' Interest		
SIR Royalty Income Fund	35,616,956	35,616,956
SIR Corp.	61,968,426	61,952,598
	<hr/>	<hr/>
Total partners' interest	97,585,382	97,569,554

	As at December 31, 2017 \$	As at December 31, 2016 \$
Revenues	17,302,269	16,783,430
	<hr/>	<hr/>
Net earnings and comprehensive income of the Partnership	17,219,940	16,719,251

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Notes to Consolidated Financial Statements
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The reconciliation of the Fund's investment in the Partnership to the Partnership's partners' interest is as follows:

	As at December 31, 2017 \$	As at December 31, 2016 \$
Investment in the Partnership	50,984,321	50,984,321
Transaction costs incurred by the Partnership to issue the Ordinary LP units	(3,533,090)	(3,533,090)
Difference between carrying value and fair value on the conversion of the Class A GP units to Class A LP units	<u>(11,834,275)</u>	<u>(11,834,275)</u>
Partners' interest to SIR Royalty Income Fund	<u>35,616,956</u>	<u>35,616,956</u>

The reconciliation of the Partnership's net earnings to the Fund's equity income is as follows:

	Year ended December 31, 2017 \$	Year ended December 31, 2016 \$
Net earnings and comprehensive income of the Partnership	17,219,940	16,719,251
Priority income allocated to SIR Corp. (Class C GP and Class B GP units)	<u>(3,000,012)</u>	<u>(3,000,012)</u>
Residual earnings	14,219,928	13,719,239
SIR Corp.'s share	<u>(3,168,469)</u>	<u>(3,980,621)</u>
Equity income	<u>11,051,459</u>	<u>9,738,618</u>

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The following table presents the carrying amounts of assets and liabilities recognized by the Fund relating to its interest in the Partnership as well as the Fund's maximum exposure to loss from those interests:

	As at December 31, 2017 \$		As at December 31, 2016 \$	
	Carrying Amount	Maximum Exposure to Loss	Carrying Amount	Maximum Exposure to Loss
Distributions receivable	3,677,558	3,677,558	3,461,628	3,461,628
Advances payable	(2,520,068)	(2,520,068)	(2,759,268)	(2,759,268)
Amounts due from related parties	1,157,490	1,157,490	702,360	702,360
Investment in SIR Royalty Limited Partnership	50,984,321	50,984,321	50,984,321	50,984,321
Total	52,141,811	52,141,811	51,686,681	51,686,681

The maximum exposure to loss is equal to the current carrying amounts of the assets and liabilities recognized by the Fund. The Fund does not provide financial support to the Partnership, nor has the Fund provided any guarantees or other contingent support to the Partnership.

7 Financial instruments

Classification

As at December 31, 2017 and 2016, the classifications of the financial instruments, as well as their carrying and fair values, are as follows:

		Carrying and fair value	
Classification		As at December 31, 2017 \$	As at December 31, 2016 \$
Cash	Loans and receivables	373,651	340,896
Amounts due from related parties	Loans and receivables	3,927,558	3,712,400
Loan receivable from SIR Corp.	Loans and receivables	See below	See below
Accounts payable and accrued liabilities	Financial liabilities at amortized cost	121,788	101,294
Amounts due to related parties	Financial liabilities at amortized cost	2,521,071	2,759,268

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Carrying and fair values

Cash, amounts due from related parties, accounts payable and accrued liabilities, and amounts due to related parties are short-term financial instruments whose fair value approximates the carrying amount given that they will mature in the short term. The carrying value of the SIR Loan as at December 31, 2017 is \$40,000,000 (December 31, 2016 – \$40,000,000). The fair value of the SIR Loan is estimated to be \$42,500,000. The fair value was estimated by discounting the expected cash flows using a current market interest rate adjusted for SIR's credit risk. The estimate of fair value is within level 3 of the fair value hierarchy.

Objectives and policy relating to financial risk management

Financial risk management is carried out by management and the Trustees of the Fund. The Fund's main financial risk exposure, as well as its risk management policy, is detailed as follows:

Interest rate risk

The SIR Loan has a fixed interest rate of 7.5% per annum and has been designated as loans and receivable financial asset. Accordingly, changes in interest rates would not impact the consolidated statements of earnings and comprehensive income or the carrying value of the SIR Loan. However, the fair value of the SIR Loan will vary with changes in interest rates. The Fund is restricted to investing excess cash in short-term investments and it is not the Fund's practice to hedge against changes in interest rates.

Credit risk

The Fund is exposed to credit risk in its cash, amounts due from related parties and the SIR Loan. The maximum exposure to credit risk is the full carrying value of the financial instruments. The Fund minimizes the credit risk of cash by depositing funds with reputable financial institutions and minimizes the credit risk of its amounts due from related parties by managing and analyzing the cash flow of these related parties through the preparation of budgets and forecasts. As at December 31, 2017, amounts due from related parties are not past due. Credit risk also arises from the potential default of SIR on the SIR Loan. Management monitors the SIR Loan for impairment. To date, a provision for uncollectible amounts has not been necessary.

SIR has certain restrictions relating to its Credit Agreement, which could affect payments to the Fund if a default or an event of default were to occur (note 5).

Liquidity risk

Liquidity risk is the risk the Fund will not be able to meet its financial obligations as they fall due and meet expected distributions to its unitholders. The Fund currently settles these obligations out of cash. The ability to do this relies on the Fund collecting its distributions from the Partnership and interest on the SIR Loan. The Fund intends to maintain equal monthly distributions to its unitholders. However, the Trustees of the Fund may authorize increased or decreased distributions from time to time or halt distributions entirely, as they see fit, at their sole discretion. Both the Fund and the Partnership prepare budgets and forecasts to evaluate their ability to meet future cash obligations.

SIR Royalty Income Fund

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8 Fund units

An unlimited number of Fund units may be issued pursuant to the Declaration of Trust. Fund units are redeemable by the holder at a price equal to the lesser of 90% of the market price of a Fund unit during the ten consecutive trading day period ending on the trading day immediately prior to the date on which the Fund units were surrendered for redemption and an amount based on the closing price on the redemption date, subject to certain restrictions. Each holder of Fund units participates pro rata in any distributions from the Fund.

During the year ended December 31, 2016, SIR converted 750,000 of its Class A GP Units into 750,000 Fund units and sold these Fund units. In exchange for the Fund issuing an additional 750,000 Fund units, the Fund received an increased interest in the Partnership recorded at fair value of \$10,612,500. The issuance of Fund units has been recorded at \$10,612,500, being the gross proceeds received by SIR for the sale of the Fund units received. In accordance with the exchange agreement between the Fund, the Partnership, the Trust and SIR, the Fund exchanged the Class A GP Units received from SIR for the 750,000 Class A LP Units. Accordingly the Partnership issued 750,000 Class A LP Units to the Fund. This transaction did not have a dilutive effect on the Fund.

There were no conversions of Class A GP Units into Fund units during the year ended December 31, 2017.

As at December 31, 2017, there are 8,375,567 (December 31, 2016 – 8,375,567) Fund units issued and outstanding. Each Fund unit is entitled to one vote at any meeting of unitholders.

During the year ended December 31, 2017, the Fund declared distributions of \$1.16 per unit (2016 – \$1.14 per unit). Subsequent to December 31, 2017, distributions of \$0.095 per unit were declared and paid in the month of January and February 2018.

The distribution policy of the Fund is, at the discretion of the Trustees, to make distributions of its available cash to the fullest extent possible, taking into account trends in revenues, earnings and cash flows.

9 Earnings per Fund unit

Basic earnings per Fund unit is computed by dividing net earnings by the weighted average number of Fund units outstanding during the year.

SIR has the right to convert the Class A GP Units into Fund units. Diluted earnings per Fund unit is calculated using the weighted average number of Fund units outstanding adjusted to include the effect of the conversion of the Class A GP Units into Fund units.

SIR Royalty Income Fund

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The following table reconciles the basic and diluted weighted average number of Fund units outstanding and basic and diluted earnings per Fund unit:

	Basic	Adjustment for conversion of Class A GP units	Diluted
Net earnings for the year ended December 31, 2017	\$ 9,814,119	\$ 2,319,412	\$ 12,133,531
Net earnings per Fund unit for the year ended December 31, 2017	\$ 1.17		\$ 1.17
Weighted average number of Fund units outstanding for the year ended December 31, 2017	8,375,567	1,981,616	10,357,183
Net earnings for the year ended December 31, 2016	\$ 8,877,677	\$ 2,878,976	\$ 11,756,653
Net earnings per Fund unit for the year ended December 31, 2016	\$ 1.13		\$ 1.13
Weighted average number of Fund units outstanding for the year ended December 31, 2016	7,890,635	2,546,029	10,436,664

10 Related party transactions and balances

During the year ended December 31, 2017, the Fund recorded equity income of \$11,051,459 (2016 - \$9,738,618) and received distributions of \$10,835,529 (2016 - \$9,544,729) from the Partnership. The Fund, indirectly through the Trust, is entitled to receive a pro rata share of all residual distributions. The Fund's equity income is dependent upon the revenues generated by SIR for the restaurants subject to the Licence and Royalty Agreement. Under the terms of the Licence and Royalty Agreement, SIR may be required to pay a Make-Whole Payment in respect of the reduction in revenues for restaurants permanently closed during a reporting period. SIR is not required to pay any Make-Whole Payment in respect of a permanently closed restaurant following the date on which the number of restaurants in the Royalty Pooled Restaurants is equal to or greater than 68 or following October 12, 2019, whichever occurs first. On January 1 of each year (the Adjustment Date), the restaurants subject to the Licence and Royalty Agreement are adjusted for new restaurants opened for at least 60 days preceding such Adjustment Date in the previous fiscal year. At each Adjustment Date, SIR will be entitled to convert its Class B GP Units into Class A GP Units based on a conversion formula defined in the Partnership Agreement.

SIR Royalty Income Fund

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On January 1 of each year, Class B GP Units are converted into Class A GP Units for new SIR Restaurants added to the Royalty Pooled Restaurants based on 80% of the initial estimated revenues and the formula defined in the Partnership Agreement. Additional Class B GP Units may be converted into Class A GP Units in respect of these new SIR Restaurants if actual revenues of the new SIR Restaurants exceeded 80% of the initial estimated revenues and the formula defined in the Partnership Agreement. Conversely, converted Class A GP Units will be returned by SIR if the actual revenues of the new SIR Restaurants are less than 80% of the initial estimated revenues. In December of each year, an additional distribution will be payable to the Class B GP unitholders provided that actual revenues of the new SIR Restaurants exceed 80% of the initial estimated revenues, or there will be a reduction in the distributions to the Class A GP unitholders if revenues are less than 80% of the initial estimated revenues.

On January 1, 2018, three (January 1, 2017 - one) new SIR Restaurants were added to Royalty Pooled Restaurants in accordance with the Partnership Agreement. As consideration for the additional Royalty associated with the addition of three new SIR Restaurants on January 1, 2018 (January 1, 2017 - one), as well as the Second Incremental Adjustment for one new SIR Restaurant added to Royalty Pooled Restaurants on January 1, 2017 (January 1, 2016 - two), SIR converted its Class B GP Units into Class A GP Units based on the formula defined in the Partnership Agreement. The number of Class B GP Units that SIR converted into Class A GP Units was reduced by an adjustment for the permanent closure of three (January 1, 2017 - one) SIR Restaurants during the prior year. The net effect of these adjustments to Royalty Pooled Restaurants was that SIR converted 34,810 Class B GP Units into 34,810 Class A GP Units (January 1, 2016 – SIR exchanged 79,481 Class A GP Units into 79,481 Class B GP Units) on January 1, 2018 at a value of \$2,846,999 (January 1, 2017 - \$15,828) (note 6).

In addition, the revenues of the one (January 1, 2016 – two) new SIR Restaurant added to Royalty Pooled Restaurants on January 1, 2017 was less than 80% of the Initial Adjustment's estimated revenue and, as a result, the distributions on the Class A GP Units were reduced by a special conversion refund of \$52,078 in December 2017 and paid in January 2018 (December 31, 2016 – \$492 paid in January 2017). As a result of the permanent closure of three SIR Restaurants during the year, Make-Whole Payments totalling \$296,231 (year ended December 31, 2016 – \$77,345) were paid by SIR to the Partnership.

Class A GP Units and Class B GP Units are held by SIR.

The Partnership has entered into an arrangement with the Fund and the Trust whereby the Partnership will provide or arrange for the provision of services required in the administration of the Fund and the Trust. The Partnership has arranged for these services to be provided by SIR GP Inc. in its capacity as the Managing General Partner, or SIR as the General Partner. SIR, on behalf of SIR GP Inc., also provides services to the Partnership for its administration. For the year ended December 31, 2017, the Partnership provided these services to the Fund and the Trust for consideration of \$24,000 (2016 - \$24,000), which was the amount of consideration agreed to by the related parties and has been recorded in general and administrative expenses.

SIR Royalty Income Fund

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Amounts due from (to) related parties consist of:

	As at December 31, 2017 \$	As at December 31, 2016 \$
SIR Corp.		
Interest receivable	250,000	250,000
Advances receivable	-	772
Amounts receivable from SIR Corp.	<u>250,000</u>	<u>250,772</u>
Distributions receivable from SIR Royalty Limited Partnership	<u>3,677,558</u>	<u>3,461,628</u>
Amounts due from related parties	<u>3,927,558</u>	<u>3,712,400</u>
SIR Corp.		
Advances payable	1,003	-
Advances payable to SIR Royalty Limited Partnership	<u>2,520,068</u>	<u>2,759,268</u>
	<u>2,521,071</u>	<u>2,759,268</u>

Amounts due from (to) related parties are non-interest bearing and due on demand. All advances were conducted as part of the normal course of business operations.

Compensation of key management

The Fund does not have any employees. Compensation awarded to the Board of Trustees consists of fees of \$106,200 for the year ended December 31, 2017 (2016 - \$91,900).

11 Capital management

The Fund's capital consists of units of the Fund, as described in note 8. The objectives in managing the capital are to safeguard the Fund's ability to continue as a going concern, to provide an adequate return to its unitholders appropriate to their level of risk and to distribute excess cash to the unitholders. The Fund has no third party debt or bank lines of credit. The Fund had no capital expenditures during the year ended December 31, 2017 and is not expected to have significant capital expenditures in the future.

SIR has a Credit Agreement, which requires the Fund and the Partnership to subordinate and postpone their claims against SIR to the claims of the Lender in the event of a default (note 5).

SIR Royalty Income Fund

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12 Net change in non-cash working capital items

Net change in non-cash working capital items comprises:

	Year ended December 31, 2017 \$	Year ended December 31, 2016 \$
Prepaid expenses and other assets	87	(4,018)
Amounts due from related parties	772	3,561
Accounts payable and accrued liabilities	20,494	1,804
Amounts due to related parties	(238,197)	58,185
	<u>(216,844)</u>	<u>59,532</u>

13 Economic dependence

The Fund's income is derived from interest income on the SIR Loan and distributions from the Partnership; accordingly, the Fund is economically dependent on SIR.

14 Income taxes

Income tax expense is as follows:

	Year ended December 31, 2017 \$	Year ended December 31, 2016 \$
Current	3,742,017	3,266,896
Deferred	56,000	184,000
	<u>3,798,017</u>	<u>3,450,896</u>

The Fund's income not distributed to its unitholders is taxable at a rate of 53.53% (2016 – 53.53%). Distributions to unitholders are taxable at the combined federal and provincial tax rate, which is 26.5% for the year ended December 31, 2017 (2016 – 26.5%).

SIR Royalty Income Fund

Notes to Consolidated Financial Statements

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The reconciliation of the Fund's effective tax rate to the combined Canadian federal and provincial tax rate is as follows:

	Year ended December 31, 2017 \$	Year ended December 31, 2016 \$
Earnings before income taxes	13,612,136	12,328,573
Income tax provision at 53.53% (2016 – 53.53%)	7,286,576	6,599,485
Add (deduct):		
Partnership expenses deductible for tax purposes	56,000	55,000
Change in tax rates	-	129,000
Permanent differences	122,320	(43,450)
Other	(3,974)	17,186
Differences in tax rates	(3,662,905)	(3,306,325)
	<u>3,798,017</u>	<u>3,450,896</u>

Deferred tax liabilities consist of the following:

	Investment in the Partnership \$
Balance as at December 31, 2015	1,601,000
Charged to consolidated statements of earnings	<u>184,000</u>
Balance as at December 31, 2016	1,785,000
Charged to consolidated statements of earnings	<u>56,000</u>
Balance as at December 31, 2017	<u>1,841,000</u>