EXTENDICARE®

... helping people live better

MANAGEMENT'S DISCUSSION AND ANALYSIS

Year Ended December 31, 2018

Extendicare Inc.
Dated: February 28, 2019

50 SINCE 1968
YEARS OF HELPING
PEOPLE LIVE BETTER

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TABLE OF CONTENTS

BASIS OF PRESENTATION

This Management's Discussion and Analysis (MD&A) provides information on Extendicare Inc. and its subsidiaries, and unless the context otherwise requires, references to "Extendicare", the "Company", "we", "us" and "our" or similar terms refer to Extendicare Inc., either alone or together with its subsidiaries. The Company's common shares (the "Common Shares") are listed on the Toronto Stock Exchange (TSX) under the symbol "EXE". The registered office of Extendicare is located at 3000 Steeles Avenue East, Suite 700, Markham, Ontario, Canada, L3R 9W2.

Extendicare and its predecessors have been in operation since 1968, providing care and services to seniors throughout Canada. Following the sale of its U.S. business in 2015 and the repositioning of the Company as a pure-play Canadian services provider to the expanding senior care sector, we have continued to grow the Company's operations across the continuum of seniors' care.

Extendicare has prepared this MD&A to provide information to current and prospective investors of the Company to assist them to understand Extendicare's financial results for the year ended December 31, 2018. This MD&A should be read in conjunction with Extendicare's audited consolidated financial statements for the years ended 2018 and 2017, and the notes thereto, prepared in accordance with International Financial Reporting Standards (IFRS). These financial statements and notes are available on Extendicare's website at www.extendicare.com. All currencies are in Canadian dollars unless otherwise indicated. Except as otherwise specified, references to years indicate the fiscal year ended December 31, 2018, or December 31 of the year referenced.

The discussion and analysis in this MD&A are based upon information available to management as of February 28, 2019. This MD&A should not be considered all-inclusive, as it excludes changes that may occur in general economic, political and environmental conditions. Additionally, other events may or may not occur, which could affect the Company in the future.

ADDITIONAL INFORMATION

Additional information about Extendicare, including its latest Annual Information Form, may be found on SEDAR's website at www.sedar.com under Extendicare's issuer profile and on Extendicare's website at www.extendicare.com. A copy of this and other public documents of Extendicare are available upon request to the Corporate Secretary of Extendicare.

FORWARD-LOOKING STATEMENTS

Information provided by Extendicare from time to time, including in this Annual Report, contains or may contain forward-looking statements concerning anticipated future events, results, circumstances, economic performance or expectations with respect to the Company, including, without limitation: statements regarding its business operations, business strategy, growth strategy, results of operations and financial condition; statements relating to the expected annual revenue, net operating income yield (NOI Yield) to be derived from development projects and adjusted funds from operations to be derived from acquisitions and development projects; and statements relating to indemnification provisions and deferred consideration in respect of disposed operations. Forward-looking statements can be identified by the expressions "anticipate", "believe", "estimate", "expect", "intend", "objective", "plan", "project", "will" or other similar expressions or the negative thereof. These forward-looking statements reflect the Company's current expectations regarding future results, performance or achievements and are based upon information currently available to the Company and on assumptions that the Company believes are reasonable.

Although forward-looking statements are based upon estimates and assumptions that the Company believes are reasonable based upon information currently available, these statements are not representations or guarantees of future results, performance or achievements of the Company and are inherently subject to significant business, economic and competitive uncertainties and contingencies. In addition to the assumptions and other factors referred to specifically in connection with these forward-looking statements, the risks, uncertainties and other factors that could cause the actual results, performance or achievements of Extendicare to differ materially from those expressed or implied by the forward-looking statements, include, without limitation, the following: changes in the overall health of the economy and government; the ability of the Company to attract and retain qualified personnel; changes in the health care industry in general and the long-term care industry in particular because of political and economic influences; changes in applicable accounting policies; changes in regulations governing the health care and long-term care industries and the compliance by Extendicare with such regulations; changes in government funding levels for health care services; changes in tax laws; resident care and class action litigation, including the Company's exposure to punitive damage claims, increased insurance costs and other claims; the ability of Extendicare to maintain and increase resident occupancy levels and home health care volumes; changes in competition; changes in demographics and local environment economies; changes in foreign exchange and interest rates; changes in the financial markets, which may affect the ability of Extendicare to refinance debt; and the availability and terms of capital to Extendicare to fund capital expenditures and acquisitions; changes in the anticipated outcome and benefits of dispositions, acquisitions and development projects, including risks relating to completion; and those other risks, uncertainties and other factors identified in the Company's other public filings with the Canadian securities regulators available on SEDAR's website at www.sedar.com under Extendicare's issuer profile.

The forward-looking statements contained in this Annual Report are expressly qualified by this cautionary statement. Given these risks and uncertainties, readers are cautioned not to place undue reliance on the forward-looking statements of Extendicare. The forward-looking statements speak only as of the date of this Annual Report. Except as required by applicable securities laws, the Company assumes no obligation to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise.

NON-GAAP MEASURES

Extendicare assesses and measures operating results and financial position based on performance measures referred to as "net operating income", "net operating income margin", "EBITDA", "Adjusted EBITDA", "Adjusted EBITDA margin", "earnings before depreciation, amortization, and other expense", "earnings (loss) from continuing operations before separately reported items, net of taxes", "Funds from Operations", and "Adjusted Funds from Operations". These measures are commonly used by Extendicare and its investors as a means of assessing the performance of the core operations in comparison to prior periods. They are presented by Extendicare on a consistent basis from period to period, thereby allowing for consistent comparability of its operating performance. In addition, the Company assesses its return on investment in development activities using the non-GAAP financial measure "NOI Yield". These measures are not recognized under GAAP and do not have standardized meanings prescribed by GAAP. These non-GAAP measures are presented in this document because either: (i) management believes that they are a relevant measure for users of the Company's financial statements to assess the Company's operating performance and ability to pay cash dividends; or (ii) certain ongoing rights and obligations of Extendicare may be calculated using these measures. Such non-GAAP measures may differ from similar computations as reported by other issuers, and accordingly, may not be comparable to similarly titled measures as reported by such issuers. They are not intended to replace earnings (loss) from continuing operations, net earnings (loss), cash flow, or other measures of financial performance and liquidity reported in accordance with GAAP.

References to “net operating income”, or “NOI”, in this document are to revenue less operating expenses, and this value represents the underlying performance of our operating business segments. References to “net operating income margin” are to net operating income as a percentage of revenue.

References to “EBITDA” in this document are to earnings (loss) from continuing operations before net finance costs, income taxes, depreciation and amortization. References to “Adjusted EBITDA” in this document are to EBITDA adjusted to exclude the line item “other expense”, and as a result, is equivalent to the line item “earnings before depreciation, amortization, and other expense” reported on the consolidated statements of earnings. References to “Adjusted EBITDA Margin” are to Adjusted EBITDA as a percentage of revenue. Management believes that certain lenders, investors and analysts use EBITDA and Adjusted EBITDA to measure a company’s ability to service debt and meet other payment obligations, and as a common valuation measurement in the long-term care industry. For example, certain of our debt covenants use Adjusted EBITDA in their calculations.

References to “earnings (loss) from continuing operations before separately reported items, net of tax” in this document are to earnings (loss) from continuing operations, excluding the following separately reported line items: “fair value adjustments”, “loss (gain) on foreign exchange and investments”, and “other expense”. These line items are reported separately and excluded from certain performance measures, because they are transitional in nature and would otherwise distort historical trends. They relate to the change in the fair value of, or gains and losses on termination of, convertible debentures, and interest rate agreements, as well as gains or losses on the disposal or impairment of assets and investments, and foreign exchange gains or losses on capital items. In addition, these line items may include acquisition related costs, restructuring charges, proxy contest costs, and the write-off of unamortized deferred financing costs on early retirement of debt. The above separately reported line items are reported on a pre-tax and on an after-tax basis as a means of deriving earnings (loss) from operations and related earnings per share excluding such items.

“Funds from Operations”, or “FFO”, is defined as Adjusted EBITDA less depreciation for furniture, fixtures, equipment and computers, or “depreciation for FFEC”, accretion costs, net interest expense, and current income taxes. Depreciation for FFEC is considered representative of the amount of maintenance (non-growth) capital expenditures, or “maintenance capex”, to be used in determining “Funds from Operations”, as the depreciation term is generally in line with the life of these assets. FFO is a recognized earnings measure that is widely used by public real estate entities, particularly by those entities that own and/operate income-producing properties. Management believes that certain investors and analysts use FFO, and as such has included FFO to assist with their understanding of the Company’s operating results.

“Adjusted Funds from Operations”, or “AFFO”, is defined as FFO plus: i) the reversal of non-cash deferred financing and accretion costs; ii) the reversal of non-cash share-based compensation; iii) the principal portion of government capital funding; iv) amounts received from income support arrangements; and v) the reversal of income or loss of the captive insurance company that was included in the determination of FFO, as those operations are funded through investments held for U.S. self-insured liabilities, which are not included in the Company’s reported cash and short-term investments. In addition, AFFO is further adjusted to account for the difference in total maintenance capex incurred from the amount deducted in the determination of FFO. Since our actual maintenance capex spending fluctuates on a quarterly basis with the timing of projects and seasonality, the adjustment to AFFO for these expenditures from the amount of depreciation for FFEC already deducted in determining FFO, may result in an increase to AFFO in the interim periods reported. Management believes that AFFO is a relevant measure of the ability of the Company to earn cash and pay cash dividends to shareholders.

Both FFO and AFFO are subject to other adjustments, as determined by management in its discretion, that are not representative of Extendicare’s operating performance.

References to “payout ratio” in this document are to the ratio of dividends declared per share to AFFO per basic share.

References to “NOI Yield” in this document are to a financial measure used by the Company to assess its return on investment in development activities. NOI Yield is defined by the Company as the estimated stabilized NOI of a development property in the first year it achieves expected stabilized occupancy divided by the estimated Adjusted Development Costs, as defined below. Management believes that this is a relevant measure of the Company’s total economic return of a development project.

“Adjusted Development Costs” is defined as development costs on a GAAP basis (which includes the cost of land, hard and soft development costs, furniture, fixtures and equipment) plus/minus cumulative net operating losses/earnings generated by the development property prior to achieving expected stabilized occupancy, plus an estimated imputed cost of capital during the development period through to the expected stabilized occupancy.

Reconciliations of “earnings (loss) from continuing operations before income taxes” to “Adjusted EBITDA” and “net operating income” are provided under the headings “2018 Selected Quarterly Information”, “2018 Fourth Quarter Financial Review” and “2018 Financial Review”.

Reconciliations of “earnings from continuing operations” to “FFO” and “AFFO” are provided under the heading “Adjusted Funds from Operations”.

Reconciliations of “net cash from operating activities” to “AFFO” are provided under the heading “Adjusted Funds from Operations – Reconciliation of Net Cash from Operating Activities to AFFO”.

BUSINESS STRATEGY

Our strategy is to be the leading provider of care and services to seniors in Canada. To do this, we strive to provide quality, person-centred care through compassionate caregivers across the continuum of care – offering the right care at the right time, in the right place for Canadian seniors as they age and their care and service needs change – and to be an employer of choice in the communities in which we operate.

Our core long-term care services are complemented by a market leading home health care platform operating under the ParaMed banner and a private-pay retirement business operating under the Esprit Lifestyle Communities banner, as well as growing management/consulting and group purchasing divisions. We have continued to grow Esprit through acquisition and development and to pursue private-pay home health care opportunities with the intent to diversify our revenue streams to achieve a better balance between government and privately funded activities.

We believe that the effective execution of this strategy will provide an appropriate and consistent return to our shareholders who have demonstrated their belief in our mission by investing in Extendicare.

SIGNIFICANT 2018 EVENTS AND DEVELOPMENTS

This section provides an update on our current activities related to the growth of our retirement operations and the completion of our convertible debt refinancing in 2018. Refer to the discussion under the heading “Other Significant Developments” for a summary of other developments affecting the financial results or operations of Extendicare.

Growth of Retirement Operations

As part of the execution of our strategy to continue to grow along the senior care and services continuum, we continue to expand our private-pay retirement operations through the acquisition and development of retirement communities under our Esprit Lifestyle Communities brand. Our retirement communities offer a variety of lifestyle options, including independent and enhanced living and memory care, as well as short-term stay, and respite care.

During 2018, Esprit Lifestyle Communities had nine retirement communities in operation that it had either acquired or developed since 2015, and in January 2019, it opened its tenth, Bolton Mills Retirement Community (Bolton Mills) in Bolton, Ontario.

RETIREMENT ACQUISITIONS

In April 2018, the Company completed the acquisition of the Lynde Creek Retirement Community, located in Whitby, Ontario, for a cash purchase price of $33.8 million, including working capital adjustments (the “Lynde Creek Acquisition”). The acquired community consists of Lynde Creek Manor, a retirement residence offering 93 independent and assisted living suites, (the “Manor”); Lynde Creek Village, a life lease seniors community of 113 townhomes, (the “Village”); and 3.7 acres of adjacent land for expansion (the “Excess Land”). Further details of the Lynde Creek Acquisition are provided in *note 6* of the audited consolidated financial statements.

The Manor is a modern private pay luxury retirement residence with 93 suites offering independent supportive living (ISL) and assisted living (AL) suites. The Village is an enclave of 113 townhomes adjacent to the Manor. Included in the purchase agreement is the ownership of the underlying land and the leasehold interest related to the life leases. Upon the resale of a townhome, the Company earns a fee equal to 10% of the proceeds. The Excess Land is situated immediately adjacent to the Manor, with zoning that allows for a strategic expansion to include additional ISL/AL suites or seniors’ apartments.

2018 COMPLETED PROJECTS

In November 2018, we completed the 45-suite expansion of Douglas Crossing Retirement Community (Douglas Crossing), in Uxbridge, Ontario, and at January 31, 2019, the expanded 148-suite community was 80% leased. Phase 1, or 103 suites, opened in October 2017, and by the end of 2018 was 92% leased. The robust pre-lease activity of phase 1 led to the decision in 2017 to accelerate the phase 2 expansion plans. The Adjusted Development Costs for the total 148-suite project are estimated to be $35.7 million, with an expected stabilized occupancy of 94% in the 2019 fourth quarter, an estimated stabilized NOI of $4.1 million and a corresponding NOI Yield of 11.4%.

At the end of December 2018, we completed development of Bolton Mills, a 112-suite retirement community in Bolton, Ontario, and welcomed its first resident in January 2019. The Adjusted Development Costs for this project are estimated to be $30.7 million, with an expected stabilized occupancy of 95% in the 2021 fourth quarter, an estimated stabilized NOI of $2.4 million and a corresponding NOI Yield of 7.8%.

PROJECTS UNDER CONSTRUCTION

We currently have a 124-suite retirement project under construction in Barrie, Ontario, that is scheduled to open in the 2019 fourth quarter. The Adjusted Development Costs for this project are estimated to be $38.5 million, with an expected stabilized occupancy of 92% in the 2022 second quarter, an estimated stabilized NOI of $3.2 million and a corresponding NOI Yield of 8.2%.

Issue of 2025 Convertible Debentures and Redemption of 2019 Convertible Debentures

In April 2018, the Company issued $126.5 million aggregate principal amount of 5.00% convertible unsecured subordinated debentures due April 30, 2025 (the "2025 Debentures"), with a conversion price of $12.25 per Common Share (the "Offering"). The initial offering for $110.0 million of the 2025 Debentures closed on April 17, 2018, and the exercise of the over-allotment option for $16.5 million debentures closed on April 25, 2018.

The net proceeds from the Offering of $120.9 million, together with cash on hand, was used by the Company to finance the redemption of its outstanding 6.00% convertible unsecured subordinated debentures due September 30, 2019 (the "2019 Debentures"). The redemption of the 2019 Debentures was completed on April 30, 2018, at a price equal to the sum of the outstanding aggregate principal amount of $126.5 million and all accrued and unpaid interest thereon for a total of $127.1 million, or $1,004.93 for each $1,000 principal amount of 2019 Debentures. As a result of the early redemption, the unaccreted liability of $1.4 million and unamortized deferred financing costs of $1.1 million were expensed, and the related equity portion of $5.6 million was classified as part of accumulated deficit during the 2018 second quarter. Further details of the issuance and redemption are provided in *note 12* of the audited consolidated financial statements.

BUSINESS OVERVIEW

Extendicare, through its subsidiaries, is the largest private-sector operator of long-term care centres in Canada and we believe is the largest private-sector provider of publicly funded home health care services in Canada through our wholly owned subsidiary ParaMed Inc. (ParaMed). In addition, the Company owns and operates retirement communities under the Esprit Lifestyle Communities brand, provides management and consulting services to third-party owners of senior care and living centres through its Extendicare Assist division, and provides group purchasing services to third-party clients through its SGP Purchasing Partner Network, or SGP, division. In 2018, approximately 56% of the revenue from our Canadian operations was derived from our long-term care operations, approximately 39% was from our home health care business, approximately 3% was from our retirement living operations, and the balance was from the Extendicare Assist and SGP divisions.

As at December 31, 2018, Extendicare owned and operated 58 LTC centres, 9 retirement communities, and managed 53 senior care and living centres for third parties. In total, we operated 120 senior care and living centres across four provinces in Canada, with capacity for 15,447 residents, with a significant presence in Ontario and Alberta, where approximately 76% and 11% of our residents, respectively were served. ParaMed's home health care services operated from 35 locations across six provinces (29 in Ontario, 1 in British Columbia, 2 in Alberta, 1 in Manitoba, 1 in Nova Scotia, and 1 in Quebec) providing approximately 10.9 million hours of service in 2018. SGP Purchasing Partner Network provided group purchasing services to third-party clients representing approximately 51,100 seniors across Canada. Our highly trained workforce of approximately 23,000 individuals across Canada is dedicated to helping people live better through a commitment to quality service and passion for what we do.

The table below summarizes the senior care and living centres operated by Extendicare, including those managed for third parties, as at December 31, 2018. Included are nine LTC centres in Ontario that the Company operates under 25-year finance lease arrangements, with full ownership obtained at the end of the lease term. In addition to the following, the Company owns land adjacent to its retirement residence at Lynde Creek in Whitby, Ontario, on which there is an enclave of 113 townhomes, known as Lynde Creek Village, that are leased by the Company to seniors under life leases.

	Long-term Care		Retirement Living		Chronic Care Unit		Total	
By Province	**No. of Centres**	**Resident Capacity**	**No. of Centres**	**Resident Capacity**	**No. of Centres**	**Resident Capacity**	**No. of Centres**	**Resident Capacity**
Owned/Leased								
Ontario	34	5,207	5	472	–	–	39	5,679
Alberta	14	1,519	–	–	–	–	14	1,519
Saskatchewan	5	649	4	341	–	–	9	990
Manitoba	5	762	–	–	–	–	5	762
	58	8,137	9	813	–	–	67	8,950
Managed								
Ontario	42	5,338	6	660	1	120	49	6,118
Alberta	1	102	1	109	–	–	2	211
Manitoba	2	168	–	–	–	–	2	168
	45	5,608	7	769	1	120	53	6,497
Total	**103**	**13,745**	**16**	**1,582**	**1**	**120**	**120**	**15,447**

(1) The centres are categorized based on the predominant level of care provided, the type of licensing and the type of funding provided. For example, two of our long-term care centres with retirement wings have been categorized as LTC centres. In addition, government-funded supportive living suites have been categorized as LTC centres due to the nature of the regulatory oversight and government-determined fee structure.

The following reflects the change in operating capacity of our Canadian senior care and living centres during 2018 and 2017.

	2018		2017	
Senior Care and Living Centres	**No. of Centres**	**Resident Capacity**	**No. of Centres**	**Resident Capacity**
As at beginning of year	**116**	**15,004**	118	15,022
Managed contracts added	**4**	**524**	7	764
Managed contracts ceased	**(1)**	**(243)**	(10)	(900)
Retirement communities acquired/developed	**1**	**138**	1	103
LTC addition	**–**	**24**	–	–
Operational capacity adjustments	**–**	**–**	–	15
As at end of year	**120**	**15,447**	116	15,004

Operating Segments

The Company reports the following segments within its Canadian operations: i) long-term care; ii) retirement living; iii) home health care; iv) management, consulting and group purchasing as “other Canadian operations”; and v) the Canadian corporate functions and any intersegment eliminations as “corporate Canada”. For financial reporting purposes, the Company’s owned and operated centres are reported under the “long-term care” or the “retirement living” operating segment based on the predominate level of care provided. The Company’s managed centres are reported under the “other Canadian operations” segment, as the revenue from those operations is earned on a fee-for-service basis.

The Company continues to group its remaining U.S. operations as one segment, consisting of its wholly owned Bermuda-based captive insurance company, Laurier Indemnity Company, Ltd. (the “Captive”) that insured Extendicare’s U.S. general and professional liability risks up to the date of the sale of the Company’s U.S. business in 2015 (the “U.S. Sale Transaction”). The Captive’s expense incurred or release of reserves for self-insured liabilities as well as the disposed U.S. businesses are presented as discontinued operations; while the Captive’s costs to administer and manage the settlement of the remaining claims are reported as continuing operations within the U.S. segment.

The following describes the continuing businesses and operating segments of Extendicare.

LONG-TERM CARE (including government-funded supportive living)

Extendicare owns and operates for its own account 58 LTC centres with capacity for 8,137 residents, inclusive of a stand-alone designated supportive living centre (140 suites) and a designated supportive living wing (60 suites) in Alberta, and two retirement wings (76 suites) in Ontario. Revenue from the long-term care operations represented 56.5% of consolidated revenue from continuing operations in 2018 (2017 year – 56.2%).

In Canada, provincial legislation and regulations closely control all aspects of operation and funding of LTC centres, including the fee structure, subsidies, the adequacy of physical centres, standards of care and accommodation, equipment and personnel. A substantial portion of the fees paid to providers of these services are funded by provincial programs, with a portion to be paid by the resident. Nobody is refused access to long-term care due to an inability to pay. A government subsidy, generally based on an income test, is available for residents who are unable to afford the resident co-payment. In Alberta, designated supportive living centres provide services similar to those provided by retirement communities, and were introduced by Alberta Health Services (AHS) as an alternative setting for residents not yet requiring the needs of a more expensive LTC centre. The designated supportive living operations are licensed, regulated and funded by AHS in a similar manner to LTC centres, including a government-determined fee structure.

In Ontario, operators have the opportunity to receive additional funding through higher accommodation rates charged to residents for private and semi-private accommodation, at maximum preferred accommodation rates that are fixed by the government. Operators are permitted to designate up to 60% of the resident capacity of a centre as preferred accommodation and charge higher accommodation rates that vary according to the structural classification of the LTC centre.

The following summarizes the composition of the owned/leased LTC centres operated by Extendicare in Ontario, as at December 31, 2018, as well as the maximum preferred differential rates for each classification of bed.

					Composition of Beds	
Ontario Owned/Leased	**No. of Centres**	**Private $26.04 premium**	**Private $18.74 premium**	**Semi-private $8.33 premium**	**Basic/Other**	**Total**
New	13	1,106	–	–	741	1,847
Class C (1)	21	–	476	1,396	1,412	3,284
	34	1,106	476	1,396	2,153	5,131

(1) Beds in operation of 3,284 exclude 3 beds held in abeyance.

RETIREMENT LIVING

Under the Esprit Lifestyle Communities brand, the Company owned and operated nine retirement communities with 813 suites as at December 31, 2018, with a tenth community (112 suites) that opened in January 2019. Four of these communities (341 suites) are located in Saskatchewan and six communities (584 suites) are located in Ontario. A new retirement community (124 suites) is presently under construction in Ontario, and plans are under way for a 59-suite expansion of our 63-suite Empire Crossing retirement community in Port Hope, Ontario.

Extendicare's retirement communities provide accommodation and services to private-pay residents at rates set by the Company based on the services provided and market conditions. The monthly fees vary depending on the type of accommodation, level of care and services chosen by the resident, and the location of the retirement community. Residents are able to choose the living arrangements best suited to their personal preference and needs, as well as the level of care and support they receive as their needs evolve over time. Revenue from these operations represented 3.0% of consolidated revenue from continuing operations in 2018 (2017 year – 1.9%).

HOME HEALTH CARE

Extendicare provides home health care services through ParaMed, whose professionals and staff members are skilled in providing complex nursing care, occupational, physical and speech therapy, and assistance with daily activities to accommodate clients of all ages living at home. Revenue from these operations represented 38.5% of consolidated revenue from continuing operations in 2018 (2017 year – 39.7%).

Provincial governments fund a wide range of home health care services, and contract these services to providers such as ParaMed. In 2018, ParaMed received approximately 98% of its revenue from contracts tendered by locally administered provincial agencies (2017 year – 98%), with the remainder from private-pay clients. During 2018, ParaMed's 35 locations across Canada provided approximately 10.9 million hours of service, of which approximately 83% were provided in Ontario, 11% in British Columbia, 4% in Alberta, and the balance were provided in Manitoba, Nova Scotia and Quebec.

OTHER CANADIAN OPERATIONS

Extendicare's other Canadian operations are composed of its management and consulting services provided by Extendicare Assist, and group purchasing services provided by SGP Purchasing Partner Network. Revenue from these two divisions, collectively, represented 2.0% of consolidated revenue from continuing operations in 2018 (2017 year – 1.7%).

Management and Consulting Services

Through its Extendicare Assist division, Extendicare leverages its expertise in operating senior care centres in providing a wide range of management and consulting services to third-party owners of senior care and living centres. Extendicare Assist partners with not-for-profit and for-profit organizations, hospitals and municipalities that seek to improve their management practices, quality of care practices and operating efficiencies. Extendicare Assist provides a broad range of services aimed at meeting the needs of its partners, from operational consulting to overall facility management. The management service offering can include a broad spectrum of services, including: financial administration, record keeping, regulatory compliance and purchasing. In addition, Extendicare Assist provides consulting services to third parties for the development and redevelopment of long-term care centres, and secured such a contract in 2018 with a Toronto area hospital network.

As a skilled manager and operator of senior care centres for third parties, Extendicare Assist's managed portfolio consisted of 53 senior care centres with capacity for 6,497 residents as at December 31, 2018 (December 31, 2017 – 50 centres with capacity for 6,216 residents).

Group Purchasing Services

Through its SGP Purchasing Partner Network division, Extendicare offers cost-effective purchasing contracts to other senior care providers for food, capital equipment, furnishings, cleaning and nursing supplies, and office products. SGP negotiates long-term and high volume contracts with suppliers that provide members with preferred pricing, thereby providing a cost-effective way to secure quality national brand-name products, along with a range of innovative services. As at December 31, 2018, SGP provided services to third-party clients, serving approximately 51,100 seniors across Canada, and beginning in January 2019, brought on new clients increasing those served to over 56,800 (December 31, 2017 – 45,200 seniors).

U.S. REMAINING OPERATIONS – CAPTIVE INSURANCE COMPANY

Prior to the U.S. Sale Transaction, Extendicare self-insured certain risks related to general and professional liability of its disposed U.S. operations through the Captive. The obligation to settle any such claims relating to the period prior to the closing of the U.S. Sale Transaction, including claims incurred but yet to be reported, remains with Extendicare, which it intends to continue to fund through the Captive. The majority of the risks that Extendicare self-insured relating to the U.S. operations are long-term in nature, and accordingly, claim payments for any particular policy year can occur over a long period of time. In addition, through the Captive, the Company maintained third-party liability insurance on a "claims made" basis, as opposed to "occurrence based" coverage, meaning that some level of coverage may continue to be required. Any expense incurred or release of reserves for U.S. self-insured liabilities are presented as discontinued operations; while the costs to administer and manage the settlement of the remaining claims are reported as continuing operations within the U.S. segment.

As at December 31, 2018, the accrual for U.S. self-insured general and professional liabilities was $37.1 million (US$27.2 million) compared to $61.1 million (US$48.6 million) at the beginning of the year, and the investments held for U.S. self-insured liabilities totalled $67.9 million (US$49.8 million) compared to $86.3 million (US$68.6 million) at the beginning of the year, with the decline in each primarily reflecting the "run off" of these operations and release of reserves. Following the completion of an independent actuarial review, the Company released US$9.9 million of reserves for self-insured liabilities in 2018, bringing the total since the sale of the U.S. operations in 2015 to US$29.6 million. Following the release of these reserves, the Captive has transferred a total of US$28.5 million of its funds previously held for investment to the Company for general corporate use since the sale in 2015, of which US$7.5 million was transferred in October 2018. The loss provisions for our U.S. general and professional liability risks are based upon management's best available information, including independent actuarial estimates. The Captive is currently appropriately capitalized, but there can be no assurance that it will remain as such in the future should general and professional liability claims incurred prior to the closing of the U.S. Sale Transaction, including claims incurred but yet to be reported, increase significantly. For further information on our self-insured liabilities, refer to the discussion under the heading "Accrual for U.S. Self-insured Liabilities" found within the "Liquidity and Capital Resources" section of this MD&A.

KEY PERFORMANCE INDICATORS

In addition to those measures identified under the heading "Non-GAAP Measures", management uses certain key performance indicators in order to compare the financial performance of Extendicare's continuing operations between periods. In addition, we assess the operations on a same-store basis between the reported periods. Such performance indicators may not be comparable to similar indicators presented by other companies. Set forth below is an analysis of the key performance indicators and a discussion of significant trends when comparing Extendicare's financial results from continuing operations.

The following is a glossary of terms for some of our key performance indicators:

"Stabilized community" is the classification by the Company of a retirement community that has achieved its expected stabilized occupancy level, which varies from project to project; such operations in respect of this report specifically refer to five retirement communities (Empire Crossing, Harvest, Lynde Creek Manor, Riverbend Crossing and Stonebridge Crossing);

"Non same-store" or "NSS", generally refers to those centres or business that were not continuously operated by us since the beginning of the previous fiscal year or have been classified as held for sale, such operations in respect of this report specifically refer to one retirement community that opened during 2017 (Douglas Crossing), Lynde Creek that was acquired in April 2018, and two retirement communities that were under development (Bolton and Barrie);

"Occupancy" is measured as the percentage of the number of earned resident days (or the number of occupied suites in the case of a retirement community) relative to the total available resident days. Total available resident days is the number of beds (or suites in the case of a retirement community) available for occupancy multiplied by the number of days in the period; and

"Same-store" or "SS" generally refers to those centres or businesses that were continuously operated by us since the beginning of the previous fiscal year, and which are not classified as held for sale; such operations in respect of this report specifically refer to all continuing operations excluding the four retirement communities classified as NSS above.

Long-term Care

The following table provides the average occupancy levels of our LTC operations for the past eight quarters.

Long-term Care Centres					**2018**					**2017**
Average Occupancy *(%)*	**Q1**	**Q2**	**Q3**	**Q4**	**Year**	**Q1**	**Q2**	**Q3**	**Q4**	**Year**
Total LTC	**96.4%**	**97.2%**	**97.8%**	**97.6%**	**97.3%**	97.2%	97.6%	98.2%	97.7%	97.7%
Ontario LTC										
Total operations	**97.1%**	**97.7%**	**98.3%**	**98.2%**	**97.8%**	97.6%	98.2%	98.5%	98.2%	98.1%
Preferred Accommodation (1)										
"New" centres – private	**96.3%**	**96.7%**	**97.6%**	**96.6%**	**96.8%**	97.1%	98.0%	98.3%	98.1%	97.9%
"C" centres – private	**97.4%**	**97.3%**	**97.8%**	**97.6%**	**97.5%**	98.5%	98.3%	97.8%	98.8%	98.4%
"C" centres – semi-private	**65.2%**	**65.7%**	**66.5%**	**66.1%**	**65.9%**	64.5%	65.7%	67.3%	66.5%	66.1%

(1) Average occupancy reported for the available private and semi-private rooms reflects the percentage of residents occupying those beds and paying the respective premium rates.

The average occupancy at our LTC centres was 97.6% this quarter compared to 97.7% in the 2017 fourth quarter, and to 97.8% in the 2018 third quarter. For the year, occupancy averaged 97.3% compared to 97.7% in 2017. In terms of the quarterly trends throughout the year, slightly lower occupancy levels are to be expected during the winter months as a result of outbreaks, which can lead to a temporary freeze on admissions. In addition, occupancy levels in the 2018 first quarter were impacted by the fill-up of a 24-bed addition to one of our LTC centres that opened in February, yet achieved stabilized occupancy levels in April 2018.

In Ontario, overall government funding is occupancy-based, but once the average occupancy level of 97% or higher for the calendar year is achieved, operators receive government funding based on 100% occupancy. Extendicare's LTC centres in Ontario achieved an overall average occupancy of 97.8%, with all but two of the centres achieving the 97% occupancy threshold.

In addition, Extendicare's Ontario LTC centres receive premiums for preferred accommodation. The average occupancy of the private beds in our "New" centres was 96.8% this year compared to 97.9% in 2017. The average occupancy of the private beds at our Class C centres was 97.5% this year compared to 98.4% in 2017.

Retirement Living

During 2018, we had nine retirement communities in operation, two of which were classified as non same-store. Five of the retirement communities were classified as stabilized, including Lynde Creek Manor, which had achieved stabilized occupancy at the time it was acquired earlier this year, and four that were acquired in 2015 (Empire, Harvest, Riverbend, and Stonebridge). The remaining four communities were classified as lease-up communities during 2018.

AS AT OCCUPANCY

The following table provides the combined occupancy of our stabilized and lease-up retirement communities at the end of each quarter in 2018 and 2017.

Retirement Communities				**2018**				**2017**
As at Occupancy *(%)*	**Mar. 31**	**Jun. 30**	**Sept. 30**	**Dec. 31**	**Mar. 31**	**Jun. 30**	**Sept. 30**	**Dec. 31**
Stabilized communities (Empire/Harvest/ Lynde Creek/Riverbend/Stonebridge)	**90.5%**	**93.2%**	**94.8%**	**95.0%**	83.8%	83.2%	89.6%	93.4%
Lease-up communities	**70.6%**	**76.4%**	**82.4%**	**81.0%**	38.6%	43.9%	55.7%	63.0%

The average occupancy of the stabilized communities improved to 95.0% on December 31, 2018, from 93.4% on December 31, 2017. In terms of the quarterly trends throughout the year, lower occupancy levels can be expected during the winter months as a result of higher attrition, as was experienced in the first half of 2018 from the 2017 year-end levels. The average occupancy of the four lease-up communities grew to 81.0%% at year end from 63.0% on December 31, 2017, with the slight decline from September 30, 2018 due to the completion of the 45-suite addition at Douglas Crossing.

AVERAGE OCCUPANCY

The following table provides the average occupancy of the retirement communities in total and for each of the stabilized and lease-up groupings for the past eight quarters. The average occupancy of the stabilized communities improved to 94.8% this quarter from 93.4% in each of the 2017 fourth and 2018 third quarters, and averaged 93.3% for the year.

					2018					**2017**
Retirement Communities	**Q1**	**Q2**	**Q3**	**Q4**	**Year**	**Q1**	**Q2**	**Q3**	**Q4**	**Year**
Average Occupancy *(%)* – total	**80.4%**	**84.4%**	**87.9%**	**88.4%**	**85.5%**	63.4%	66.6%	71.9%	75.9%	69.7%
Stabilized communities	**92.6%**	**92.1%**	**93.4%**	**94.8%**	**93.3%**	82.7%	83.1%	86.8%	93.4%	86.5%
Lease-up communities	**67.6%**	**74.5%**	**80.6%**	**80.6%**	**75.9%**	34.0%	41.7%	49.4%	55.5%	46.0%

Home Health Care

The following table provides the service volumes of our home health care operations for the past eight quarters.

Home Health Care					**2018**					**2017**
Service Volumes	**Q1**	**Q2**	**Q3**	**Q4**	**Year**	**Q1**	**Q2**	**Q3**	**Q4**	**Year**
Hours of service (000's)	**2,705.0**	**2,734.8**	**2,708.6**	**2,750.0**	**10,898.4**	2,815.7	2,859.1	2,833.6	2,818.4	11,326.8
Hours per day	**30,055**	**30,053**	**29,441**	**29,891**	**29,859**	31,285	31,418	30,800	30,634	31,032

Revenue from provincial programs represented approximately 98% of Extendicare's home health care revenue in 2018 (2017 year – 98%). ParaMed's average daily hours of service increased this quarter from the 2018 third quarter by 1.5% to 29,891, the first quarter-over-quarter sequential increase in the past six quarters. For the year, ParaMed's average daily hours of service were 29,859, or 3.8% below 2017, largely due to challenges with the Ontario operations. Competition for personal support workers (PSWs), and to a lesser extent nurses, intensified in 2018. A labour shortage in many areas across the country has adversely impacted our ability to continue to meet the growing demand in services. We continue efforts to build capacity to address these challenges and to take advantage of the significant organic growth opportunity that exists across Canada. Retention efforts have reduced turnover rates by half in the last half of 2018 compared to the beginning of the year. If sustained, we believe this will improve capacity in future quarters.

Also, in the summer of 2018 we successfully launched new enterprise software to replace three legacy systems, which is expected to enhance ParaMed's operational capabilities enabling it to respond to the growing market demand. As of the end of February 2019, we have completed the roll out of the new software to branch offices representing approximately 53% of our business volumes and anticipate completing the balance by the end of 2019. During the implementation, we will be shouldering the cost of the legacy systems and investing in significant one-time training and implementation resources. Costs incurred in 2018 in respect of the three legacy systems to be decommissioned and temporary staff for training, data migration, and implementation of the new software impacted EBITDA by approximately $3.3 million ($2.3 million at the NOI level), compared to $1.6 million at the NOI and EBITDA levels in 2017. Management anticipates these costs will escalate in 2019 to approximately $5.0 million ($2.8 million at the NOI level), after which the implementation will be complete. As we start to leverage the new system throughout 2019, we expect productivity and service volumes to improve.

For further information on the home health care operations, refer to the discussion under the heading "Update of Regulatory and Funding Changes Affecting Results – Ontario Home Health Care Legislation and Funding".

2018 SELECTED ANNUAL INFORMATION

The following is a summary of selected annual financial information for each of the past three years.

(thousands of dollars unless otherwise noted)	**2018**	**2017**	**2016**
Financial Results			
Revenue	**1,120,007**	1,097,331	1,060,758
Earnings before depreciation, amortization and other expense (Adjusted EBITDA)	**94,238**	97,597	92,935
Earnings from continuing operations	**8,084**	31,712	31,417
per basic share *($)*	**0.09**	0.36	0.36
Gain (loss) on sale of U.S. operations, net of taxes	**–**	–	(8,458)
Earnings (loss) from discontinued operations	**23,654**	(29,580)	12,493
Net earnings	**31,738**	2,132	35,452
per basic share *($)*	**0.36**	0.02	0.40
per diluted share *($)*	**0.36**	0.02	0.40
AFFO (continuing operations)	**57,751**	58,495	66,722
per basic share *($)*	**0.653**	0.659	0.755
AFFO	**57,751**	58,495	65,056
per basic share *($)*	**0.653**	0.659	0.736
Cash dividends declared	**42,351**	42,583	42,422
per share *($)*	**0.480**	0.480	0.480
Financial Position *(at year end)*			
Total assets	**896,324**	934,281	988,617
Total non-current liabilities	**543,359**	588,804	605,353
Long-term debt	**454,344**	476,404	448,742
Long-term debt, including current portion	**528,970**	536,068	503,568

Financial Results – The selected information provided for each of the years under the heading "Financial Results", reflects the classification of disposed U.S. operations as discontinued. The U.S. senior care operations were sold in 2015 and the U.S. information technology hosting and professional services business was sold in 2016, resulting in a loss, net of tax of $8.4 million recorded in 2016. The financial results for 2017 reflect an improvement in earnings from continuing operations over 2016, resulting from growth in home health care volumes, continued lease up of retirement communities, and an increase in clients served by the Extendicare Assist and SGP divisions, partially offset by higher costs of resident care in our LTC operations and a reduction in interest revenue in connection with deferred consideration from the disposed U.S. operations. A comparison of the 2018 financial results to 2017 is provided under the heading "2018 Financial Review".

Financial Position – Since the end of 2016, total assets and non-current liabilities have declined, largely due to the "run off" of the U.S. self-insured liabilities and related investments held by the Captive and an impairment charge recorded in 2018. Total assets declined by $54.3 million and $38.0 million in 2017 and 2018, respectively. The investments held by the Captive declined by $49.8 million in 2017 and by $18.4 million in 2018. In addition, the Company recorded an impairment charge of $16.2 million in 2018 in respect of certain of its retirement and LTC centres (refer to the discussion under the heading "Other Significant Developments – Impairment Charge").

In 2017, total non-current liabilities declined by $16.5 million, largely due to the decline in the accrual for U.S. self-insured liabilities by $33.7 million (US$22.0 million), partially offset by an increase in long-term debt. Total long-term debt, including current portion, increased by $32.5 million, reflecting the issuance of debt in connection with the acquisition and development of our retirement communities.

In 2018, total non-current liabilities declined by $45.4 million, largely due to the decline in the accrual for U.S. self-insured liabilities of $24.0 million (US$21.4 million) and a decline in long-term debt. Total long-term debt, including current portion, declined by $7.1 million primarily due to the convertible debt refinancing completed in 2018, and resulting bifurcation of a component to equity.

A comparison between the 2018 and 2017 financial results is provided in the discussion under the headings "2018 Financial Review" and "Liquidity and Capital Resources".

2018 SELECTED QUARTERLY INFORMATION

The following is a summary of selected quarterly financial information for the past eight quarters.

				2018				2017
(thousands of dollars unless otherwise noted)	**Q4**	**Q3**	**Q2**	**Q1**	**Q4**	**Q3**	**Q2**	**Q1**
Revenue	**288,793**	**280,302**	**279,488**	**271,424**	281,398	273,230	273,845	268,858
Net operating income	**32,863**	**35,492**	**36,307**	**29,322**	35,622	34,729	33,867	31,604
NOI margin	***11.4%***	***12.7%***	***13.0%***	***10.8%***	*12.7%*	*12.7%*	*12.4%*	*11.8%*
Adjusted EBITDA	**22,538**	**24,393**	**27,330**	**19,977**	27,555	24,025	24,588	21,429
Adjusted EBITDA margin	***7.8%***	***8.7%***	***9.8%***	***7.4%***	*9.8%*	*8.8%*	*9.0%*	*8.0%*
Earnings (loss) from continuing operations	**(9,055)**	**7,598**	**5,975**	**3,566**	10,301	6,545	9,919	4,947
Earnings (loss) from discontinued operations	**15,562**	**975**	**5,852**	**1,265**	3,333	–	(32,913)	–
Net earnings (loss)	**6,507**	**8,573**	**11,827**	**4,831**	13,634	6,545	(22,994)	4,947
AFFO (continuing operations)	**11,955**	**13,379**	**17,133**	**14,669**	15,713	15,646	14,448	12,688
per basic share *($)*	**0.135**	**0.151**	**0.194**	**0.166**	0.178	0.176	0.162	0.143
AFFO	**11,955**	**13,379**	**17,133**	**14,669**	15,713	15,646	14,448	12,688
per basic share *($)*	**0.135**	**0.151**	**0.194**	**0.166**	0.178	0.176	0.162	0.143
Maintenance Capex								
Continuing operations	**4,817**	**3,639**	**3,783**	**1,051**	3,271	2,777	1,858	907
Discontinued operations	**–**	**–**	**–**	**–**	–	–	–	–
Cash dividends declared	**10,612**	**10,591**	**10,570**	**10,578**	10,623	10,642	10,666	10,652
per share *($)*	**0.120**	**0.120**	**0.120**	**0.120**	0.120	0.120	0.120	0.120
Weighted Average Number of Shares								
Basic	**88,612**	**88,412**	**88,208**	**88,379**	88,633	88,844	88,938	88,807
Diluted	**98,962**	**98,788**	**98,595**	**99,688**	99,916	100,123	100,244	100,086

The following is a reconciliation of "earnings (loss) from continuing operations before income taxes" to Adjusted EBITDA and "net operating income".

				2018				2017
(thousands of dollars)	**Q4**	**Q3**	**Q2**	**Q1**	**Q4**	**Q3**	**Q2**	**Q1**
Earnings (loss) from continuing operations before income taxes	**(12,327)**	**10,135**	**9,131**	**5,380**	13,212	9,874	12,763	6,715
Add (Deduct):								
Depreciation and amortization	**10,184**	**9,014**	**8,235**	**7,837**	8,170	7,766	7,911	7,532
Net finance costs	**8,039**	**5,244**	**6,591**	**6,580**	6,173	6,385	3,914	7,182
Other expense	**16,642**	**–**	**3,373**	**180**	–	–	–	–
Adjusted EBITDA	**22,538**	**24,393**	**27,330**	**19,977**	27,555	24,025	24,588	21,429
Add (Deduct):								
Administrative costs	**8,601**	**9,376**	**7,309**	**7,718**	6,372	9,058	7,524	8,513
Lease costs	**1,724**	**1,723**	**1,668**	**1,627**	1,695	1,646	1,755	1,662
Net operating income	**32,863**	**35,492**	**36,307**	**29,322**	35,622	34,729	33,867	31,604

There are a number of factors affecting the trend of our quarterly results from continuing operations. With respect to our core operations, while year-over-year quarterly comparisons will generally remain comparable, sequential quarters can vary materially for seasonal and other trends. The significant factors that impact the results from period to period are as follows:

- Ontario long-term care funding tied to flow-through funding envelopes requires revenue be deferred until it is matched with the related costs for resident care in the periods in which the costs are incurred, resulting in a fluctuation in revenue and operating expenses by quarter, and they are generally at their lowest in the first quarter and at their highest in the fourth quarter;
- Ontario long-term care providers generally receive annual flow-through funding increases and case mix index adjustments effective April 1st and accommodation funding increases effective July 1st, and Alberta long-term care providers generally receive annual inflationary rate increases and acuity-based funding adjustments on April 1st, and accommodation funding increases effective July 1st;
- maintenance capex spending, which impacts our AFFO, fluctuates on a quarterly basis with the timing of projects and seasonality, and is generally at its lowest in the first quarter and its highest in the fourth quarter; and
- utility costs are generally at their highest in the first quarter and their lowest in the second and third quarters, and can vary by as much as $1.5 million to $1.6 million quarterly.

In addition, we report as separate line items, “other expense”, “fair value adjustments”, and “loss (gain) on foreign exchange and investments”, as these are transitional in nature and would otherwise distort historical trends. Those items impacting our results are as follows:

- transaction and integration costs in connection with acquisitions, asset impairment charges, gains or losses on disposals, and other costs considered transitional in nature are reported as “other expense”; as a result of these items, the results from continuing operations included “other expense” of $20.2 million in 2018 ($0.2 million in the first quarter, $3.4 million in the second quarter, and $16.6 million in the fourth quarter), compared to no such charges in 2017);
- interest rate swaps are measured at fair value through profit or loss each period, along with realized gains or losses, as part of “fair value adjustments”; as a result, a net loss of $1.0 million was recorded in 2018 (gain of $0.3 million, nil, gain of $0.5 million, and loss of $1.8 million in each of the quarters, respectively), compared to a net gain of $2.5 million in 2017 (loss of $0.1 million, gain of $1.1 million, gain of $1.2 million, and a gain of $0.3 million, in each of the quarters, respectively); and
- foreign currency exchange rate fluctuations between the U.S. and Canadian dollars impact translation of our remaining U.S. net assets in connection with net proceeds and deferred consideration received in respect of the disposed U.S. operations and repatriation of funds from our Captive, in addition, our investments held for U.S. self-insured liabilities are measured at fair value through profit and loss and reflected as part of “loss (gain) on foreign exchange and investments” (in 2017 unrealized changes in fair value were reflected in other comprehensive income); as a result of these activities, a net gain of $1.2 million was recorded in 2018 (loss of $0.2 million, gain of $0.4 million, gain of $0.9 million, and gain of $0.1 million, in each of the quarters, respectively), compared to a net gain of $0.8 million in 2017 (loss of $0.4 million , gain of $1.5 million, loss of $0.7 million, and a gain of $0.4 million, in each of the quarters, respectively).

Further details on the above can be found under the sections “Significant 2018 Events and Developments”, “Key Performance Indicators”, “Other Significant Developments” and “Update of Regulatory and Funding Changes Affecting Results”.

2018 FOURTH QUARTER FINANCIAL REVIEW

The following provides a breakdown of our consolidated statement of earnings between our Canadian and remaining U.S. operations.

	Three months ended December 31						
			2018			2017	Total
(thousands of dollars)	Canada	U.S.	Total	Canada	U.S.	Total	Change
Revenue	**288,516**	**277**	**288,793**	279,085	2,313	281,398	7,395
Operating expenses	**255,930**	**–**	**255,930**	245,776	–	245,776	10,154
Net operating income	**32,586**	**277**	**32,863**	33,309	2,313	35,622	(2,759)
Administrative costs	**8,262**	**339**	**8,601**	6,462	(90)	6,372	2,229
Lease costs	**1,724**	**–**	**1,724**	1,695	–	1,695	29
Adjusted EBITDA	**22,600**	**(62)**	**22,538**	25,152	2,403	27,555	(5,017)
Depreciation and amortization	**10,184**	**–**	**10,184**	8,170	–	8,170	2,014
Other expense	**16,642**	**–**	**16,642**	–	–	–	16,642
Earnings (loss) before net finance costs and income taxes	**(4,226)**	**(62)**	**(4,288)**	16,982	2,403	19,385	(23,673)
Interest expense (net of capitalized interest)	**6,685**	**–**	**6,685**	7,342	–	7,342	(657)
Interest revenue	**(926)**	**–**	**(926)**	(1,091)	–	(1,091)	165
Accretion	**299**	**336**	**635**	351	265	616	19
Fair value adjustments	**1,792**	**–**	**1,792**	(271)	–	(271)	2,063
Loss (gain) on foreign exchange and investments	**(503)**	**356**	**(147)**	(179)	(244)	(423)	276
Net finance costs (income)	**7,347**	**692**	**8,039**	6,152	21	6,173	1,866
Earnings (loss) from continuing operations before income taxes	**(11,573)**	**(754)**	**(12,327)**	10,830	2,382	13,212	(25,539)
Income tax expense (recovery)							
Current	**2,001**	**–**	**2,001**	1,679	–	1,679	322
Deferred	**(5,273)**	**–**	**(5,273)**	1,232	–	1,232	(6,505)
Total income tax expense	**(3,272)**	**–**	**(3,272)**	2,911	–	2,911	(6,183)
Earnings (loss) from continuing operations	**(8,301)**	**(754)**	**(9,055)**	7,919	2,382	10,301	(19,356)
Earnings from discontinued operations	**–**	**15,562**	**15,562**	–	3,333	3,333	12,229
Net earnings (loss)	**(8,301)**	**14,808**	**6,507**	7,919	5,715	13,634	(7,127)
Earnings (loss) from continuing operations	**(8,301)**	**(754)**	**(9,055)**	7,919	2,382	10,301	(19,356)
Add (Deduct) (1)**:**							
Fair value adjustments	**1,315**	**–**	**1,315**	(199)	–	(199)	1,514
Loss (gain) on foreign exchange and investments	**(600)**	**356**	**(244)**	(206)	(244)	(450)	206
Other expense	**12,153**	**–**	**12,153**	–	–	–	12,153
Earnings (loss) from continuing operations before separately reported items, net of taxes	**4,567**	**(398)**	**4,169**	7,514	2,138	9,652	(5,483)

(1) The separately reported items being added to or deducted from earnings (loss) from continuing operations are net of income taxes, and are non-GAAP measures. Refer to the discussion of non-GAAP measures.

The following provides a reconciliation of “earnings from continuing operations before income taxes” to “Adjusted EBITDA” and “net operating income”.

	Three months ended December 31						
			2018			2017	Total
(thousands of dollars)	Canada	U.S.	Total	Canada	U.S.	Total	Change
Earnings (loss) from continuing operations before income taxes	**(11,573)**	**(754)**	**(12,327)**	10,830	2,382	13,212	(25,539)
Add (Deduct):							
Depreciation and amortization	**10,184**	**–**	**10,184**	8,170	–	8,170	2,014
Net finance costs (income)	**7,347**	**692**	**8,039**	6,152	21	6,173	1,866
Other expense	**16,642**	**–**	**16,642**	–	–	–	16,642
Adjusted EBITDA	**22,600**	**(62)**	**22,538**	25,152	2,403	27,555	(5,017)
Add (Deduct):							
Administrative costs	**8,262**	**339**	**8,601**	6,462	(90)	6,372	2,229
Lease costs	**1,724**	**–**	**1,724**	1,695	–	1,695	29
Net operating income	**32,586**	**277**	**32,863**	33,309	2,313	35,622	(2,759)

The following is an analysis of the consolidated results from operations for the 2018 fourth quarter in comparison to the 2017 fourth quarter. Refer to the discussion that follows under the heading “Summary of Results of Operations by Segment” for an analysis of the revenue and net operating income by operating segment, including the components of non same-store revenue and net operating income.

Consolidated Revenue

Consolidated revenue from continuing operations grew by $7.4 million or 2.6% to $288.8 million in the 2018 fourth quarter, driven primarily by LTC funding enhancements, expansion of the retirement living operations, home health care funding increases, including $1.2 million accrued to support legislated amendments resulting from the *Fair Workplaces, Better Jobs Act, 2017* (Ontario), or Bill 148, that came into effect on January 1, 2018, and growth in management and group purchasing services, partially offset by a decline in home health care volumes, and lower investment income from the Captive. For further information on Bill 148, refer to the discussion under the heading “Update of Regulatory and Funding Changes Affecting Results – Ontario Home Health Care Legislation and Funding”.

Consolidated Operating Expenses

Consolidated operating expenses from continuing operations increased by $10.1 million or 4.1% to $255.9 million in the 2018 fourth quarter, driven by increased costs of resident care, expansion of the retirement living operations, and higher labour costs, including the impact on the home health care operations of Bill 148, partially offset by the impact of lower home health care volumes delivered. Total labour costs increased by $7.6 million over the 2017 fourth quarter, and represented 85.1% and 85.5% of operating expenses in the fourth quarters of 2018 and 2017, respectively, and as a percentage of revenue were 75.4% and 74.7%, respectively.

Consolidated Net Operating Income

Consolidated net operating income from continuing operations declined by $2.7 million or 7.7% to $32.9 million in the 2018 fourth quarter, and represented 11.4% of revenue compared to 12.7% in the same 2017 period. Net operating income from the Canadian operations declined by $0.7 million and was favourably impacted by home health care funding enhancements, and growth of our retirement living, management and group purchasing operations, offset by lower home health care volumes and higher labour related costs, including the impact of Bill 148. Net operating income from our U.S. operations reflects investment income from the Captive, which was nominal this quarter compared to the same 2017 period.

Administrative and Lease Costs

Administrative and lease costs from continuing operations increased by $2.3 million in the 2018 fourth quarter, and were impacted by increased costs of approximately $0.4 million to support the implementation of new enterprise software, a non-recurring reinsurance premium refund of $0.5 million received by the Captive in 2017, and other higher compensation costs and professional fees.

Consolidated Adjusted EBITDA

Consolidated Adjusted EBITDA from continuing operations declined by $5.0 million to $22.5 million this quarter, and represented 7.8% of revenue compared to 9.8% in the same 2017 period, of which $2.5 million was from the Canadian operations, reflecting the $0.7 million decline in net operating income and increase in administrative and lease costs.

Other Expense

Other expense of $16.6 million ($12.2 million after tax) recorded this period related primarily to an impairment charge in respect of certain of the Company’s retirement and LTC centres (refer to discussion under the heading “Other Significant Developments – Impairment Charge”).

Net Finance Costs

Net finance costs increased by $1.8 million to $8.0 million this quarter, primarily due to a net change in loss (gain) on foreign exchange and the Captive’s investments and interest rate swap fair value adjustments aggregating $2.3 million, partially offset by slightly lower net interest costs associated with a lower weighted average interest rate and decline in net debt levels.

Income Taxes

The Company recognized a consolidated income tax recovery this quarter of $3.3 million, representing an effective tax rate of 26.5%, compared to a provision of $2.9 million and an effective tax rate of 22.0% in the 2017 fourth quarter. The effective tax rate of the Canadian operations was 28.3% this quarter compared to 26.9% in the 2017 fourth quarter, and was impacted by, among other things, fair value adjustments, gains and losses on foreign exchange and investments, and other expense items that have been separately reported. The effective tax rate of the Canadian operations excluding the impact of separately reported items was 28.2% compared to 27.6%.

Discontinued Operations

Earnings from discontinued operations relate to the former U.S. operations. The after-tax earnings of $15.5 million in the 2018 fourth quarter included $6.0 million related to the Captive's reserves (release and favourable impact of discount rate adjustments), a $3.6 million decrease in indemnification provisions and other items, and a net tax recovery of $5.9 million. The after-tax earnings of $3.3 million in the 2017 fourth quarter related to a release of the Captive's reserves of $3.1 million and a net reduction in indemnification provisions and other items of $0.3 million, partially offset by a tax provision of $0.1 million.

Summary of Results of Operations by Segment

The following provides an analysis of the operating performance of each of our operating segments. Refer to the table at the end of the discussion for a summary of the segmented "revenue", "operating expenses" and "net operating income".

LONG-TERM CARE OPERATIONS

Net operating income from our long-term care operations was $18.8 million this quarter compared to $18.3 million in the 2017 fourth quarter, representing 11.4% of revenue compared to 11.6%, respectively. Revenue this quarter grew by $6.0 million, or 3.8%, of which approximately $2.1 million related to the Ontario flow-through funding envelopes, and was therefore directly offset by increased costs of resident care, and the balance was from other funding enhancements. Operating expenses increased by $5.5 million, or 3.9%, and included the impact of higher labour, maintenance, supply, and food costs. Total labour costs increased by $3.3 million and represented 81.2% of operating expenses this quarter compared to 82.0% in the same 2017 period.

RETIREMENT LIVING OPERATIONS

Net operating income from our retirement living operations improved by $1.3 million this quarter, with growth from same-store operations of $0.4 million, reflecting an increase in average occupancy to 90.7% from 81.0% in the 2017 fourth quarter. Non same-store net operating income improved by $0.9 million this period, reflecting the contribution from the Lynde Creek Acquisition in April 2018 and the opening of Douglas Crossing in October 2017, partially offset by pre-opening costs associated with two communities under construction.

HOME HEALTH CARE OPERATIONS

Net operating income from our home health care operations declined by $3.1 million or 27.9% to $7.9 million this quarter, and represented 7.3% of revenue compared to 10.1% in the 2017 fourth quarter. Operations were impacted this quarter by a 2.4% decline in volumes, and higher labour related costs, partially offset by government contract funding increases. The reduction in home health care volumes was in large part due to an industry-wide capacity shortage of PSWs, and to a lesser extent nurses, which has adversely impacted our ability to continue to meet the growing demand, and in some locations has given rise to increased overtime and use of subcontracted staff. Initiatives are under way to improve our ability to attract and retain care staff. As well, in addition to temporary costs associated with the implementation of new enterprise software, the number of back office administrative staff increased as we manage through the implementation process and associated re-engineering of workflows. Despite the reduction in business volumes as compared to the same 2017 period, total labour costs increased this quarter by $3.6 million and represented 92.8% of operating expenses compared to 91.9% in the same 2017 period. While volumes this quarter were below that of the same 2017 period, this was the first time in six quarters that we experienced a quarter-over-quarter sequential increase in business volumes. Refer to the discussions under the heading "Key Performance Indicators – Home Health Care" and "Update of Regulatory and Funding Changes Affecting Results – Ontario Home Health Care Legislation and Funding".

OTHER CANADIAN OPERATIONS

Net operating income from our management and group purchasing operations increased by $0.6 million this quarter, and represented 61.7% of revenue compared to 57.8% in the 2017 fourth quarter, due to growth in clients served.

U.S. OPERATIONS

The decline in net operating income from the U.S. operations reflected lower investment income from the Captive, and the impact of a non-recurring reinsurance premium refund received in the 2017 fourth quarter.

The following summarizes our segmented "revenue", "operating expenses" and "net operating income".

Three months ended December 31 *(thousands of dollars)*	**Long-term Care**	**Retirement Living**	**Home Health Care**	**Other Canadian Operations**	**Corporate Canada**	**Total Canada**	**Total U.S.**	**Total**
2018 – Same-store								
Revenue	**164,656**	**6,433**	**109,012**	**5,808**	**1**	**285,910**	**277**	**286,187**
Operating expenses	**145,849**	**4,788**	**101,097**	**2,223**	**–**	**253,957**	**–**	**253,957**
Net operating income	**18,807**	**1,645**	**7,915**	**3,585**	**1**	**31,953**	**277**	**32,230**
NOI margin %	***11.4%***	***25.6%***	***7.3%***	***61.7%***	***100.0%***	***11.2%***	***100.0%***	***11.3%***
2018 – Non Same-store								
Revenue	**–**	**2,606**	**–**	**–**	**–**	**2,606**	**–**	**2,606**
Operating expenses	**–**	**1,973**	**–**	**–**	**–**	**1,973**	**–**	**1,973**
Net operating income	**–**	**633**	**–**	**–**	**–**	**633**	**–**	**633**
2018 – Total								
Revenue	**164,656**	**9,039**	**109,012**	**5,808**	**1**	**288,516**	**277**	**288,793**
Operating expenses	**145,849**	**6,761**	**101,097**	**2,223**	**–**	**255,930**	**–**	**255,930**
Net operating income	**18,807**	**2,278**	**7,915**	**3,585**	**1**	**32,586**	**277**	**32,863**
NOI margin %	***11.4%***	***25.2%***	***7.3%***	***61.7%***	***100.0%***	***11.3%***	***100.0%***	***11.4%***
2017 – Same-store								
Revenue	158,694	5,746	109,141	5,149	3	278,733	2,313	281,046
Operating expenses	140,349	4,492	98,160	2,175	–	245,176	–	245,176
Net operating income	18,345	1,254	10,981	2,974	3	33,557	2,313	35,870
NOI margin %	*11.6%*	*21.8%*	*10.1%*	*57.8%*	*100.0%*	*12.0%*	*100.0%*	*12.8%*
2017 – Non Same-store								
Revenue	–	352	–	–	–	352	–	352
Operating expenses	–	600	–	–	–	600	–	600
Net operating loss	–	(248)	–	–	–	(248)	–	(248)
2017 – Total								
Revenue	158,694	6,098	109,141	5,149	3	279,085	2,313	281,398
Operating expenses	140,349	5,092	98,160	2,175	–	245,776	–	245,776
Net operating income	18,345	1,006	10,981	2,974	3	33,309	2,313	35,622
NOI margin %	*11.6%*	*16.5%*	*10.1%*	*57.8%*	*100.0%*	*11.9%*	*100.0%*	*12.7%*
Change in Total								
Revenue	5,962	2,941	(129)	659	(2)	9,431	(2,036)	7,395
Operating expenses	5,500	1,669	2,937	48	–	10,154	–	10,154
Net operating income	462	1,272	(3,066)	611	(2)	(723)	(2,036)	(2,759)

2018 FINANCIAL REVIEW

The following provides a breakdown of our consolidated statement of earnings between our Canadian and remaining U.S. operations.

							Years ended December 31
			2018			2017	Total
(thousands of dollars)	**Canada**	**U.S.**	**Total**	**Canada**	**U.S.**	**Total**	**Change**
Revenue	**1,119,602**	**405**	**1,120,007**	1,092,082	5,249	1,097,331	22,676
Operating expenses	**986,023**	**–**	**986,023**	961,509	–	961,509	24,514
Net operating income	**133,579**	**405**	**133,984**	130,573	5,249	135,822	(1,838)
Administrative costs	**31,828**	**1,176**	**33,004**	30,333	1,134	31,467	1,537
Lease costs	**6,742**	**–**	**6,742**	6,758	–	6,758	(16)
Adjusted EBITDA	**95,009**	**(771)**	**94,238**	93,482	4,115	97,597	(3,359)
Depreciation and amortization	**35,270**	**–**	**35,270**	31,379	–	31,379	3,891
Other expense	**20,195**	**–**	**20,195**	–	–	–	20,195
Earnings (loss) before net finance costs and income taxes	**39,544**	**(771)**	**38,773**	62,103	4,115	66,218	(27,445)
Interest expense (net of capitalized interest)	**27,584**	**–**	**27,584**	28,082	–	28,082	(498)
Interest revenue	**(3,761)**	**–**	**(3,761)**	(3,695)	(207)	(3,902)	141
Accretion	**1,250**	**1,628**	**2,878**	1,529	1,283	2,812	66
Fair value adjustments	**956**	**–**	**956**	(2,474)	–	(2,474)	3,430
Loss (gain) on foreign exchange and investments	**(1,105)**	**(98)**	**(1,203)**	666	(1,530)	(864)	(339)
Net finance costs (income)	**24,924**	**1,530**	**26,454**	24,108	(454)	23,654	2,800
Earnings (loss) from continuing operations before income taxes	**14,620**	**(2,301)**	**12,319**	37,995	4,569	42,564	(30,245)
Income tax expense (recovery)							
Current	**8,129**	**–**	**8,129**	10,149	–	10,149	(2,020)
Deferred	**(3,894)**	**–**	**(3,894)**	603	100	703	(4,597)
Total income tax expense	**4,235**	**–**	**4,235**	10,752	100	10,852	(6,617)
Earnings (loss) from continuing operations	**10,385**	**(2,301)**	**8,084**	27,243	4,469	31,712	(23,628)
Earnings (loss) from discontinued operations	**–**	**23,654**	**23,654**	–	(29,580)	(29,580)	53,234
Net earnings (loss)	**10,385**	**21,353**	**31,738**	27,243	(25,111)	2,132	29,606
Earnings (loss) from continuing operations	**10,385**	**(2,301)**	**8,084**	27,243	4,469	31,712	(23,628)
Add (Deduct) (1)**:**							
Fair value adjustments	**702**	**–**	**702**	(1,813)	–	(1,813)	2,515
Loss (gain) on foreign exchange and investments	**(1,225)**	**(98)**	**(1,323)**	805	(1,512)	(707)	(616)
Other expense	**15,165**	**–**	**15,165**	–	–	–	15,165
Earnings (loss) from continuing operations before separately reported items, net of taxes	**25,027**	**(2,399)**	**22,628**	26,235	2,957	29,192	(6,564)

(1) The separately reported items being added to or deducted from earnings (loss) from continuing operations are net of income taxes, and are non-GAAP measures. Refer to the discussion of non-GAAP measures.

The following provides a reconciliation of "earnings from continuing operations before income taxes" to "Adjusted EBITDA" and "net operating income".

							Years ended December 31
			2018			2017	Total
(thousands of dollars)	**Canada**	**U.S.**	**Total**	**Canada**	**U.S.**	**Total**	**Change**
Earnings (loss) from continuing operations before income taxes	**14,620**	**(2,301)**	**12,319**	37,995	4,569	42,564	(30,245)
Add (Deduct):							
Depreciation and amortization	**35,270**	**–**	**35,270**	31,379	–	31,379	3,891
Net finance costs (income)	**24,924**	**1,530**	**26,454**	24,108	(454)	23,654	2,800
Other expense	**20,195**	**–**	**20,195**	–	–	–	20,195
Adjusted EBITDA	**95,009**	**(771)**	**94,238**	93,482	4,115	97,597	(3,359)
Add (Deduct):							
Administrative costs	**31,828**	**1,176**	**33,004**	30,333	1,134	31,467	1,537
Lease costs	**6,742**	**–**	**6,742**	6,758	–	6,758	(16)
Net operating income	**133,579**	**405**	**133,984**	130,573	5,249	135,822	(1,838)

The following is an analysis of the consolidated results from operations for 2018 in comparison to 2017. Refer to the discussion that follows under the heading "Summary of Results of Operations by Segment" for an analysis of the revenue and net operating income by operating segment, including the components of non same-store revenue and net operating income.

Consolidated Revenue

Consolidated revenue from continuing operations grew by $22.7 million or 2.1% to $1,120.0 million in 2018, driven primarily by LTC funding enhancements (despite the impact of a $0.8 million prior period settlement adjustment received in the 2017 first quarter), expansion of the retirement living operations, home health care funding increases, including $5.3 million in enhanced funding to offset costs related to Bill 148, and growth in management and group purchasing services, partially offset by a decline in home health care volumes, and lower investment income from the Captive. For further information on Bill 148, refer to the discussion under the heading "Update of Regulatory and Funding Changes Affecting Results – Ontario Home Health Care Legislation and Funding".

Consolidated Operating Expenses

Consolidated operating expenses from continuing operations increased by $24.5 million or 2.5% to $986.0 million in 2018, driven by, increased costs of resident care, expansion of the retirement living operations, and higher labour related costs, including the impact of Bill 148, increased overtime and use of subcontracted staff in response to industry wide staffing shortages in certain positions and locations, and the implementation of a new enterprise system, partially offset by lower direct costs due to the impact of lower home health care volumes delivered. Total labour costs increased by $15.7 million over 2017, and represented 86.0% and 86.6% of operating expenses in 2018 and 2017, respectively, and as a percentage of revenue were 75.7% and 75.9%, respectively.

Consolidated Net Operating Income

Consolidated net operating income from continuing operations declined by $1.8 million or 1.4% to $134.0 million in 2018, and represented 12.0% of revenue compared to 12.4% in 2017. Net operating income from the Canadian operations improved by $3.0 million or 2.3% to $133.6 million, and as a percentage of revenue was 11.9% this year compared to 12.0% in 2017, reflecting growth of our retirement living, management and group purchasing operations, partially offset by a decline in contribution from our LTC operations of $0.9 million due to prior period adjustments and higher costs of resident care, and a decline of $5.8 million from our home health care operations due to higher labour related costs and lower business volumes. Net operating income from our U.S. operations reflects investment income from the Captive, which was nominal this period compared to $5.2 million in 2017.

Administrative and Lease Costs

Administrative and lease costs from continuing operations increased by $1.6 million in 2018, and were impacted by increased costs of approximately $1.0 million to support the implementation of new enterprise software. Both periods included lump-sum executive compensation charges, net of the impact of forfeited non-cash share-based awards, of $1.7 million in 2018 and $2.0 million in 2017.

Consolidated Adjusted EBITDA

Consolidated Adjusted EBITDA from continuing operations declined by $3.4 million or 3.4% to $94.2 million this year, representing 8.4% of revenue compared to 8.9% in 2017. Adjusted EBITDA from the Canadian operations improved by $1.5 million, and as a percentage of revenue was 8.5% compared to 8.6% in 2017. Adjusted EBITDA from the U.S. operations declined by $4.9 million reflecting lower investment income from the Captive.

Other Expense

Other expense of $20.2 million ($15.2 million after tax) recorded this year included an impairment charge of $16.2 million in respect of certain of the Company's retirement and LTC centres (refer to discussion under the heading "Other Significant Developments – Impairment Charge"), $2.5 million expensed in connection with the redemption of the 2019 Debentures, and transaction costs of $1.0 million associated with the Lynde Creek Acquisition.

Net Finance Costs

Net finance costs increased by $2.8 million to $26.5 million this year, reflecting a net change in interest rate swap fair value adjustments and loss (gain) on foreign exchange and the Captive's investments aggregating $3.1 million, partially offset by slightly lower net interest costs associated with a lower weighted average interest rate and decline in net debt levels.

Income Taxes

The consolidated income tax provision in 2018 was $4.2 million, and represented an effective tax rate of 34.4%, compared to $10.8 million and an effective tax rate of 25.5% in 2017, with the increase primarily reflecting the proportion of taxable and non-taxable entities. The effective tax rate of the Canadian operations was 29.0% this year compared to 28.3% in 2017, and was impacted by, among other things, fair value adjustments, gains and losses on foreign exchange and investments, and other expense items that have been separately reported. The effective tax rate of the Canadian operations excluding the impact of separately reported items was 27.8% compared to 27.5%.

Discontinued Operations

Earnings (loss) from discontinued operations relate to the former U.S. operations. The after-tax earnings of $23.6 million in 2018 included $14.1 million related to the Captive's reserves (release and favourable impact of discount rate adjustments), a $3.6 million decrease in indemnification provisions and other items, and a net tax recovery of $5.9 million. The after-tax loss of $29.6 million in 2017 related to the write-off of deferred consideration of $37.5 million, and a net increase in indemnification provisions and other items of $4.8 million, partially offset by a release of the Captive's reserves of $5.7 million, and a tax recovery of $7.0 million.

Summary of Results of Operations by Segment

The following provides an analysis of the operating performance of each of our operating segments. Refer to the table at the end of the discussion for a summary of the segmented "revenue", "operating expenses" and "net operating income".

LONG-TERM CARE OPERATIONS

Net operating income from our long-term care operations declined by $0.9 million to $73.0 million in 2018, representing 11.5% of revenue this year compared to 12.0% in 2017, and included the impact of $0.8 million of favourable prior period revenue adjustments received in 2017. Revenue grew by $15.6 million, or 2.5%, of which approximately $6.5 million related to Ontario flow-through funding envelopes, and was therefore directly offset by increased costs of resident care, approximately $0.4 million was from improvements in preferred accommodation, and the balance was from other funding enhancements. Operating expenses increased by $16.5 million, or 3.0%, primarily due to higher labour, supply, maintenance, and food costs. Recruitment challenges in some markets have led to an increased use of subcontracted staff and overtime premiums in response to staffing shortages. Total labour costs increased by $9.8 million and represented 82.5% of operating expenses this year compared to 83.2% in 2017.

RETIREMENT LIVING OPERATIONS

Net operating income from our retirement living operations improved by $6.6 million this year, reflecting continued improvements across all communities and the acquisition completed in April 2018. On a same-store basis, growth in net operating income of $3.5 million was primarily attributable to higher revenue, reflecting an improvement in average occupancy to 85.7% this year from 70.8% in 2017. Non same-store net operating income improved by $3.1 million this period, reflecting the contribution from the Lynde Creek Acquisition and the opening of Douglas Crossing, partially offset by pre-opening costs associated with two communities under construction.

HOME HEALTH CARE OPERATIONS

Net operating income from our home health care operations declined by $5.8 million or 13.4% to $38.0 million this year, and represented 8.8% of revenue compared to 10.1% in 2017. Operations were impacted this year by a 3.8% decline in volumes, and higher labour related costs, partially offset by government contract funding increases. The reduction in home health care volumes was in large part due to an industry-wide capacity shortage of PSWs, and to a lesser extent nurses, which has adversely impacted our ability to continue to meet the growing demand, and in some locations has given rise to increased overtime and use of subcontracted staff. Initiatives are under way to improve our ability to attract and retain care staff. In addition to temporary costs associated with the implementation of new enterprise software, the number of back office administrative staff increased as we manage through the implementation process and associated re-engineering of workflows. Despite the reduction in business volumes in 2017, total labour costs increased this year by $2.5 million and represented 92.8% of operating expenses compared to 92.5% in 2017. Refer to the discussion under the heading "Key Performance Indicators – Home Health Care" and "Update of Regulatory and Funding Changes Affecting Results – Ontario Home Health Care Legislation and Funding".

OTHER CANADIAN OPERATIONS

Net operating income from our management and group purchasing operations increased by $3.1 million this period, and represented 60.7% of revenue compared to 55.4% in 2017, due to growth in clients served.

U.S. OPERATIONS

The decline in net operating income from the U.S. operations reflected lower investment income from the Captive.

The following summarizes our segmented "revenue", "operating expenses" and "net operating income".

Years ended December 31 *(thousands of dollars)*	**Long-term Care**	**Retirement Living**	**Home Health Care**	**Other Canadian Operations**	**Corporate Canada**	**Total Canada**	**Total U.S.**	**Total**
2018 – Same-store								
Revenue	**632,533**	**24,466**	**431,343**	**22,291**	**23**	**1,110,656**	**405**	**1,111,061**
Operating expenses	**559,489**	**18,093**	**393,354**	**8,750**	**–**	**979,686**	**–**	**979,686**
Net operating income	**73,044**	**6,373**	**37,989**	**13,541**	**23**	**130,970**	**405**	**131,375**
NOI margin %	***11.5%***	***26.0%***	***8.8%***	***60.7%***	***100.0%***	***11.8%***	***100.0%***	***11.8%***
2018 – Non Same-store								
Revenue	**–**	**8,946**	**–**	**–**	**–**	**8,946**	**–**	**8,946**
Operating expenses	**–**	**6,337**	**–**	**–**	**–**	**6,337**	**–**	**6,337**
Net operating income	**–**	**2,609**	**–**	**–**	**–**	**2,609**	**–**	**2,609**
2018 – Total								
Revenue	**632,533**	**33,412**	**431,343**	**22,291**	**23**	**1,119,602**	**405**	**1,120,007**
Operating expenses	**559,489**	**24,430**	**393,354**	**8,750**	**–**	**986,023**	**–**	**986,023**
Net operating income	**73,044**	**8,982**	**37,989**	**13,541**	**23**	**133,579**	**405**	**133,984**
NOI margin %	***11.5%***	***26.9%***	***8.8%***	***60.7%***	***100.0%***	***11.9%***	***100.0%***	***12.0%***
2017 – Same-store								
Revenue	616,887	20,321	435,718	18,789	15	1,091,730	5,249	1,096,979
Operating expenses	542,965	17,448	391,867	8,387	–	960,667	–	960,667
Net operating income	73,922	2,873	43,851	10,402	15	131,063	5,249	136,312
NOI margin %	*12.0%*	*14.1%*	*10.1%*	*55.4%*	*100.0%*	*12.0%*	*100.0%*	*12.4%*
2017 – Non Same-store								
Revenue	–	352	–	–	–	352	–	352
Operating expenses	–	842	–	–	–	842	–	842
Net operating loss	–	(490)	–	–	–	(490)	–	(490)
2017 – Total								
Revenue	616,887	20,673	435,718	18,789	15	1,092,082	5,249	1,097,331
Operating expenses	542,965	18,290	391,867	8,387	–	961,509	–	961,509
Net operating income	73,922	2,383	43,851	10,402	15	130,573	5,249	135,822
NOI margin %	*12.0%*	*11.5%*	*10.1%*	*55.4%*	*100.0%*	*12.0%*	*100.0%*	*12.4%*
Change in Total								
Revenue	15,646	12,739	(4,375)	3,502	8	27,520	(4,844)	22,676
Operating expenses	16,524	6,140	1,487	363	–	24,514	–	24,514
Net operating income	(878)	6,599	(5,862)	3,139	8	3,006	(4,844)	(1,838)

ADJUSTED FUNDS FROM OPERATIONS

The following provides a reconciliation of our "net earnings" to FFO and AFFO. A reconciliation of our "net cash from operating activities" to AFFO is also provided under the heading "Reconciliation of Net Cash from Operating Activities to AFFO".

	Three months ended December 31			Twelve months ended December 31		
(thousands of dollars unless otherwise noted)	**2018**	**2017**	**Change**	**2018**	**2017**	**Change**
Net earnings	**6,507**	13,634	(7,127)	**31,738**	2,132	29,606
Add (Deduct):						
Depreciation and amortization	**10,184**	8,170	2,014	**35,270**	31,379	3,891
Depreciation for FFEC (maintenance capex) (1)	**(1,882)**	(1,914)	32	**(7,422)**	(7,495)	73
Other expense (continuing operations)	**16,642**	–	16,642	**20,195**	–	20,195
Other expense (income) (discontinued operations)	**(9,663)**	(3,441)	(6,222)	**(17,755)**	36,576	(54,331)
Fair value adjustments	**1,792**	(271)	2,063	**956**	(2,474)	3,430
Gain on foreign exchange and investments	**(147)**	(423)	276	**(1,203)**	(864)	(339)
Current income tax recovery on other expense, fair value adjustments, and gain/loss on foreign exchange and investments (2)	**(12,076)**	(1,391)	(10,685)	**(11,805)**	(1,230)	(10,575)
Deferred income tax expense (recovery)	**830**	2,570	(1,740)	**1,936**	(5,063)	6,999
FFO	**12,187**	16,934	(4,747)	**51,910**	52,961	(1,051)
Amortization of deferred financing costs	**391**	417	(26)	**1,736**	1,728	8
Accretion costs	**635**	616	19	**2,878**	2,812	66
Non-cash share-based compensation	**214**	289	(75)	**430**	1,496	(1,066)
Principal portion of government capital funding	**1,300**	1,232	68	**5,200**	4,928	272
Income support (retirement acquisitions)	**–**	–	–	**–**	66	(66)
Amounts offset through investments held for self-insured liabilities (3)	**163**	(2,418)	2,581	**850**	(4,178)	5,028
Additional maintenance capex (1)	**(2,320)**	(1,357)	(963)	**(5,253)**	(1,318)	(3,935)
AFFO	**12,570**	15,713	(3,143)	**57,751**	58,495	(744)
Per Basic Share *($)*						
FFO	**0.137**	0.191	(0.054)	**0.587**	0.596	(0.009)
AFFO	**0.142**	0.178	(0.036)	**0.653**	0.659	(0.006)
Per Diluted Share *($)*						
FFO	**0.137**	0.191	(0.054)	**0.587**	0.596	(0.009)
AFFO	**0.138**	0.171	(0.033)	**0.634**	0.640	(0.006)
Dividends *($)*						
Declared	**10,612**	10,623	(11)	**42,351**	42,583	(232)
Declared per share *($)*	**0.120**	0.120	–	**0.480**	0.480	–
Weighted Average Number of Shares *(thousands)*						
Basic	**88,612**	88,633		**88,403**	88,805	
Diluted	**98,962**	99,916		**98,753**	100,088	
Total maintenance capex (1)	**4,202**	3,271	931	**12,675**	8,813	3,862

(1) The aggregate of the items "depreciation for FFEC" and "additional maintenance capex" represents our total actual maintenance capex incurred in the period. An amount equivalent to our depreciation for FFEC, or furniture, fixtures, equipment and computers, is deducted in determining FFO, and the difference from the actual total maintenance capex incurred is adjusted for in determining AFFO.

(2) Represents current income tax with respect to items that are excluded from the computation of FFO and AFFO, such as fair value adjustments, gains or losses on foreign exchange and investments, and other expense.

(3) Represents AFFO of the Captive that decreases/(increases) the Captive's investments held for self-insured liabilities not impacting the Company's reported cash and short-term investments.

AFFO 2018 Fourth Quarter Financial Review

AFFO for the 2018 fourth quarter declined by $3.1 million to $12.6 million ($0.142 per basic share) from $15.7 million ($0.178 per basic share) in the same 2017 period, reflecting a decrease in Adjusted EBITDA (excluding the impact of any earnings from the Captive and any non-cash share-based compensation), and an increase in maintenance capex and current income taxes. A discussion of the factors impacting net earnings can be found under the heading "2018 Fourth Quarter Financial Review".

Maintenance capex was $4.2 million this quarter, compared to $3.3 million in 2017, and compared to $3.6 million in the 2018 third quarter, representing 1.5%, 1.2% and 1.3% of revenue, respectively.

AFFO 2018 Financial Review

AFFO for the year declined by $0.7 million to $57.8 million ($0.653 per basic share) from $58.5 million ($0.659 per basic share) in 2017, reflecting an improvement in Adjusted EBITDA (excluding the impact of any earnings from the Captive and any non-cash share-based compensation) , and lower current income taxes of $1.9 million, offset by an increase in maintenance capex of $3.9 million. AFFO for both years was impacted by lump-sum executive cash compensation charges of $2.1 million and $1.5 million on an after-tax basis in 2018 and 2017, respectively. A discussion of the factors impacting net earnings can be found under the heading "2018 Financial Review".

Our current income taxes benefitted in 2018 from favourable timing differences, and the utilization of tax loss carryforwards, and represented an effective tax rate on FFO of 13.6% in 2018 compared to 16.1% in 2017. In 2019, we anticipate our effective tax rate on FFO will be in the range of 17% to 19%. The determination of FFO includes a deduction for current income tax expense, and does not include deferred income tax expense. As a result, the effective tax rates on our FFO can be impacted by: adjustments to our estimates of annual deferred timing differences, particularly when dealing with cash-based tax items versus accounting accruals; changes in the proportion of earnings between taxable and non-taxable entities; book-to-file adjustments for prior year filings; and the ability to utilize loss carryforwards.

Maintenance capex was $12.7 million in 2018, compared to $8.8 million in 2017, representing 1.1% and 0.8% of revenue, respectively. These costs fluctuate on a quarterly and annual basis with the timing of projects and seasonality. Management monitors and prioritizes the capital expenditure requirements of its properties throughout the year, taking into account the urgency and necessity of the expenditure. In 2019, we are expecting to spend in the range of $10 million to $12 million in maintenance capex.

Reconciliation of Net Cash from Operating Activities to AFFO

The following provides a reconciliation of our "net cash from operating activities" to AFFO.

	Three months ended December 31		**Twelve months ended December 31**	
(thousands of dollars)	**2018**	**2017**	**2018**	**2017**
Net cash from operating activities	**1,189**	10,581	**39,473**	47,160
Add (Deduct):				
Net change in operating assets and liabilities, including interest, taxes and payments for U.S. self-insured liabilities	**26,196**	10,980	**36,708**	20,562
Current income tax on items excluded from AFFO (1)	**(12,076)**	(1,391)	**(11,805)**	(1,230)
Depreciation for FFEC (maintenance capex) (2)	**(1,882)**	(1,914)	**(7,422)**	(7,495)
Additional maintenance capex (2)	**(2,320)**	(1,357)	**(5,253)**	(1,318)
Principal portion of government capital funding	**1,300**	1,232	**5,200**	4,928
Income support (retirement acquisitions)	**–**	–	**–**	66
Amounts offset through investments held for self-insured liabilities (3)	**163**	(2,418)	**850**	(4,178)
AFFO	**12,570**	15,713	**57,751**	58,495

(1) Represents current income tax with respect to items that are excluded from the computation of AFFO, such as fair value adjustments, gains or losses on foreign exchange, and other expense.

(2) The aggregate of the items "depreciation for FFEC" and "additional maintenance capex" represents our total actual maintenance capex incurred in the period. An amount equivalent to our depreciation for FFEC, or furniture, fixtures, equipment and computers, is deducted in determining FFO, and the difference from the actual total maintenance capex incurred is adjusted for in determining AFFO.

(3) Represents AFFO of the Captive that decreases/(increases) its investments held for self-insured liabilities not impacting the Company's reported cash and short-term investments.

OTHER SIGNIFICANT DEVELOPMENTS

The discussion under the heading “Significant 2018 Events and Developments” summarizes our current activities related to the growth of our retirement living operations and convertible debenture activity. This section provides a summary of other developments that have impacted the financial results or operations of Extendicare for 2018 in comparison to 2017.

Impairment Charge

In the 2018 fourth quarter, the Company recorded an impairment charge of $16.2 million ($11.8 million after tax), in respect of certain of its retirement communities ($15.9 million), and LTC centers ($0.3 million). Further details are provided in *note 19* of the audited consolidated financial statements.

The impairment charge for the retirement living operations relates to the write down of the carrying value of the property and equipment of three Saskatchewan retirement communities that were acquired in late 2015 and early 2016, two of which were newly opened at that time and are still in lease up. These communities have not performed as expected, primarily due to competitive market conditions resulting in lower rates and occupancy and higher labour and benefit costs.

Expansion of Alberta Long-term Care Centre

In February 2018, the Company completed a 24-bed addition to its Extendicare Eaux Claires long-term care centre in Edmonton, Alberta, at a cost of $3.6 million. The initial 180-bed centre was built in 2011 with a design allowing for expansion. This addition achieved stabilized occupancy in April 2018, and is anticipated to provide incremental net operating income of approximately $0.6 million annually.

2015 U.S. Sale Transaction – Deferred Consideration

As part of the proceeds from the U.S. Sale Transaction, the Company was entitled to receive an ongoing cash stream for a period of 15 years relating to certain U.S. skilled nursing centres that were leased prior to the closing (the “Leased Centres”). The present value ascribed to these proceeds was reflected as deferred consideration and was recorded at amortized cost using the effective interest method. During the 2017 second quarter, the Company was notified of the potential for an event of default by the operator of the Leased Centres, and subsequently received notice that the operator of the Leased Centres had failed to make its required minimum lease payments. As a result of events and discussions that transpired during 2017, the remaining balance of the deferred consideration of $37.5 million (US$27.9 million) was written off in 2017.

Other Financing Activity

In August 2018, the Company renewed Canadian Mortgage and Housing Corporation mortgages in the amount of $8.3 million for a term of four years to August 2022, at a fixed rate of 2.96%.

In September 2018, the Company secured financing of $10.5 million on one of its Ontario retirement communities for a term of 10 years, with a variable rate of prime plus 0.5%. In conjunction therewith, the Company entered into an interest rate swap contract to lock in the interest rate at 5.04% for the full term of the financing.

In the 2018 third quarter, the Company secured construction financing of $27.2 million for its retirement development project in Barrie, Ontario, with an additional letter of credit facility of $1.0 million. Loan payments are interest-only based on a variable 30-day banker’s acceptance rate plus 2.25%, with no standby fee. The construction loan is repayable on demand and, in any event, is to be fully repaid by the earlier of September 2023 and three months following stabilized occupancy as defined by the agreement.

UPDATE OF REGULATORY AND FUNDING CHANGES AFFECTING RESULTS

In Canada, provincial legislation and regulations closely control all aspects of operation and funding of long-term care centres and publicly funded home health care services, including the fee structure, subsidies, the adequacy of physical centres, standards of care and accommodation, equipment and personnel. A substantial portion of the fees paid to providers of these services are funded by provincial programs, with a portion to be paid by residents or clients. Each province has a different system for managing the services provided. In some provinces, the government has delegated responsibility for the funding and administration of long-term care programs to regional health authorities. As a result, there can be significant variability in the regulations governing the provision of and reimbursement for care from location to location. The Company is unable to predict whether governments will adopt changes in their funding or regulatory programs, and if adopted and implemented, the impact, if any, such changes will have on the Company's business, results of operations and financial condition.

In most provinces, a license must be obtained from the applicable provincial ministry of health in order to operate either a long-term care centre or a retirement centre. In general, the issuance of new licenses for LTC beds is infrequent because of the funding implications for the provincial governments, while the issuance of licenses for retirement centres is less restrictive as the funding for these services is generally private-pay. In addition to the license procedure, or in some provinces in place of, LTC operators in Alberta, Manitoba, Ontario and Saskatchewan are required to sign service contracts that incorporate service expectations with the applicable provincial health authority.

The People's Health Care Act, 2019 (Ontario) (Bill 74)

On February 26, 2019, the Ontario government tabled Bill 74, *The People's Health Care Act, 2019* (Ontario), which proposes to create an agency called Ontario Health to act as a central point of accountability and oversight for the province's public health care system. Organizations to be integrated into Ontario Health include Cancer Care Ontario, Health Quality Ontario, eHealth Ontario, Health Shared Services Ontario, and the Local Health Integrated Networks. The government has indicated that the transition will roll out in phases to ensure continuity of care.

The government also announced its intent to create local Ontario Health Teams to guide patients and families between providers and through transitions. These teams of local health care providers would implement a community-based health care delivery model that connects care and includes providers such as primary care and hospitals, home care and long-term care, and mental health and addictions supports. Working as a coordinated group, they would share responsibility for care plans, service provision and outcomes.

The details as to how these Ontario Health Teams will be constituted have yet to be released. Given that all the government funded ParaMed business in Ontario is contracted through the LHINs today, the ParaMed LHIN contracts will have to be assigned or reissued by Ontario Health or its assigns as the LHINs are integrated into the new agency.

Although this represents a significant change in the contracting mechanism for the home care business in Ontario, the underlying market demand is such that it is likely Extendicare will be able to transition services into the new business model with minimal interruption. The Company is unable to predict the nature and extent such changes will have on the Company's business, results of operations and financial condition.

Fair Workplaces, Better Jobs Act, 2017 (Ontario) (Bill 148)

In November 2017, Bill 148, *Fair Workplaces, Better Jobs Act, 2017* (Ontario), received Royal Assent, and came into effect in 2018. The Act contains a number of amendments to both the *Employment Standards Act* (ESA) and the *Labour Relations Act* (LRA), as part of the Ontario government's efforts to overhaul workplace laws. These changes included, among other things: an increase in minimum wage to $14 per hour that took effect on January 1, 2018, with a further increase to $15 per hour that was to take effect on January 1, 2019; revisions to vacation, public holiday pay and personal leave entitlements that took effect on January 1, 2018; equal pay for equal work standards that took effect on April 1, 2018; amendments to schedule change notifications and minimum "on call" payments that were to take effect on January 1, 2019; and lower voting thresholds for unionization. In May 2018, the government filed Ontario Regulation 375/18, which prescribed a return to the method of determining public holiday pay using the formula that applied prior to Bill 148, effective July 1, 2018. In November 2018, legislation was enacted that amended or reversed many of the changes enforced by Bill 148, refer to the discussion under the heading "Making Ontario Open for Business Act, 2018 (Bill 47)".

Operationally, the Act necessitated changes in the manner in which the Company manages its workforce in a number of business areas and could result in increased unionization. Financially, the impact of Bill 148 on the Company's private-pay and long-term care businesses has not been significant.

With respect to the Company's government-funded home health care operations, the Company has recorded $5.3 million of enhanced funding in 2018 to offset costs related to Bill 148, of which $2.0 million was received in respect of quarter ended March 31, 2018. While the government has yet to announce continued funding post March 31, 2018, it has indicated its intentions to continue to engage with the Local Health Integration Networks (LHINs), contracted service provider organizations, and home care employer associations to evaluate the legislation and to assess the costs associated with Bill 148 for fiscal 2018/2019. The Company believes that the funding it has accrued for the period April 1, 2018 to December 31, 2018 is a reasonable estimation. There can, however, be no assurance that any such government funding will be received, or to the extent any funding is received that it will be commensurate with the Company's additional costs resulting from such legislative changes.

While the Company does not anticipate the increases to the minimum wage will have a significant impact on the financial results given the current pay rates of its workforce, there can be no assurance that these changes will not necessitate increased pay rates for those already above the minimum wage, in order for the Company to retain and attract employees.

As the Company's labour costs account for approximately 86% of its operating costs, increased labour costs could have a significant adverse effect on the Company's results from operations and cash flows, should such cost increases not be offset by commensurate increases in government funding. Management is unable to predict the nature and extent of any changes the government may make to its funding programs or the effect of any such changes on the Company, but it anticipates that the government will comply with its contractual obligations relating thereto.

Making Ontario Open for Business Act, 2018 (Bill 47)

In November 2018, Bill 47, *Making Ontario Open for Business Act, 2018* (Ontario), received Royal Assent and came into force the same day. The Act makes many changes to various pieces of legislation governing employment and labour relations in Ontario, principally the ESA and LRA, and reverses many of the changes to the ESA and LRA that were enacted by Bill 148. Bill 47, among other things: freezes the minimum wage at $14 an hour until October 1, 2020, following which it will be adjusted annually by the rate of inflation; removes the entitlement to two paid personal leave days; cancels a range of scheduling change protections that were to come into force in 2019; eliminates changes to the equal pay for equal work standards impacting part-time, contract, and temporary workers; and repeals the new public holiday pay calculations. As a result, Bill 47 reduces some of the operational and financial impacts resulting from Bill 148 on the Company's financial results, as discussed above.

Strengthening Quality and Accountability for Patients Act, 2017 (Ontario)

Bill 160, *Strengthening Quality and Accountability for Patients Act, 2017* (Ontario), received Royal Assent in December 2017. The Act, which supports the Ontario government's Patients First: Action Plan for Health Care, includes new legislation as well as changes to a number of existing pieces of legislation. The Act, among other things, provides updates to the *Long-Term Care Homes Act, 2007* (LTCHA) to add new enforcement tools, including financial penalties, and new provincial offences to ensure operators are addressing concerns promptly. In December 2018, the government notified the sector that the in-force date of January 1, 2019 for the financial penalties associated with this Act had been delayed and that no new in-force date had been set. The legislation also includes a consent-based framework to protect residents who need to be secured in a LTC centre for safety reasons. In addition, the Act provides updates to the *Retirement Homes Act, 2010* that would strengthen the oversight powers of the Retirement Homes Regulatory Authority (RHRA) and increase transparency, accountability and governance of the RHRA. In addition, as part of a stated commitment to "improve the transparency of public information related to the Long-Term Care Home Quality Inspection Program in Ontario", the Ontario Ministry of Health and Long-term Care (MOHLTC) released information on the performance of every LTC centre in the province in April 2018.

Ontario LTC Redevelopment and Expansion

Extendicare continues to advance the redevelopment of its 21 Class C LTC centres (3,287 beds) in Ontario under the MOHLTC's enhanced redevelopment program.

In October 2018, the MOHLTC announced that it is moving forward with building 6,000 new LTC beds across the province following a call for applications (CFA) in February 2018, stating that these represented the first wave of more than 15,000 new LTC beds that the government has committed to build over the next five years. The MOHLTC indicated that applications for new beds that had not advanced in this first round will be considered in future CFAs.

Extendicare plans to participate in requests for new beds to enhance its redevelopment projects and in new developments where market opportunity exists as part of its approach to campus of care. In 2018, the Company was awarded 158 new beds in connection with three of its redevelopment projects. To date, the MOHLTC has approved the licensing applications for two of our LTC centres, one in Stittsville and one in Sudbury, and we have a further five applications that have advanced past the initial stage of the MOHLTC's review process. Each project is unique and the overall plan involves a combination of new construction and retrofits. While factors could arise that affect the timing or sequence of our redevelopment plans, we are working closely with the MOHLTC with a goal to accelerating redevelopment of these seven centres. As these redevelopment projects are completed, we expect to realize the benefit of improved performance and extended license terms. Other projects will move forward provided they meet our investment objectives.

Ontario Long-term Care Funding

Ontario is Extendicare's largest market for its senior care services. Funding for LTC centres in Ontario is based on reimbursement for the level of care assessed to be required by the residents, in accordance with scheduled rates. The MOHLTC allocates funds through "funding envelopes", specifically: nursing and personal care (NPC); programs and support services (PSS); and accommodation (which includes a sub-envelope for raw food). The funding for the NPC and PSS envelopes is generally adjusted annually based on the acuity of residents as determined by a classification assessment of resident care needs. The NPC, PSS and food envelopes are "flow-through" envelopes, whereby any deviation in actual costs from scheduled rates is either absorbed by the provider (if actual costs exceed funding allocations) or is returned to the MOHLTC (if actual costs are below funding allocations). With respect to the accommodation envelope, providers retain any excess funding received over costs incurred. The province sets the rates for standard accommodation, as well as the maximum amounts that a provider can charge for semi-private and private accommodation (preferred accommodation). The provider is permitted to bill and retain the premiums charged for preferred accommodation. The accommodation rates are substantially paid for by the resident; however, the province guarantees funding for standard accommodation through resident subsidies. Overall government funding is occupancy-based, but once the average occupancy level of 97% or higher for the calendar year is achieved, operators receive government funding based on 100% occupancy. In addition, under the MOHLTC's occupancy protection program, providers with occupancy levels equal to 90% and less than 94% receive funding based on their actual occupancy plus 1%, and those with occupancy levels equal to 94% and less than 97% receive funding based on their actual occupancy plus 2%. In 2018, all but two of Extendicare's LTC centres in Ontario achieved the 97% occupancy threshold.

On April 1st each year, the MOHLTC generally provides flow-through funding adjustments on the government funded portion of the fees. Funding for the NPC and PSS flow-through funding envelopes increased by 2% on April 1, 2018. Extendicare estimates that these funding enhancements, along with our case mix index and re-indexing adjustments, represent additional annual revenue of approximately $2.7 million to offset additional costs for resident care and services within the NPC and PSS flow-through funding envelopes (April 2017 – $3.4 million).

On July 1st each year, the MOHLTC generally implements annual accommodation funding increases to the per diem rates provided to long-term care providers. The July 1, 2018 funding enhancements increased the daily rates for the non flow-through component of the accommodation envelope by $0.91 (1.6%) and by $0.54 (6.0%) for the flow-through food component. Extendicare estimates that this enhanced funding represents additional annual revenue of approximately $2.7 million in total, of which approximately $1.0 million is flow-through funding (2017 – $2.5 million in total, of which $1.0 million was flow-through).

In addition, LTC operators in Ontario are permitted to designate up to 60% of the resident capacity of a centre as preferred accommodation and charge higher accommodation rates that vary according to the structural classification of the LTC centre. For beds that are not classified as "New" or "A" beds, the maximum preferred accommodation premiums increased on July 1, 2018, by $0.13 to $8.33 per day for a semi-private room and by $0.29 to $18.74 per day for a private room. For beds that are classified as "New" and "A" beds, the maximum preferred accommodation premiums increased on July 1, 2018, by $0.19 to $12.49 per day for a semi-private room and by $0.41 to $26.04 per day for a private room. Extendicare has 13 "New" LTC centres in Ontario with 1,847 beds, of which 1,106 are private beds, from which it will benefit from this premium increase as new residents are admitted.

Alberta Long-term Care Funding

Alberta is Extendicare's second largest market for its senior care services. Since April 2010, AHS has been using an activity-based funding system for continuing care centres that includes the measurement of a resident's acuity through the use of a resident assessment instrument – minimum data set, or RAI-MDS, to determine the resident's level of care and resources required. The Alberta Continuing Care Association is actively engaged in discussions with the Alberta Government and AHS to further enhance care funding to accommodate higher expenses within continuing care, and to revise the existing funding model used within continuing care. It was anticipated that a revised care funding model would have been implemented during 2016; however, following receipt of public input to inform new or revised legislation, the provincial government has yet to release its strategy related to continuing care and its approach to long-term care for the future.

The April 1, 2018 funding adjustments for long-term care and designated supportive living for fiscal 2018/2019 represent additional annual revenue of approximately $1.2 million. Last year, the April 1, 2017 funding changes for fiscal 2017/2018 represented additional annual revenue of approximately $0.9 million. In addition, in the 2017 first quarter, AHS provided retroactive funding adjustments for fiscal 2015/2016 and 2016/2017 in recognition of labour contract settlements of $0.8 million and an ongoing annual revenue increase of approximately $0.5 million.

On July 1, 2018, the annual accommodation charge adjustments (the portion paid directly by residents of long-term care and designated supportive living centres) increased by 2.2%, based on inflation as reflected by Alberta's CPI. Extendicare estimates that the 2.2% increase represents additional revenue of approximately $0.7 million (July 2017 – $0.6 million).

Ontario Home Health Care Funding

Extendicare's ParaMed Home Health Care division operates in six provinces across Canada, currently providing approximately 10.9 million hours of service annually, which we believe makes ParaMed the largest private-sector provider of publicly funded home health care in Canada, and the largest in Ontario. The Ontario market currently represents approximately 83% of ParaMed's service volumes, of which approximately 98% are received from government-funded contracts at specified rates, and the remainder from private-pay clients. The Company is unable to predict whether the government will adopt changes in its funding or budget priorities, and if adopted and implemented, the impact, if any, such changes will have on the Company's business, results of operations and financial condition.

In shaping the delivery of health care to Canadians, both the federal and provincial governments have stated that home health care is an area that merits further investment to ensure that more health care services are available in the home. Recent health accord agreements reached between the federal government and each of the provinces that began in fiscal 2017/2018, include targeted funding for home health care. For Ontario alone, targeted home health care funding has been reported to be an additional $2.3 billion over the next decade. In addition, as part of its initiative to improve and make the health care system more efficient, the Ontario government has noted that insufficient capacity in the health care system, like home care, is contributing to the problem of hallway health care in the province (refer to the discussion under the heading "The People's Health Care Act, 2019 (Ontario) (Bill 74)"). As governments continue to recognize the benefits of this segment of the Canadian health care system, we believe that ParaMed is well-positioned to take advantage of the significant organic growth opportunity that exists today, and that steps we are taking to position ParaMed as the employer of choice for caregivers will further enhance our position. In addition, ParaMed continues to assess private-pay home health care opportunities that may enable it to further leverage its platform.

As part of the 2018 Ontario Budget, the government announced funding enhancements effective April 1, 2018, to provide contract rate increases of 2% for nursing and therapies contracts, 1% for harmonized personal support service contracts and 2% for other personal support contracts. These rate increases are estimated to provide additional revenue for ParaMed of approximately $5.2 million annually based on volumes experienced since April 1, 2018. More generally under the 2018 Ontario Budget, the government announced plans to invest an additional $650 million on home care over the next three years, that would include $180 million in new funding for 2.8 million more personal support hours, 284,000 more nursing visits and 58,000 more therapy visits. Over the next three years, the Budget allocates $45 million to improve working conditions and contract rates for PSWs, registered practical nurses, registered nurses and therapists; $23 million to add an estimated 5,500 PSWs to the workforce; $38 million in education and training for new and existing PSWs; and $65 million for a pilot program to establish a tax-free savings account on behalf of eligible PSWs.

In August 2018, the MOHLTC announced that it was winding down the Self-Directed Personal Support Services Ontario agency, which was still in its set-up phase, in order to reduce the administrative burden of delivering home health care. The program, initially announced in October 2017, was intended to provide personal support services from a new provincial agency.

LIQUIDITY AND CAPITAL RESOURCES

Sources and Uses of Cash

The following summarizes the sources and uses of cash between our continuing and discontinued operations for 2018 and 2017.

			2018			2017
(thousands of dollars unless otherwise noted)	**Continuing**	**Discontinued**	**Total**	**Continuing**	**Discontinued**	**Total**
Cash provided by operating activities, before working capital changes and interest and income taxes	**94,668**	–	**94,668**	99,333	–	99,333
Net change in operating assets and liabilities						
Accounts receivable	**(8,172)**	–	**(8,172)**	9,569	–	9,569
Other assets	**(536)**	–	**(536)**	4,283	–	4,283
Accounts payable and accrued liabilities	**2,210**	–	**2,210**	(6,144)	–	(6,144)
	(6,498)	–	**(6,498)**	7,708	–	7,708
Interest, taxes and claims payments						
Interest paid	**(28,383)**	–	**(28,383)**	(29,560)	–	(29,560)
Interest received	**3,785**	–	**3,785**	3,932	–	3,932
Income taxes paid	**(8,862)**	–	**(8,862)**	(10,093)	–	(10,093)
Payments for U.S. self-insured liabilities	–	**(15,237)**	**(15,237)**	–	(24,160)	(24,160)
	(33,460)	**(15,237)**	**(48,697)**	(35,721)	(24,160)	(59,881)
Net cash from operating activities	**54,710**	**(15,237)**	**39,473**	71,320	(24,160)	47,160
Net cash from investing activities	**(70,289)**	**15,237**	**(55,052)**	(18,564)	24,160	5,596
Net cash from financing activities	**(48,763)**	–	**(48,763)**	(23,612)	–	(23,612)
Net cash from discontinued operations	–	–	–	–	–	–
Foreign exchange gain (loss) on U.S. cash held	**2,079**		**2,079**	(2,570)	–	(2,570)
Increase (decrease) in cash and short-term investments	**(62,263)**	–	**(62,263)**	26,574	–	26,574
Cash and short-term investments at beginning of year	**128,156**		**128,156**	101,582		101,582
Cash and short-term investments at end of year	**65,893**	–	**65,893**	128,156	–	128,156
Average U.S./Canadian dollar exchange rate			**1.2957**			1.2986

As at December 31, 2018, Extendicare had cash and short-term investments on hand of $65.9 million reflecting a decrease in cash of $62.3 million from the beginning of the year, primarily related to the acquisition completed in the 2018 second quarter, growth capital expenditures and the purchase of Common Shares for cancellation. Cash flow generated from the operating activities of our continuing operations of $54.7 million was in excess of cash dividends paid of $37.4 million by $17.3 million, and was used to support maintenance capex and principal debt repayments.

Discontinued operations reflect the payment of claims for U.S. self-insured liabilities as a component of net cash from operating activities, which payments are funded by the Captive's investments held for self-insured liabilities. Changes in the Captive's investments are reported as a component of net cash from investing activities, as those invested funds are not included in cash and short-term investments.

Net cash from operating activities of the continuing operations was a source of cash of $54.7 million in 2018 compared to $71.3 million in 2017, primarily due to a $14.2 million net decline in the change in operating assets and liabilities between periods.

Net cash from investing activities of the continuing operations was a use of cash of $70.3 million in 2018 compared to $18.6 million in 2017. The 2018 activity included the Lynde Creek Acquisition of $33.8 million and purchases of property, equipment and other intangible assets, as set out in the table below, partially offset by funds of $9.7 million repatriated from the Captive, and the collection of other assets. The 2017 activity included the repatriation of funds from the Captive in the amount of $21.1 million and the collection of other assets, offset by capital expenditures. Growth capex, excluding acquisitions, relates to the construction of new beds, building improvements or other capital costs, all of which are aimed at earnings growth. The increase in growth capex relates primarily to the development of retirement communities and redevelopment of LTC centres in Ontario. Maintenance capex relates to our actual capital expenditures incurred to sustain and upgrade existing property and equipment. Management monitors and prioritizes the capital expenditure requirements of its properties throughout the year, taking into account the urgency and necessity of the expenditure. In 2019, we are projecting to spend in the range of $10 million to $12 million in maintenance capex, and in the range of $50 million to $55 million in growth capex related primarily to the retirement development and LTC redevelopment projects.

(thousands of dollars)	**2018**	**2017**
Growth capex	**39,291**	33,521
Deduct: capitalized interest	**(1,318)**	(1,197)
Growth capex, excluding capitalized interest	**37,973**	32,324
Maintenance capex	**12,675**	8,813
	50,648	41,137

Net cash from financing activities of the continuing operations was a use of cash of $48.8 million in 2018 compared to a use of cash of $23.6 million in 2017. The 2018 activity included debt repayments of $32.4 million, cash dividends paid of $37.4 million, Common Shares acquired for cancellation under a normal course issuer bid at a cost of $6.3 million, and financing costs primarily related to the issuance and redemption of convertible debentures, partially offset by draws on construction financing of $23.0 million and mortgage financing of $10.5 million secured on a retirement community. The 2017 activity included debt repayments of $22.0 million, cash dividends paid of $37.5 million, and Common Shares acquired for cancellation of $6.5 million, partially offset by the refinancing of long-term debt for a net issuance of $26.4 million, and draws on construction financing of $17.3 million. For information on the change in long-term debt, refer to "Liquidity and Capital Resources – Long-term Debt".

Capital Structure

SHAREHOLDERS' EQUITY

The following summarizes our shareholders' equity for 2018 and 2017.

(thousands of dollars unless otherwise noted)	**2018**	**2017**
Shareholders' Equity		
Common Shares	**492,064**	490,881
Equity portion of convertible debentures	**7,085**	5,573
Contributed surplus	**2,706**	2,437
	501,855	498,891
Accumulated deficit at beginning of year	**(365,084)**	(322,025)
Adoption of new standard on financial instruments	**4,334**	–
Net earnings for the period	**31,738**	2,132
Dividends declared	**(42,351)**	(42,583)
Equity portion of redeemed convertible debentures	**5,573**	
Purchase of Common Shares in excess of book value and other	**(2,357)**	(2,608)
Accumulated deficit at end of period	**(368,147)**	(365,084)
Accumulated other comprehensive loss	**(7,717)**	(4,851)
Shareholders' Equity	**125,991**	128,956
U.S./Canadian dollar exchange rate at end of period	**1.3637**	1.2571

Share Information *(thousands)*	**February 27, 2019**	**December 31, 2018**	December 31, 2017
Common Shares (TSX symbol: EXE) (1)	**88,615.0**	**88,490.0**	**88,523.3**

(1) Closing market value per the TSX on February 27, 2019, was $7.56.

The retrospective adoption of the new standard on financial instruments resulted in the reclassification of $4.3 million to the opening accumulated deficit in connection with unrealized gains on the investments held for self-insured liabilities that had been recorded as part of accumulated other comprehensive loss as at December 31, 2017. The net increase in the equity portion of convertible debentures reflects the classification of the equity portion of the 2025 Debentures issued this year, partially offset by the reclassification of the equity portion of the 2019 Debentures to the accumulated deficit upon their redemption.

DISTRIBUTIONS

The declaration and payment of distributions is at the discretion of our board of directors (the "Board") as to the amount and timing of dividends to be declared and paid, after consideration of a number of factors including results of operations, requirements for capital expenditures and working capital, future financial prospects of Extendicare, debt covenants and obligations, and any other factors deemed relevant by the Board. If our Board determines that it would be in Extendicare's best interests, it may modify the amount and frequency of dividends to be distributed to holders of Common Shares.

The Company declared cash dividends of $0.48 per share in 2018 and 2017, for total dividends of $42.3 million and $42.6 million, respectively. The portion of dividends paid in cash in 2018 was $37.4 million (2017 – $37.5 million), and $4.9 million (2017 – $5.1 million) was by way of Common Shares issued under a dividend reinvestment plan (2018 – 650,361 shares and 2017 – 535,025 shares).

Net cash from operating activities was $39.5 million in 2018 and $47.2 million in 2017, and included payments of $15.2 million and $24.2 million, respectively, for U.S. self-insured liabilities that were funded by investments held by the Captive that are reported as a source of cash from investing activities. For further information on the sources and uses of cash between our continuing and discontinued operations, refer to the previous discussion under the heading "Liquidity and Capital Resources – Sources and Uses of Cash".

Compared to our AFFO of $57.8 million in 2018, dividends declared of $42.3 million represented a payout ratio of approximately 73% (2017 – 73%). For further information on our AFFO, refer to the discussion under the heading "Adjusted Funds from Operations".

NORMAL COURSE ISSUER BID

During 2018, under a normal course issuer bid that commenced on January 15, 2018 and ended on January 14, 2019, the Company acquired and cancelled 703,585 Common Shares at an average price of $8.89 per share, for a total cost of $6.3 million. During 2017, under a previous normal course issuer bid, the Company acquired and cancelled 696,220 Common Shares at a weighted average price of $9.27 per share, for a total cost of $6.5 million.

In January 2019, Extendicare received the approval of the TSX to renew its normal course issuer bid (the "Bid") to purchase for cancellation up to 8,830,000 Common Shares (approximately 10% of the public float) through the facilities of the TSX, and on alternative Canadian trading systems. The Bid commenced on January 15, 2019, and provides Extendicare with flexibility to purchase Common Shares for cancellation until January 14, 2020, or on such earlier date as the Bid is complete. Subject to the TSX's block purchase exception, on any trading day, purchases under the Bid will not exceed 54,852 Common Shares. The price that Extendicare will pay for any Common Shares purchased under the Bid will be the prevailing market price at the time of purchase and any Common Shares purchased will be cancelled.

Long-term Debt

CONTINUITY OF LONG-TERM DEBT

Long-term debt totalled $529.0 million as at December 31, 2018, compared with $536.1 million as at December 31, 2017, representing a decrease of $7.1 million, primarily due to debt repayments and a change in the equity component of the convertible debentures following the refinancing this year, partially offset by draws on construction loans and mortgage financing of $10.5 million secured on a retirement community. The long-term debt activity for 2017 included a net $26.4 million refinancing of $3.6 million of mortgages on nine Alberta LTC centres with a $30.0 million term loan with the Canadian Imperial Bank of Commerce (the "CIBC Term Loan"), draws on construction loans and an increase in finance lease obligations for customized cloud-based software, partially offset by scheduled debt repayments. Extendicare and its subsidiaries are in compliance with all of their respective financial covenants as at December 31, 2018. Details of the components, terms and conditions of long-term debt are provided in *note 12* of the audited consolidated financial statements.

The following summarizes the changes in the carrying amounts of long-term debt for 2018 and 2017.

(millions of dollars)	**2018**	**2017**
Long-term debt at beginning of year, prior to deferred financing costs	**541.8**	510.3
Issue of long-term debt		
2025 Debentures at face value	**126.5**	–
Construction loans	**23.0**	17.3
Mortgages	**10.5**	–
CIBC Term Loan	**–**	26.4
Finance lease obligations	**–**	8.9
Redemption of 2019 Debentures at face value	**(126.5)**	–
Repayment of long-term debt	**(32.4)**	(22.0)
Change in equity component of convertible debentures and other	**(5.5)**	0.9
	537.4	541.8
Deferred financing costs at end of year	**(8.4)**	(5.7)
Long-term debt at end of year	**529.0**	536.1
Less: current portion	**(74.7)**	(59.7)
	454.3	476.4

CREDIT FACILITIES

In November 2017, the Company arranged for a demand credit facility in the amount of $65.0 million (the "ParaMed Credit Facility") that is secured by the assets of our home health care business, and is available for general corporate purposes of the Company. The ParaMed Credit Facility has no financial covenants, but does contain normal and customary terms. The entire $65.0 million was available and unutilized as at December 31, 2018.

Extendicare has a demand credit facility in the amount of $47.3 million with the Royal Bank of Canada (the "RBC Credit Facility") that is secured by 13 Class C LTC centres in Ontario and is guaranteed by certain Canadian subsidiaries of Extendicare. As at December 31, 2018, Extendicare had letters of credit totalling $45.0 million issued under the RBC Credit Facility, of which $38.0 million secure our defined benefit pension plan obligations and the balance were issued in connection with obligations relating to recently acquired centres and those centres under development. The letter of credit to secure the pension plan obligations renews annually in May based on an actuarial valuation. The RBC Credit Facility has no financial covenants, but does contain normal and customary terms including annual re-appraisals of the centres that could limit the maximum amount available.

LONG-TERM DEBT MATURITIES AND WEIGHTED AVERAGE INTEREST RATES

The table below presents the principal, or notional, amounts and related weighted average interest rates by year of maturity, of the Company's long-term debt obligations as at December 31, 2018. The Company had an aggregate of $52.9 million drawn on construction loans at year end, which are repayable on demand and, in any event, are to be fully repaid by the earlier of achieving stabilized occupancy as defined by the agreements and specified dates between late 2019 and 2023. Consequently, these loans are reflected as current and due in 2019 in the following table. Permanent financing will be sought for each upon maturity.

(millions of dollars)	**2019**	**2020**	**2021**	**2022**	**2023**	**After 2023**	**Total**	**Fair Value**
Convertible debentures (at face value)								
Fixed rate	–	–	–	–	–	126.5	**126.5**	125.6
Average interest rate	–	–	–	–	–	5.00%	**5.00%**	
Long-term debt								
Fixed rate (including fixed through swap)	15.4	60.1	15.1	58.7	45.7	88.8	**283.8**	286.0
Average interest rate	4.23%	4.08%	4.29%	3.98%	4.54%	5.59%	**4.28%**	
Variable rate	52.9	–	–	–	–	–	**52.9**	52.9
Average interest rate	4.71%	–	–	–	–	–	**4.71%**	
Finance lease obligations								
Fixed rate	7.7	9.1	9.6	8.6	9.2	36.8	**81.0**	92.3
Average interest rate	6.15%	6.19%	6.22%	7.00%	7.01%	6.98%	**6.72%**	

Management has limited the amount of debt that may be subject to changes in interest rates, with all of the debt currently at fixed rates, other than the construction loans of $52.9 million. The Company's variable-rate mortgages on its retirement communities and the CIBC Term Loan, aggregating $84.8 million at year end, have effectively been converted to fixed rate financing with interest rate swaps over the full term. As at December 31, 2018, the net carrying value of the interest rate swaps was an asset of $2.0 million.

The following summarizes key metrics of our consolidated long-term debt as at December 31, 2018 and 2017.

	December 31, 2018	December 31, 2017
Weighted average interest rate of long-term debt outstanding	**4.9%**	5.0%
Weighted average term to maturity of long-term debt outstanding	**7.4 yrs**	7.1 yrs
Weighted average term to maturity of long-term debt outstanding, excluding finance lease obligations	**7.3 yrs**	6.7 yrs
Trailing twelve months consolidated net interest coverage ratio[(1)]	**3.7 X**	3.8 X
Trailing twelve months consolidated interest coverage ratio[(2)]	**3.2 X**	3.3 X
Debt to Gross Book Value (GBV)		
Total assets (carrying value)	**896,324**	934,281
Accumulated depreciation on property and equipment	**226,416**	214,889
Accumulated amortization on other intangible assets	**18,509**	12,229
GBV	**1,141,249**	1,161,399
Debt [(3)]	**544,111**	543,446
Debt to GBV	**47.7%**	46.8%

(1) Net interest coverage is defined as Adjusted EBITDA divided by net interest (interest expense before reduction of capitalized interest, net of interest revenue).

(2) Interest coverage is defined as Adjusted EBITDA divided by interest expense before reduction of capitalized interest.

(3) Debt includes convertible debentures at face value of $126.5 million, and excludes deferred financing costs.

Future Liquidity and Capital Resources

Extendicare's consolidated cash and short-term investments on hand was $65.9 million as at December 31, 2018, compared with $128.2 million at the beginning of the year, and excluded restricted cash of $2.3 million, and $67.9 million (US$49.8 million) of investments held by our Captive to support the accrual for U.S. self-insured liabilities of $37.1 million (US$27.2 million). In addition, the Company has $65.0 million available to draw under its ParaMed Credit Facility.

The Company has three unencumbered retirement communities (Lynde Creek, West Park and Yorkton). In addition, construction financings in the aggregate of up to $77.7 million have been secured on the three retirement communities that were under construction during 2018 (Douglas Crossing, Bolton and Barrie), of which $43.9 million was drawn at year end. As at December 31, 2018, the Company had incurred approximately $79.8 million of the estimated $104.9 million of Adjusted Development Costs for these three retirement communities.

Management believes that cash from operating activities and future debt financings will be available and sufficient to support Extendicare's ongoing business operations, maintenance capex, and debt repayment obligations. Growth through redevelopment of our LTC centres over the next few years, strategic acquisitions and developments will necessitate the raising of funds through debt financings and the capital markets. Decisions will be made on a specific transaction basis and will depend on market and economic conditions at the time.

OTHER CONTRACTUAL OBLIGATIONS AND CONTINGENCIES

The table below provides summary information relating to the contractual obligations, other than long-term debt, as at December 31, 2018. Due to the uncertainty as to the timing of payments to be made with respect to certain obligations, the table excludes the accrual for U.S. self-insured liabilities of $37.1 million and the decommissioning provisions of $9.4 million. In addition, the table excludes our defined benefit pension plan obligations, which are described more fully below.

(millions of dollars)	2019	2020	2021	2022	2023	After 2023	Total
Operating lease obligations	3.5	1.7	1.4	1.0	0.3	–	**7.9**
Purchase obligations	16.0	–	–	–	–	–	**16.0**
	19.5	1.7	1.4	1.0	0.3	–	**23.9**

Defined Benefit Pension Plan Obligations

The contractual obligations table excludes our defined benefit pension plan obligations. The accrued benefit liability on our statement of financial position as at December 31, 2018 was $36.1 million (2017 – $36.6 million). We currently have defined benefit registered and supplementary plans covering certain executives, both of which have been closed to new entrants since 2000. The registered defined benefit plan was in an actuarial deficit of $2.6 million with plan assets of $5.1 million and accrued benefit obligations of $7.7 million at year end (2017 – an actuarial deficit of $2.5 million with plan assets of $5.4 million and accrued benefit obligations of $7.9 million). The accrued benefit obligations of the supplementary plan were $33.5 million at year end (2017 – $34.1 million). We do not set aside assets in connection with the supplementary plan and the benefit payments will be paid from cash from operations. The benefit obligations under the supplementary plan are secured by a letter of credit totalling $38.0 million as at December 31, 2018 (2017 – $39.9 million). This letter of credit renews annually in May based on an actuarial valuation of the pension obligations. The annual benefit payments under the supplementary pension plan to be funded from cash from operations over the next five years are expected to be in the range of $2.0 million to $2.2 million, and the annual contributions to the registered pension plan over the next five years are expected to be less than $0.1 million. Since the majority of our accrued benefit obligations represent our obligation under our non-registered supplementary plan, which is not required to be funded, changes in future market conditions are not expected to have a material adverse effect on our cash flow requirements with respect to our pension obligations, or on our pension expense.

Accrual for U.S. Self-insured Liabilities

The obligation to settle any U.S. self-insured general and professional liability claims relating to the period prior to the closing of the U.S. Sale Transaction, including claims incurred but yet to be reported, remains with Extendicare, which it intends to continue to fund through the Captive. Consequently, the balance of the accrual for self-insured liabilities and the related investments held for self-insured liabilities remain on the consolidated statement of financial position. However, any expense incurred or release of reserves for U.S. self-insured liabilities are presented as discontinued operations; while the Captive’s costs to administer and manage the settlement of the remaining claims are reported as continuing operations within the U.S. segment.

Management regularly evaluates and semi-annually engages an independent third-party actuary to provide a report to determine the appropriateness of the carrying value of this liability. The most recent independent actuarial review was conducted at the end of 2018, which confirmed the adequacy of our reserves.

As at December 31, 2018, the accrual for U.S. self-insured general and professional liabilities was $37.1 million (US$27.2 million) compared to $61.1 million (US$48.6 million) at the beginning of the year. The decline of US$21.4 million reflected claim payments of US$11.8 million, a release of reserves of $13.0 million (US$9.9 million) and an adjustment to the discount factor of US$0.9 million, partially offset by accretion of the discounted liability. Since the sale of the U.S. operations in 2015, US$29.6 million of the Captive’s reserves have been released and reflected in discontinued operations.

During 2017, payments for self-insured liabilities were $24.2 million (US$18.6 million) and $5.7 million (US$4.4 million) in reserves were released and reflected in discontinued operations.

Most of the risks that Extendicare self-insures are long-term in nature, and accordingly, claim payments for any particular policy year occur over a long period of time. However, management estimates and allocates a current portion of the accrual for self-insured liabilities on the statement of financial position. As at December 31, 2018, management estimated that approximately $12.3 million of the accrual for self-insured general and professional liabilities will be paid within the next year. The timing of payments is not directly within management’s control; therefore, estimates could change in the future.

The Captive holds investments sufficient to support the accrual for self-insured liabilities and to meet required statutory solvency and liquidity ratios. These invested funds are reported in other assets and totalled $67.9 million (US$49.8 million) as at December 31, 2018, compared to $86.3 million (US$68.6 million) at the beginning of the year. Since the sale of the U.S. operations in 2015, the Captive has transferred US$28.5 million of its funds previously held for investment to the Company for general corporate use, of which US$7.5 million was transferred in 2018 (2017 – US$16.0 million). Management believes there are sufficient invested funds held to meet estimated current claims payment obligations.

Legal Proceedings, Claims and Regulatory Actions

Extendicare and its consolidated subsidiaries are defendants in various actions and proceedings that are brought against them from time to time in connection with their operations.

As previously disclosed, in April 2018, the Company was served with a statement of claim alleging negligence by the Company in the operation of its long-term care centres and its provision of care to residents and seeking $150 million in damages. The claim sought an order certifying the claim as a class action pursuant to the *Class Proceedings Act* (Ontario). By order of the Ontario Superior Court of Justice the class proceeding was discontinued on October 25, 2018. Following the discontinuance, the plaintiff who commenced the class proceeding still has the option to pursue a claim on her own behalf while others may also do so separately on their own behalf. The Company intends to defend itself against any and all such individual claims and does not believe the outcome on any or all such claims would have a material adverse impact on its business, results of operations or financial condition and in any event believes that any potential liability would be resolved within the limits of its insurance coverage.

On September 19, 2018, the Company was served with a statement of claim that seeks an order certifying the claim as a class action pursuant to the *Class Proceedings Act* (Ontario). The claim alleges that the Company failed to properly apply certain required medical equipment sterilization protocols at one or more of its home health care clinics and seeks $20 million in damages. The Company does not believe that the lawsuit or the damages sought have merit. The Company intends to vigorously defend itself against the claim and does not believe the outcome will have a material adverse impact on its business, results of operations or financial condition and in any event believes that any potential liability would be resolved within the limits of its insurance coverage.

The provision of health care services is subject to complex government regulations. Every effort is made by the Company to prevent deficiencies in the quality of patient care through quality assurance strategies and to remedy any such deficiencies cited by government inspections within the applicable prescribed period of time. Extendicare accrues for costs that may result from investigations, or any possible related litigation, to the extent that an outflow of funds is probable and a reliable estimate of the amount of the associated costs can be made.

RELATED PARTY TRANSACTIONS

As previously announced, Extendicare's former President and Chief Executive Officer, Tim Lukenda stepped down from his position on October 22, 2018. In connection with his separation agreement, Mr. Lukenda was entitled to receive a cash payment in the amount of $2.9 million, and was required to forfeit, for no consideration, all of the performance share units (PSUs) credited to his account under the Company's long-term incentive plan. The terms of Mr. Lukenda's departure from the Company took into account the payments that Mr. Lukenda would have been entitled to receive upon a termination of his employment by the Company without cause or by the employee for good reason and a deduction based on the full amount of the $2.0 million cash retention bonus that was paid to Mr. Lukenda in September 2017. The Company reflected a charge in the 2018 third quarter for the cash payment of $2.9 million, partially offset by the reversal of $1.2 million in connection with the forfeiture of the PSUs.

During Mr. Lukenda's employment with Extendicare, the Company provided management services to a long-term care centre and group purchasing services to retirement centre owned by Mr. Lukenda and members of his family through a company in which Mr. Lukenda had an approximate 7.1% direct and indirect ownership interest. Mr. Lukenda's employment contract provided a mechanism and process that effectively removed him from the decision-making process in situations where a conflict of interest may have arisen on any matter between the two companies.

RISKS AND UNCERTAINTIES

The risks and uncertainties described below could adversely affect the business, results of operations and financial condition of Extendicare, cause the trading price of the Company's securities to decline and cause the actual outcome of matters to differ materially from the expectations of the Company regarding future results, performance or achievements reflected in information in this MD&A and other information provided by Extendicare from time to time. The risks and uncertainties described below, which is not an exhaustive description of the risks and uncertainties faced by Extendicare, should be carefully considered by investors.

General Business Risks

Extendicare is subject to general business risks inherent in the senior care industry, including: changes in government regulation and oversight; changing consumer preferences; fluctuations in occupancy levels and business volumes; changes in government funding and reimbursement programs, including the inability to achieve adequate government funding increases; increases in labour costs and other operating costs; changes in labour relations; competition from other senior care providers, including from, or the oversupply of, other similar centres; changes in neighbourhood or location conditions and general economic conditions; health related risks; disease outbreaks and control risks; changes in accounting principles and policies; the imposition of increased taxes or new taxes; capital expenditure requirements; changes in interest rates; and changes in the availability and cost of long-term financing, which may render refinancing of long-term debt difficult or unattractive. Any one of, or a combination of, these factors may adversely affect the business, results of operations and financial condition of the Company.

In addition, there are inherent legal, reputational and other risks involved in providing accommodation and health care services to seniors. The vulnerability and limited mobility of some seniors enhances such risks. Such risks include fires or other catastrophic events at a Company location which may result in injury or death, negligent or inappropriate acts by employees or others who come into contact with our residents and clients, and unforeseen events at locations at which the Company operates that result in damage to the Company's brand or reputation or to the industry as a whole.

Risks Related to Growth and Redevelopment Activities

The Company expects that it will continue to have opportunities to acquire businesses and properties, develop properties, redevelop or expand existing centres, and grow its home health care, private-pay retirement, management/consulting and group purchasing businesses, but there can be no assurance that this will be the case.

The number of licensed LTC beds are restricted by the provinces and any new licenses are awarded through a request for proposal process. The provinces also regulate the manner in which LTC centres are developed and redeveloped. If regulatory approvals are required in order to expand operations (via development or otherwise) or redevelop operations of the Company, the inability of the Company to obtain the necessary approvals, changes in standards applicable to such approvals and possible delays and expenses associated with obtaining such approvals could adversely affect the ability of the Company to expand or redevelop and, accordingly, to maintain or increase its revenue and earnings.

Approximately 40% of Extendicare's owned LTC beds are in older Ontario centres that are subject to redevelopment. Licenses for LTC centres in Ontario are issued for a fixed term of not more than 30 years, after which the license may or may not be renewed. LTC operators are to be notified of license renewals at least three years prior to the maturity date. Under the LTCHA, license terms for Class B and C LTC centres are set to expire in 2025 unless the centres are redeveloped to the government's new design standards. The significant backlog in demand for long-term care and the lack of alternative care environments makes it likely that licenses will be extended until redevelopment can be completed. The Company has 21 Class C LTC centres with 3,287 beds that it plans to redevelop under the government's enhanced redevelopment program (see "Ontario LTC Redevelopment Program" under the heading "Update of Regulatory and Funding Changes Affecting Results"). The extent to which such redevelopment plans are not implemented or proceed on significantly different timing or terms, including levels of expected government subsidy funding, could have an adverse effect on the business, results of operations and financial condition of the Company.

The success of the business acquisition and development activities of the Company, including the expansion of its private-pay retirement operations, will be determined by numerous factors, including the ability of the Company to identify suitable acquisition targets, competition for acquisition and development opportunities, purchase price, ability to obtain external sources of funding or adequate financing on reasonable terms, the financial performance of the businesses or centres after acquisition or development, and the ability of the Company to effectively integrate and operate the acquired businesses or centres. Acquired businesses or centres, and development projects, may not meet financial or operational expectations due to the possibility that the Company has insufficient management expertise to engage in such activities profitably or without incurring inappropriate amounts of risk, unexpected costs or delays associated with their acquisition or development, as well as the general investment risks inherent in any real estate investment or business acquisition. Moreover, new acquisitions may require significant management attention, place additional demands on the Company's resources, systems, procedures and controls, and capital expenditures that would otherwise be allocated by the Company in a different manner to existing businesses. Any failure by the Company to identify suitable candidates for acquisition, successfully complete development projects, secure financing, or operate the acquired and developed businesses effectively may have an adverse effect on the future growth, results of operations and financial condition of the Company.

The success of the Company’s ability to grow its management/consulting, group purchasing and home health care businesses, including the private-pay home health care segment, will be determined by numerous factors, including the ability of the Company to retain, renew and secure new contracts, identify suitable markets, develop competitive services and marketing and pricing strategies, attract and retain residents and clients, and hire, retain and motivate key personnel. Changes in government funding policies and regulatory changes, the risks related to which are described below under “Risks Related to Government Funding and Regulatory Changes”, in addition to the financial performance of these businesses, also impact Extendicare’s growth potential. Any failure by the Company to grow or operate its businesses effectively may have an adverse effect on the business, results of operations and financial condition of the Company.

Risks Related to Occupancy and Business Volumes

Senior care providers compete primarily on a local and regional basis with many other health care, long-term care and retirement living providers, including large publicly held companies, privately held companies, not-for-profit organizations, hospital-based LTC units, rehabilitation hospitals, home health care agencies, and rehabilitative therapy providers. Our ability to compete successfully varies from location to location and depends on a number of factors, including the number of competitors in the local market, the types of services available, our local reputation for quality care, the commitment and expertise of our staff, our local service offerings, the cost of care in each locality, and the physical appearance, location, age and condition of our centres. Increased competition could limit our ability to attract and retain residents and clients, maintain or increase occupancy levels and business volumes, and expand our business. An inability to continue to attract residents and clients could have an adverse effect on the business, results of operations and financial condition of the Company.

Risks Related to Government Funding and Regulatory Changes

Extendicare’s earnings are highly reliant on government funding and reimbursement programs, and the effective management of staffing and other costs of operations, which are strictly monitored by government regulatory authorities. See “Update of Regulatory and Funding Changes Affecting Results”. Given that the Company operates in a labour-intensive industry, where labour costs account for a significant portion of the Company’s operating costs (approximately 86% in 2018), government funding constraints, or funding enhancements that are not commensurate with increased costs, could have a significant adverse effect on the Company’s results from operations and cash flows. The Company is unable to predict whether governments will adopt changes in their funding and regulatory programs, and if adopted and implemented, the impact, if any, such changes will have on the Company’s business, results of operations and financial condition and the Company’s ability to grow.

Health care providers are subject to surveys, inspections, audits and investigations by government authorities to ensure compliance with applicable laws and licensure requirements of the various government funding programs. Long-term care operators and publicly funded home health care providers must comply with applicable regulations that, depending on the jurisdiction in which they operate, may relate to such matters as staffing levels, client care related operating standards, occupational health and safety, client confidentiality, billing and reimbursement, along with environmental and other standards. Retirement communities are also subject to extensive government regulation and oversight, licensure requirements and the potential for regulatory change. The government review process is intended to determine compliance with survey and certification requirements, and other applicable laws. Remedies for survey deficiencies can be levied based upon the scope and severity of the cited deficiencies.

The revocation of a license by authorities or the cancellation of a service contract due to inadequate performance by the operator has been historically infrequent and is usually preceded by a series of warnings, notices and other sanctions. The Company has never had such a license or service contract revoked in Canada.

Non-compliance with applicable laws and licensure requirements governing health care providers could result in adverse consequences, including severe penalties, which may include criminal sanctions and fines, civil monetary penalties and fines, administrative and other sanctions, including reimbursement of government funding, or exclusion from participation in government funded programs, or one or more third-party payor networks, and damage to our reputation. These penalties could have a material adverse effect on the business, results of operations and financial condition of the Company.

Every effort is made by the Company to prevent deficiencies in the quality of patient care through quality assurance strategies and to remedy any such deficiencies cited by government inspections within the applicable prescribed period of time. Extendicare accrues for costs that may result from investigations, or any possible related litigation, to the extent that an outflow of funds is probable and a reliable estimate of the amount of associated costs can be made; however, there can be no assurance that such accruals are accurate or sufficient.

With respect to home health care services, 98% of ParaMed's revenue is from contracts tendered by locally administered provincial agencies, at specified billing rates and, among other things, quality operating and performance standards. Home health care service providers must ensure their key performance indicators are meeting or exceeding provincial targets in order to continue to receive their allocated funding volumes and/or retain their contracts. Contracts with qualified service providers are generally awarded through a competitive bidding model. In Ontario, where 83% of ParaMed's business volumes were generated in 2018, the government implemented new open-ended contracts in 2012 that are evergreen contracts provided that the service provider remains in good standing. New contracts in Ontario are awarded under a bidding process to prequalified service providers. Under this new regime, all of ParaMed's government contracts in Ontario have remained in effect. In British Columbia and Alberta, where 11% and 4% of ParaMed's business volumes were generated in 2018, respectively, government contracts have specified termination dates and or/renewal periods, following which they are put out to tender. Any failure by ParaMed to retain its government contracts, including in connection with any regulatory or other funding changes, may have an adverse effect on the business, results of operations and financial condition of the Company.

Risks Related to Dependence on Key Personnel

The success of the Company depends, to a significant extent, on the efforts and abilities of its executive officers and other members of management, as well as its ability to attract and retain qualified personnel to manage existing operations and future growth. Although the Company has entered into employment agreements with certain of its key employees, it cannot be certain that any of these individuals will not voluntarily terminate his or her employment with the Company. The loss of an executive officer or other key employee could negatively affect the Company's ability to develop and pursue its business strategy, which could have a material adverse effect on the business, results of operations and financial condition of the Company.

CONFLICTS OF INTEREST

Extendicare's Board of Directors may, from time to time, in their individual capacities deal with parties with whom Extendicare may be dealing, or may be seeking investments similar to those desired by Extendicare. The relevant constating documents of the Company contain conflict of interest provisions requiring the Directors to disclose material interests in material contracts and transactions and to refrain from voting thereon.

Risks Related to Labour Intensive Business

PERSONNEL COSTS

The senior care industry is labour intensive, with approximately 86% of the Company's operating costs represented by labour costs. The Company competes with other health care providers in attracting and retaining qualified and skilled personnel to manage and operate the day-to-day operations of each of its centres and home health care services. The health care industry continues to face shortages of qualified personnel, such as nurses, certified nurse's assistants, nurse's aides, and therapists. This shortage along with general inflationary pressures may require the Company to enhance its pay and benefits package to compete effectively for qualified personnel. The Company may not be able to recover such added costs through increased government funding and reimbursement programs, or through increased rates charged to residents and clients. The inability to retain and/or attract qualified personnel and meet minimum staffing levels may result in: a reduction in occupancy levels and volume of services provided; the use of staffing agencies at added costs; an increased risk in the inability to provide continuity of care between the Company's staff and its residents and clients; and an increased risk of the Company being subject to fines and penalties. An increase in personnel costs or a failure to attract, train and retain qualified and skilled personnel could adversely affect the business, results of operations and financial condition of the Company.

The Company has contracted out selected dietary and housekeeping services provided in some of its centres. Should the Company become dissatisfied with the quality or cost of such contracted services, it may have to terminate the related contracts and recruit replacement staff at an incremental cost.

WORKPLACE HEALTH AND SAFETY

The Company recognizes that ensuring a healthy and safe workplace minimizes injuries and other risks its employees may face in carrying out their duties, improves productivity and helps to minimize any liability or penalties which could be incurred in connection with workplace injuries. The Company has health and workplace safety programs in place and has established policies and procedures aimed at ensuring compliance with applicable legislative requirements. Failure to comply with appropriate and established workplace health and safety policies and procedures or applicable legislative requirements could result in increased workplace injury-related liability and penalties, which in turn could adversely affect the reputation of the Company and have a material adverse effect on the business, results of operations and financial condition of the Company.

LABOUR RELATIONS

The Company employs approximately 23,000 persons, of whom approximately 68% are represented by labour unions. Labour relations with the unions are governed by numerous collective bargaining agreements with different unions. Upon expiration of the collective bargaining agreements, the Company may not be able to negotiate collective agreements on satisfactory terms. There can be no assurance that the Company will not at any time, whether in connection with the renegotiation of a collective bargaining agreement or otherwise, experience strikes, labour stoppages or any other type of conflict with unions or employees which could have a material adverse effect on the Company's business, operating results and financial condition. The centres that Extendicare operates are generally subject to legislation that prohibits both strikes and lock-outs, and requires compulsory arbitration to settle labour disputes. In jurisdictions where strikes and lockouts are permitted, certain essential services regulations apply which provide for the continuation of resident care and most services.

Non-unionized employees of the Company may become unionized if they are targeted for certification by a trade union. There can be no assurance that employees who are not currently unionized will not, in the future, be subject to unionization efforts, the result of which could increase the Company's labour costs, which could have a material adverse effect on the business, results of operations and financial condition of the Company.

Risks Related to Liability and Insurance

Operating in the senior care industry exposes Extendicare to an inherent risk of wrongful death, personal injury, professional malpractice and other potential claims brought by the Company's residents, clients, and employees. From time to time, Extendicare is subject to lawsuits alleging, among other claims, that the Company did not properly treat or care for a client or resident, that the Company failed to follow internal or external procedures that resulted in harm to a client or resident, or that the Company's employees mistreated the Company's residents or clients resulting in harm. In addition, attempts to advance class action lawsuits have become prevalent in the Canadian marketplace, including senior care. There can be no assurance that Extendicare will not face risks of this nature. Refer to the "Legal Proceedings, Claims and Regulatory Actions" heading under the "Other Contractual Obligations and Contingencies" section of this MD&A for further details.

Extendicare maintains business and property insurance policies in amounts and with such coverage and deductibles as deemed appropriate, based on the nature and risks of the business, historical experience and industry standards.

There can be no assurance, however, that claims in excess of the insurance coverage, or in excess of the Company's reserves, or claims not covered by the insurance coverage will not arise or that the liability coverage will continue to be available on acceptable terms. Furthermore, there are certain types of risks, generally of a catastrophic nature, such as war, non-certified acts of terrorism, or environmental contamination, which are either uninsurable or are not insurable on an economically viable basis. A successful claim against the Company not covered by, or in excess of, such insurance, or in excess of the Company's reserves for self-insured retention levels, could have a material adverse effect on the business, results of operations and financial condition of the Company. Claims against the Company, regardless of their merit or eventual outcome, may also have a material adverse effect on the ability of the Company to attract residents and clients, expand the business of the Company or maintain favourable standings with regulatory authorities.

Prior to the U.S. Sale Transaction, Extendicare self-insured certain risks related to general and professional liability of its disposed U.S. business through the Captive, its Bermuda-based captive insurance company. The obligation to settle any such claims relating to the period prior to the closing of the U.S. Sale Transaction, including claims incurred but yet to be reported, remains with Extendicare, which it intends to continue to fund through the Captive.

Risks Related to Privacy of Client Information and Cyber Security

As a custodian of a large amount of personal information, including health information, relating to its residents, clients and employees, Extendicare is exposed to the potential loss, misuse or theft of any such information. If the Company were found to be in violation of the federal and provincial laws protecting the confidentiality of patient health information, it could be subject to sanctions and civil or criminal penalties, which could increase its liabilities, harm its reputation and have a material adverse effect on the business, results of operations and financial condition of the Company. In addition, cyber attacks against large organization are increasing in sophistication and are often focused on financial fraud, compromising sensitive data for inappropriate use or disrupting business operations. Extendicare mitigates this risk by deploying appropriate information technology systems, including controls around logical access, physical access and data management, and training its employees relating to safeguarding of sensitive information.

Extendicare has deployed operational technology solutions enabling process automation, electronic health record data collection and automated business intelligence. Technology deployments also present security and privacy risks that must be managed proactively and effectively to prevent breaches that can have an adverse impact on Extendicare's reputation and results of operations. To counter internet-based and internal security threats, Extendicare also deploys leading edge solutions to identify risks to its network, software and hardware systems. Extendicare partners with leading technology security firms to mitigate identified risks and develop contingency plans. As security threats to Extendicare's financial, client and employee data increase and evolve, the Company adjusts and adopts new counter-measures in an effort to ensure it maintains high privacy and security standards.

Although to date the Company has not experienced any material losses relating to cyber attacks or other information security breaches, there can be no assurance that the Company will not incur such losses in the future. The Company's risk and exposure to these matters cannot be fully mitigated because of, among other things, the evolving nature of these threats. As cyber threats continue to evolve, the Company may be required to expend additional resources to continue to modify or enhance protective measures or to investigate and remediate any security vulnerabilities.

Risks Related to Tax Rules and Regulations

Extendicare is subject to audits from federal, state and provincial tax jurisdictions and is therefore subject to risk in the interpretation of tax legislation and regulations. Tax rules and regulations are complex and require careful review by the Company's tax management and its external tax consultants. Differences in interpretation of tax rules and regulations could result in tax assessments and penalties for the untimely payment of the determined tax liability, which could have a material adverse effect on the business, results of operations and financial condition of the Company.

Risks Related to Financing

DEBT FINANCING

Due to the level of real property ownership by the Company, a significant portion of the consolidated cash flow of the Company is devoted to servicing debt, and there can be no assurance that the Company will continue to generate sufficient cash flow from operations to meet required interest and principal payments. If the Company were unable to meet its required interest or principal payments, it could be required to seek renegotiation of such payments or obtain additional equity, debt or other financing.

Extendicare's RBC Credit Facility is a demand facility in the amount of $47.3 million that is secured by 13 Class C graded LTC centres in Ontario and is guaranteed by certain Canadian subsidiaries of the Company. As at December 31, 2018, Extendicare had letters of credit totalling $45.0 million issued under the RBC Credit Facility, of which $38.0 million secured our defined benefit pension plan obligations. The RBC Credit Facility has no financial covenants but contains normal and customary terms including annual re-appraisals of the centres that could limit the maximum level of the line of credit and other restrictions on Extendicare's subsidiaries making certain payments, investments, loans and guarantees. A demand for repayment of amounts drawn on the line of credit could inhibit the flow of cash dividends by Extendicare on a temporary basis until alternative financing is obtained.

The Company cannot predict whether future financing will be available, what the terms of such future financing will be (including, whether it will result in a higher cost of borrowing) or whether its existing debt agreements will allow for the timely arrangement and implementation of such future financing. If the Company were unable to obtain additional financing or refinancing when needed or on satisfactory terms, it could have a material adverse effect on the business, results of operations and financial condition of the Company.

DEBT COVENANTS

The Company is in compliance with all of its financial covenants as at December 31, 2018. However, there can be no assurance that future covenant requirements will be met. The Company's bank lines and other debt may be affected by its ability to remain in compliance. If the Company does not remain in compliance with its financial covenants, its ability to amend the covenants or refinance its debt may be affected.

INTEREST RATES

The Company has limited the amount of debt that may be subject to changes in interest rates. All of the Company's long-term debt is at fixed rates, other than its construction loans that had an aggregate balance of $52.9 million drawn as at December 31, 2018. The Company primarily finances its senior care and living centres through fixed-rate mortgages and considers securing interest rate swap agreements for any variable-rate debt. The Company's variable-rate mortgages on its retirement communities and the CIBC Term Loan, aggregating $84.8 million as at December 31, 2018, have effectively been converted to fixed rate financings with interest rate swaps over the full term. The Company maintains risk management control systems to monitor interest rate risk attributable to its outstanding or forecasted debt obligations as well as any offsetting hedge positions. The Company does not enter into financial instruments for trading or speculative purposes.

Risks Related to Real Property Ownership

REAL PROPERTY OWNERSHIP

All real property investments are subject to a degree of risk. They are affected by various factors, including geographic concentration, changes in general economic conditions (such as the availability of long-term mortgage funds) and in local conditions (such as an oversupply of space or a reduction in demand for real estate in the area), the attractiveness of the properties to residents, competition from other available space and various other factors. In addition, fluctuations in interest rates could have a material adverse effect on the business, results of operations and financial condition of the Company.

Extendicare owns, or operates under finance lease arrangements whereby ownership transfers at the end of the lease term, 100% of its senior care and living centres, excluding those centres operated under management contracts. Senior care and living centres are limited in terms of alternative uses; therefore, their values are directly driven by the cash flow from operations. All but nine of the Company's sixty-seven centres owned by it at December 31, 2018, are government-funded senior care centres. The value of the real property depends, in part, on government funding, license terms, and reimbursement programs. In addition, overbuilding in any of the market areas in which the Company owns or operates senior care and living centres could cause these centres to experience decreased occupancy or depressed margins, which could have a material adverse effect on the business, results of operations and financial condition of the Company. Moreover, certain significant expenditures relating to real property ownership, such as real estate taxes, maintenance costs and mortgage payments, represent liabilities that must be met regardless of whether the property is producing any income.

Real property investments are relatively illiquid, thereby limiting the ability of the Company to vary its portfolio in a timely manner in response to changed economic or investment conditions. By specializing in long-term care and retirement living centres, the Company is exposed to adverse effects on these segments of the real estate market. There is a risk that the Company would not be able to sell its real property investments or that it may realize sale proceeds below their current carrying value.

CAPITAL INTENSIVE INDUSTRY

The Company must commit a substantial portion of its funds to maintain and enhance its senior care and living centres and equipment to meet regulatory standards, operate efficiently and remain competitive in its markets. During 2018, the company incurred $12.7 million in maintenance capex, and expects to spend in the range of $10 million to $12 million in 2019 to sustain and upgrade its existing centres. In addition to recurring maintenance capex, the Company invests in enhancements of existing centres aimed at earnings growth and improved profitability, including redevelopment of centres under provincial programs. See "Risks and Uncertainties – Risks Related to Growth and Redevelopment Activities ". These, as well as other future capital requirements, could adversely impact the amount of cash available to the Company and have a material adverse effect on the business, results of operations and financial condition of the Company.

Risks Related to Environmental, Health and Safety Laws

The Company is subject to various environmental, health and safety laws and regulations, both as an owner of real property and as a provider of health care services, governing the storage, handling, use, and disposal of equipment, materials and waste products. The Company may become liable for the costs of removal or remediation of certain hazardous, toxic, or regulated substances present at, released on or disposed of from its properties or other service locations, regardless of whether or not the Company knew of, or was responsible for, their presence, release or disposal. The failure to remove, remediate, or otherwise address such substances, if any, may adversely affect operations or the ability to sell such properties or to borrow using such properties as collateral, and could potentially result in claims by public or private parties, including by way of civil action.

With respect to the Company's pre-1980 properties, management has determined that future costs could be incurred for possible asbestos remediation at these sites. Appropriate remediation procedures may be required to remove potential asbestos-containing materials, consisting primarily of floor and ceiling tiles, in connection with any major renovation or demolition. Based upon current assumptions, the estimated fair value of the decommissioning provision related to the asbestos remediation was approximately $11 million undiscounted, or $9.4 million discounted, as at December 31, 2018, refer to *note 11* of the audited consolidated financial statements.

Environmental, health and safety laws may change and the Company may become subject to more stringent laws in the future. Compliance with more stringent environmental, health and safety laws, which may be more rigorously enforced, could have a material adverse effect on the business, results of operations and financial condition of the Company.

ACCOUNTING POLICIES AND ESTIMATES

Critical Accounting Policies and Estimates

A full discussion of Extendicare's critical accounting policies and estimates is provided in *note 3* of the audited consolidated financial statements for the year ended December 31, 2018, and under the heading "Future Changes in Accounting Policies" that follows this section.

Management considers an understanding of Extendicare's accounting policies to be essential to an understanding of its financial statements because their application requires significant judgement and reliance on estimations of matters that are inherently uncertain, which affect the application of the accounting policies and reported amounts. Estimates and underlying assumptions are reviewed on an ongoing basis giving consideration to past experience and other factors that management believes are reasonable under the circumstances. Accordingly, actual results could differ from those estimated. The estimates and assumptions, which have a significant risk of causing a material adjustment to the carrying amount of assets and liabilities, are discussed below.

VALUATION OF PURCHASE PRICE ALLOCATION FOR ACQUISITIONS

Fair value is the price that would be received when selling an asset, or paid when transferring a liability in an orderly transaction (that is other than in a forced or liquidation sale) between market participants at the measurement date under current market conditions. The fair value measurement is based on the presumption that the transaction takes place either: in the principal market for the asset or liability; or in the absence of a principal market, in the most advantageous market for the asset or liability. The principal or the most advantageous market must be accessible by the Company.

The fair value of an asset or a liability is measured using the assumptions that market participants would use when pricing the asset or liability assuming that market participants act in their economic best interests. The Company uses valuation techniques that are appropriate in the circumstances and for which sufficient data are available to measure fair value, maximizing the use of relevant observable inputs and minimizing the use of unobservable inputs. The techniques used to estimate future cash flows will vary from one situation to another depending on the circumstances surrounding the asset or liability in question. Management assesses fair value based on estimated discounted cash flow projections and available market information (including the historical operating results and anticipated trends, local markets and economic conditions).

As discussed below under the heading "Valuation of Cash Generating Units and Impairment", an impairment loss is recognized when the carrying amount of an asset is not recoverable. The impairment loss is determined as the excess of the carrying value over its estimated recoverable amount.

Intangible assets with indefinite lives are also required to be assessed at a minimum annually, comparing the estimated recoverable amount to the carrying value to determine if an impairment loss is required to be recognized.

VALUATION OF CASH GENERATING UNITS AND IMPAIRMENT

Non-financial assets consist of property and equipment, intangible assets with finite lives, intangible assets with indefinite lives and goodwill. Property and equipment represents approximately 57% of the Company's total assets as at December 31, 2018, and goodwill and other intangibles represent approximately 11%. A CGU is defined to be the smallest group of assets that generates cash inflows from continuing use that is largely independent of the cash inflows of other assets. The Company has identified the home health care segment and each individual LTC centre and retirement community as a CGU.

Goodwill and indefinite-life intangibles are tested annually, except in the year of acquisition, and other assets are assessed for impairment when indicators of impairment exist. If any such indication exists, then the asset's recoverable amount is reassessed. For goodwill, and intangible assets that have indefinite useful lives or that are not yet available for use, the recoverable amount is estimated annually at the same time or more frequently if warranted. An impairment loss is recognized in net earnings if the carrying amount of an asset or its related CGU, or group of assets on the same basis as evaluated by management, exceeds its estimated recoverable amount. The recoverable amount of an asset or a CGU is the greater of its value in use and its fair value less costs to sell.

The determination of recoverable amounts can be significantly impacted by estimates related to current market valuations, current and future economic conditions in the geographical markets of each CGU, and management's strategic plans within each of its markets. Estimates and assumptions used in the determination of any impairment loss are based upon information that is known at the time, along with future outlook. When impairment tests are performed, the estimated useful lives of the assets are reassessed, with any change accounted for prospectively. Actual results can differ from these estimates, and can have either a positive or negative impact on the estimate, and impact whether an impairment situation exists.

In 2018, the Company performed the impairment assessment of its operations and recognized a pre-tax impairment charge of property and equipment in the amount of $16.2 million in respect of certain of its Saskatchewan retirement communities ($15.9 million) and of its LTC centres ($0.3 million). In 2017, the Company performed the impairment assessment of its operations and determined there was no impairment.

VALUATION OF INDEMNIFICATION PROVISIONS

As a result of the U.S. Sale Transaction, the Company has indemnified certain obligations of its former U.S. operations related to tax, a corporate integrity agreement, and other items. As at December 31, 2018, the remaining provisions totalled $13.7 million or US$10.1 million (2017 – $22.7 million or US$18.0 million) and an indemnification receivable of $2.0 million (2017 – $2.8 million). The estimates of these items are assessed every reporting period based on management's best estimate of the ultimate costs or recovery of such items, and any changes to the estimates are reflected as part of other expense in the results of discontinued operations. During 2018, favourable changes to the indemnifications totalled $3.8 million (2017 – unfavourable changes of $4.8 million), refer to *note 22* of the audited consolidated financial statements. Actual results can differ materially from the estimates made due to a number of factors including the assumptions used by management and other market forces.

SELF-INSURED LIABILITIES OF DISCONTINUED OPERATIONS

The obligation to settle any U.S. self-insured general and professional liability claims relating to the period prior to the July 2015 closing of the U.S. Sale Transaction, including claims incurred but yet to be reported, remains with Extendicare, which it intends to continue to fund through the Captive. The accrual for U.S. self-insured liabilities of our former U.S. operations is based on management's best estimate of the ultimate cost to resolve general and professional liability claims. The Company estimates the value of losses that may occur within its self-insured retention levels, based upon individual assessment of the settlement, using historical information and industry data, supported by actuarial projections, advice from legal counsel, consultants and external risk management. Actual results can differ materially from the estimates made due to a number of factors including the assumptions used by management and other market forces.

Management regularly evaluates and periodically engages an independent third-party actuary to provide a report to determine the appropriateness of the carrying value of this liability. Assumptions underlying the determination of the liability are limited by the uncertainty of predicting future events and assessments regarding expectations of several factors. Such factors include, but are not limited to: the frequency and severity of claims, which can differ materially by jurisdiction; trends in claims along with unique and identifiable settlements; the effectiveness of the claims management process; and the outcome of litigation. Therefore, management's estimate of the accrual for general and professional liability claims is significantly influenced by assumptions that are subject to judgement by management and the actuary, which may cause the expense to fluctuate significantly from one reporting period to another. Differences between the ultimate claims costs and our historical expense for loss and actuarial assumptions and estimates could have a material adverse effect on our business, results of operations and financial condition.

As at December 31, 2018, the accrual for self-insured general and professional liabilities was $37.1 million or US$27.2 million (2017 – $61.1 million or US$48.6 million) supported by investments held by the Captive of $67.9 million or US$49.8 million (2017 – $86.3 million or US$68.6 million). Changes in the level of retained risk and other significant assumptions that underlie management's estimates could have a material effect on the future carrying value of the self-insured liabilities. For example, a 1% variance in the accrual for U.S. self-insured liabilities at December 31, 2018, would have impacted our net earnings from discontinued operations by approximately $0.4 million (US$0.3 million). For further information refer to the discussion under the heading "Other Contractual Obligations and Contingencies – Accrual for U.S. Self-Insured Liabilities".

TAX UNCERTAINTIES

Tax uncertainties are evaluated on the basis of whether it is more likely than not that a tax position will ultimately be sustained upon examination by the relevant taxing authorities. Tax uncertainties are measured using a probability adjusted or expected value model whereby amounts are recorded if there is any uncertainty about a filing position, determined by multiplying the amount of the exposure by the probability that the entity's filing position will not be sustained. The assessment of tax uncertainties relies on estimates and assumptions and may involve a series of judgements about future events. New information may become available that causes the Company to change its judgement regarding the adequacy of existing tax liabilities. Such changes to tax liabilities will impact tax expense in the period that such a determination is made.

DEFERRED TAX ASSETS AND LIABILITIES

The Company uses the asset and liability method of accounting for deferred income taxes, which takes into account the differences between financial statement treatment and tax treatment of certain transactions, assets and liabilities. Deferred tax assets and liabilities are recognized to reflect the expected future tax consequences attributed to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax values as well as available tax loss carryforwards. Deferred tax assets and liabilities are measured using the substantively enacted tax rates anticipated to apply in the periods that the temporary differences are expected to be recovered or settled. In assessing whether the deferred tax assets are realizable, management considers whether it is probable (which the Company has defined as "more likely than not") that some portion or all of the deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income during the periods in which those temporary differences become deductible. Management considers the scheduled reversal of deferred tax liabilities, projected future taxable income and tax planning strategies in making this assessment. As at December 31, 2018, the Company had recognized deferred tax assets totalling $9.7 million (2017 – $13.9 million). Management believes that it is more likely than not that the Company will realize the benefits of these deductible differences. In addition, as at December 31, 2018, there were capital losses available for Canadian income tax purposes of $42.1 million (2017 – $16.5 million) that have not been tax benefited and are available indefinitely to apply against future capital gains.

New Accounting Policies Adopted

The following new standards were adopted effective January 1, 2018, and have been applied in preparing the financial results for the year ended December 31, 2018. These accounting standards are summarized below, and are more fully described in *note 4* of the audited consolidated financial statements.

REVENUE RECOGNITION

IFRS 15 "Revenue from Contracts with Customers" provides a single model and two approaches to recognizing revenue: at a point in time or over time. IFRS 15 also includes additional disclosure requirements for revenue accounted for under the standard. The standard applies to contracts with customers, excluding contracts within the scope of the standard on leases. Under IFRS 15, revenue is recognized when a customer obtains control of the goods or services. The Company adopted IFRS 15 using the cumulative effect method, which does not require restatement of comparative information. Adoption of the standard did not result in material changes to the timing or measurement of revenue recognition, and therefore, there was no cumulative effect adjustment recorded to accumulated deficit on January 1, 2018. However, under the new standard, accommodation revenue recognized under IAS 17 "Leases" is disclosed separately from services revenue recognized under IFRS 15 (refer to *note 29* of the audited consolidated financial statements).

FINANCIAL INSTRUMENTS

IFRS 9 "Financial Instruments" (IFRS 9) addresses the recognition, classification and measurement (including impairment) of financial assets and financial liabilities. This standard replaces IAS 39 "Financial Instruments: Recognition and Measurement".

Under IFRS 9, financial assets are classified based on the business model in which they are managed and the characteristics of their contractual cash flows. Financial assets are classified as measured at fair value through profit or loss (FVTPL), fair value through other comprehensive income (FVOCI), or amortized cost. The new standard eliminates the previous categories for financial assets held to maturity, loans and receivables and available for sale. There are no changes in the measurement basis of financial assets and liabilities upon adoption of IFRS 9, and therefore, there are no differences in carrying amounts.

In addition, IFRS 9 replaces the current "incurred loss" impairment model with a new "expected credit loss" model, which requires timely recognition of expected credit losses. The Company has elected to use the simplified approach and calculates impairment loss on accounts and notes receivable as lifetime expected credit loss.

The Company adopted this standard retrospectively with no restatement of prior periods. There was no material impact on adoption of the standard with the exception of a reclassification of $4.3 million from opening accumulated other comprehensive income to opening accumulated deficit, as investments held for U.S. self-insured liabilities were classified as FVTPL under IFRS 9. These investments include equity securities as well as money market funds that do not have contractual cash flows that are solely payments of principal and interest on the principal amount outstanding; therefore, they are classified as measured at FVTPL under IFRS 9.

Future Changes in Accounting Policies

The following new standard and interpretation are effective for future annual periods, and have not been applied in preparing the financial results for the year ended December 31, 2018. These are summarized below, and are more fully described in *note 5* of the audited consolidated financial statements.

LEASES

In January 2016, the IASB published IFRS 16 "Leases". The new standard requires a lessee to recognize assets and liabilities for all leases with a term of more than 12 months, unless the underlying asset is of low value, using a single model, thereby eliminating the distinction between operating and finance leases. As a lessee, the Company will recognize new assets and liabilities for its operating leases. In addition, the nature and timing of expenses related to those leases will change as IFRS 16 replaces the straight-line operating lease expense with a depreciation charge for right-of-use assets and interest expense on lease liabilities. IFRS 16 is effective for periods beginning on or after January 1, 2019, with earlier adoption permitted if IFRS 15 "Revenue from Contracts with Customers" has also been applied. The Company has assessed the impact of this new standard and its adoption is not expected to have a material impact on the consolidated financial statements. A retrospective adjustment to opening retained earnings is not expected. Based on the operating leases as at January 1, 2019, the Company will recognize a right-of-use asset and lease liability ranging between $7 million and $9 million, using a simplified approach where the asset and liability would be identical.

INCOME TAXES

On June 7, 2017, the IASB issued IFRIC Interpretation 23 "Uncertainty over Income Tax Treatments". The Interpretation provides guidance on the accounting for current and deferred tax liabilities and assets in circumstances in which there is uncertainty over income tax treatments. The interpretation is applicable for annual periods beginning on or after January 1, 2019. The Company intends to adopt the Interpretation in its financial statements for the annual period beginning on January 1, 2019. The adoption of the IFRIC Interpretation 23 is not expected to have a material impact on the consolidated financial statements.

Disclosure Controls and Procedures

Management is responsible for establishing and maintaining a system of disclosure controls and procedures (DC&P) to provide reasonable assurance that all material information relating to the Company is gathered and reported to senior management, including the Chief Executive Officer (CEO) and Chief Financial Officer (CFO), on a timely basis so that appropriate decisions can be made regarding public disclosure.

An evaluation of the effectiveness of the DC&P was conducted as at December 31, 2018, by management under the supervision of the Company's CEO and CFO. Based on this evaluation, the CEO and CFO have concluded that the Company's disclosure controls and procedures, as defined by National Instrument 52-109, *Certification of Disclosures in Issuers' Annual and Interim Filings*, were effective as at December 31, 2018.

Internal Control over Financial Reporting

Management is also responsible for establishing and maintaining adequate internal controls over financial reporting (ICFR) to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial reports for external purposes in accordance with IFRS.

Management, under the supervision of the Company's CEO and CFO, has evaluated the effectiveness of our ICFR using the 2013 Integrated Control framework as published by the Committee of Sponsoring Organizations of the Treadway Commission. Based on this evaluation, management has concluded that our ICFR were effective and that there were no material weaknesses in the Company's ICFR as at December 31, 2018.

In designing such controls, it should be recognized that due to inherent limitations, any controls, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives and may not prevent or detect misstatements. Additionally, management is required to use judgement in evaluating controls and procedures.