

Xtraction Services Holdings Corp.

Financial Statements

For the Three and Nine Months ended September 30, 2019 and 2018

(Unaudited)

(Expressed in United States Dollars)

Xtraction Services Holdings Corp.

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NOTICE OF NO AUDITOR REVIEW OF CONDENSED INTERIM CONSOLIDATED FINANCIAL STATEMENTS

The accompanying unaudited condensed interim consolidated financial statements of the Company have been prepared by and are the responsibility of the Company's management.

The Company's independent auditor has not performed a review of these condensed interim consolidated financial statements, in accordance with standards established by CPA Canada for a review of interim financial statements by an entity's auditor.

Xtraction Services Inc.
Condensed statements of comprehensive loss
For the three and six months ended September 30, 2019 and 2018
(unaudited)
(Expressed in United States Dollars)

	Note	Three months ended September 30,		Nine months ended September 30,	
		2019	2018	2019	2018
Revenue	6	\$ 959,203	\$ 63,947	\$ 1,931,228	\$ 63,947
Cost of sales	7	837,999	242,216	2,023,110	455,833
Gross profit (loss)		121,204	(178,269)	(91,882)	(391,886)
Administrative expenses	7	543,120	1,490,721	2,928,831	1,979,011
Sales and marketing expenses	7	82,389	215,885	168,036	338,554
Impairment loss on servicing equipment	12	206,100	-	206,100	-
Loss from operations		(710,405)	(1,884,875)	(3,394,849)	(2,709,451)
Interest and finance income		(17,723)	-	(17,723)	-
Financing expense, net		187,110	137,774	630,559	279,128
Accretion expense		606,056	277,579	1,518,850	731,476
Listing expense	5	363,095	-	363,095	-
Change in fair value of derivative liabilities	15,16	(1,519,953)	-	1,297,324	-
Loss on sale of property, plant and equipment and servicing equipment	12,13	81,352	-	101,569	-
Loss before income tax		(410,342)	(2,300,228)	(7,288,523)	(3,720,055)
Income tax expense	19	-	-	975	-
Loss		<u>\$ (410,342)</u>	<u>\$ (2,300,228)</u>	<u>\$ (7,289,498)</u>	<u>\$ (3,720,055)</u>
Other comprehensive loss					
Unrealized loss on foreign currency translation		27,938	-	27,938	-
Comprehensive loss		<u>\$ (438,280)</u>	<u>\$ (2,300,228)</u>	<u>\$ (7,317,436)</u>	<u>\$ (3,720,055)</u>
Loss per share - basic and diluted ¹		<u>\$ (0.01)</u>	<u>\$ (0.07)</u>	<u>\$ (0.21)</u>	<u>\$ (0.14)</u>
Weighted average shares outstanding:					
Basic and diluted (post split)		<u>36,295,018</u>	<u>30,928,971</u>	<u>33,974,478</u>	<u>26,998,042</u>

Note to table:

1) In July 2018 the Company changed its status from a limited liability company to a corporation (note 1).

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

Xtraction Services Inc.
Condensed statements of financial position
As of September 30, 2019 and December 31, 2018
(Expressed in United States Dollars)

	<u>Note</u>	<u>(unaudited)</u> <u>September 30,</u> <u>2019</u>	<u>December 31,</u> <u>2018</u>
Assets			
<i>Current assets</i>			
Cash		4,943,151	534,148
Trade and other receivables, net	8	129,597	36,421
Finance lease receivables	9	626,529	-
Inventories	10	95,187	96,166
Prepaid and other current assets	11	<u>103,494</u>	<u>109,961</u>
<i>Total current assets</i>		5,897,958	776,696
<i>Non-current assets</i>			
Servicing equipment	12	\$ 1,540,894	\$ 2,479,196
Prepaid servicing equipment	12	1,956,363	2,770,397
Property, plant and equipment	13	8,371	65,678
Intangible asset	14	<u>485,026</u>	<u>599,900</u>
<i>Total non-current assets</i>		3,990,654	5,915,171
Total assets		<u>\$ 9,888,612</u>	<u>\$ 6,691,867</u>
Shareholders' equity and liabilities			
<i>Current liabilities</i>			
Loans and borrowings, short-term	16	1,100,000	7,658
Trade and other payables	17	110,258	210,267
Accrued expenses	18	402,272	219,418
Unearned revenue	6	15,375	1,021,917
Amounts due to related parties	21	951,995	118,654
Warrant derivative liabilities	15	462,830	50,031
Redeemable common stock	16	<u>650,000</u>	<u>650,000</u>
<i>Total current liabilities</i>		3,692,730	2,277,945
<i>Non-current liabilities</i>			
Loans and borrowings, long-term	16	2,421,614	4,216,627
Embedded derivative liabilities	16	<u>646,064</u>	<u>1,091,514</u>
<i>Total non-current liabilities</i>		3,067,678	5,308,141
Total liabilities		6,760,408	7,586,086
<i>Capital and reserves</i>			
Common stock	15	\$ 2,983	\$ 3,251
Proportionate voting common stock	15	18,096	-
Additional paid-in capital	15	16,639,263	5,317,232
Accumulated other comprehensive loss		(27,938)	-
Accumulated deficit		<u>(13,504,200)</u>	<u>(6,214,702)</u>
<i>Total shareholders' equity</i>		3,128,204	(894,219)
Total shareholders' equity and liabilities		<u>\$ 9,888,612</u>	<u>\$ 6,691,867</u>

Nature of operations and background information (Note 1)
Going concern (Note 3)
Subsequent events (Note 23)

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

Xtraction Services Inc.
Condensed statements of changes in equity
For the nine months ended September 30, 2019 and 2018
(unaudited)
(Expressed in United States Dollars)

	Note	Class A member units	Class B member units	Members' Capital	Common Stock		Proportionate Voting Shares	Additional paid-in capital	Accumulated OCI	Accumulated deficit	Total
					Shares	Amount					
Balance at January 1, 2018 ⁽¹⁾		25,000,000	-	\$ 2,188,822	-	\$ -	\$ -	\$ -	\$ -	\$ (375,057)	\$ 1,813,765
Fair value allocation of loan borrowing proceeds	16	-	-	1,410,526	-	-	-	230,103	-	-	1,640,629
Exchange of Class A member units to Class A common stock	15	(25,000,000)	-	(3,599,348)	25,000,000	2,500	-	3,596,848	-	-	-
Conversion of convertible debentures to Class A common stock	16	-	-	-	6,737,588	674	-	478,459	-	-	479,133
Issuance of Class A common stock	15	-	-	-	85,000	9	-	50,991	-	-	51,000
Issuance of Class B restricted units and common stock	15	-	1,098,586	-	678,650	68	-	407,122	-	-	407,190
Cancellation of Class B restricted units	15	-	(1,098,586)	-	-	-	-	-	-	-	-
Incentive compensation	20	-	-	-	-	-	-	260,458	-	-	260,458
Net loss		-	-	-	-	-	-	-	-	(3,720,055)	(3,720,055)
Balance at September 30, 2018		<u>-</u>	<u>-</u>	<u>\$ -</u>	<u>32,501,238</u>	<u>3,251</u>	<u>-</u>	<u>\$ 5,023,981</u>	<u>\$ -</u>	<u>\$ (4,095,112)</u>	<u>\$ 932,120</u>
Balance at January 1, 2019		-	-	\$ -	32,501,238	3,251	-	\$ 5,317,232	\$ -	\$ (6,214,702)	\$ (894,219)
Issuance of Class A common stock	15	-	-	-	757,500	75	-	626,798	-	-	626,873
Fair value allocation of loan borrowing proceeds	16	-	-	-	-	-	-	260,745	-	-	260,745
Issuance of Proportionate Voting Shares	15	-	-	-	(17,737,588)	(1,774)	17,737	(15,963)	-	-	-
Shares issued to Caracara shareholders	15	-	-	-	3,896,598	390	-	952,778	-	-	953,167
Conversion of Series B and Series C debentures to common stock	15	-	-	-	10,050,378	1,005	359	8,769,030	-	-	8,770,394
Conversion of Sub Receipt debentures to common stock	15	-	-	-	363,636	36	-	264,661	-	-	264,697
Incentive compensation	20	-	-	-	-	-	-	463,983	-	-	463,983
Net loss		-	-	-	-	-	-	-	(27,938)	(7,289,498)	(7,317,436)
Balance at September 30, 2019		<u>-</u>	<u>-</u>	<u>\$ -</u>	<u>29,831,762</u>	<u>\$ 2,983</u>	<u>\$ 18,096</u>	<u>\$ 16,639,263</u>	<u>\$ (27,938)</u>	<u>\$ (13,504,200)</u>	<u>\$ 3,128,204</u>

Note to table:

1) In March 2018 the Company had a 25 for 1 unit split (note 15).

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

Xtraction Services Inc.
Condensed statements of cash flows
For the three and six months ended September 30, 2019 and 2018
(unaudited)
(Expressed in United States Dollars)

	Note	Nine months ended September 30,	
		2019	2018
Cash flows from operating activities			
Loss for the period		\$ (7,289,498)	\$ (3,720,055)
Adjustments to reconcile loss to net cash flows:			
Depreciation and amortization	12,13,14	409,503	273,879
Gain on sale of servicing equipment	12	(348,807)	-
Loss on sale of property, plant and equipment	12,13	101,568	-
Impairment loss	12	206,100	-
Noncash finance lease income	9	(180,791)	-
Incentive compensation expense	20	463,983	667,648
Warrants and debentures issued for services	15,16	803,997	-
Finance and accretion expense	16	1,518,850	784,958
Listing expense	5	363,095	-
Change in fair value of embedded derivative liabilities	16	1,297,324	-
		<u>(2,654,676)</u>	<u>(1,993,570)</u>
Adjustments to operating assets and liabilities:			
(Increase) in trade and other receivables	8	(35,926)	(79,617)
Decrease (increase) in inventories	10	979	(271,901)
Decrease (increase) in prepaid and other current assets	11	102,186	(245,997)
Increase (decrease) in trade and other payables	17	(96,805)	220,810
Increase (decrease) in accrued expenses	18	506,326	49,554
Increase (decrease) in unearned revenue	6	-	162,313
Increase (decrease) in amounts due to related parties	21	547,258	(56,885)
Net cash flows used in operating activities		<u>(1,630,658)</u>	<u>(2,215,293)</u>
Cash flows from investing activities			
Purchases of servicing equipment	12	(46,915)	(2,089,550)
Purchases of property, plant and equipment	13	(1,113)	(69,293)
Proceeds from the sale of servicing equipment and property, plant and equipment	12,13	313,380	-
Proceeds from finance lease receivables	9	57,975	-
Cash acquired as part of reverse acquisition	5	698,858	-
Net cash flows provided by (used in) investing activities		<u>1,022,185</u>	<u>(2,158,843)</u>
Cash flows from financing activities			
Proceeds from loans and borrowings	16	1,100,000	5,602,715
Proceeds from issuance of Sub Receipt debentures	16	4,472,085	-
Repayment of debt	16	(49,664)	(1,211)
Payment of debt issuance and deferred financing costs	16	(477,007)	(185,592)
Net cash flows provided by financing activities		<u>5,045,414</u>	<u>5,415,912</u>
Effect of exchange rate changes on cash		<u>(27,938)</u>	<u>-</u>
Net increase in cash		4,409,003	1,041,776
Cash at beginning of the period		534,148	848,047
Cash at end of the period		<u>\$ 4,943,151</u>	<u>\$ 1,889,823</u>
Supplemental disclosure of cash flow information:			
Cash paid for interest		<u>\$ 521</u>	<u>\$ 131,236</u>
Supplemental disclosure of non-cash transactions:			
Non-cash investing and financing activities			
Purchases of servicing equipment included in trade and other payables and amounts due to related parties	17,21	\$ 381,913	\$ 331,889
Discount on loan borrowings proceeds	16	228,183	1,640,630
Issuance of convertible debt, net of discount of \$163,563	16	55,305	-
Prepaid debt issuance costs - warrants issued	15	851,662	-
Issuance of warrants to service providers, consultants and and Series C debenture holders	15	654,912	-
Issuance of embedded derivative liabilities	16	1,044,804	-
Conversion of Series B and Series C convertible debt to common stock	16	9,349,311	-
Conversion of Sub Receipt convertible debt to common stock	16	264,697	-
Servicing equipment sold and reduction to deferred revenue	6	1,006,542	-

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

Xtraction Services Holdings Corp.

Notes to Financial Statements

(unaudited)

(Expressed in United States Dollars)

(1) Nature of operations and background information

Xtraction Services Holdings Corp. ("Xtraction Services", or "the Company") formerly known as Caracara Silver Inc. (Caracara) was incorporated under the laws of the Province of British Columbia on December 3, 2009, and is listed on the Canadian Securities Exchange ("CSE") under the symbol "XS". On March 22, 2019, the Company entered into a definitive merger agreement with Caracara pursuant to which Caracara would acquire all of the issued and outstanding common shares of Xtraction Services. The transaction was structured as a "reverse triangular merger" between the Company, Caracara and a wholly-owned subsidiary of Caracara to be incorporated under the laws of Delaware. On September 11, 2019 the merger became effective whereby Caracara's subsidiary acquired all of the issued and outstanding Class A and Class B common shares, stock options and warrants of the Company and the resulting issuer changed its name from Caracara Silver Inc. to Xtraction Services Holdings Corp. and continued with the business of the Company. Prior to the merger with Caracara the Company was originally established as a Delaware limited liability company on October 9, 2017. In July 2018, the Company filed with the Secretary of State of Delaware to change its corporate status from a Delaware limited liability company to a Delaware corporation and elected to be classified as a corporation. On July 19, 2018, the Company received a Certificate of Conversion and Certificate of Incorporation from the Secretary of State of Delaware.

The Company determined that the merger transaction constituted a reverse acquisition for accounting purposes whereby the Company acquired Caracara and its wholly-owned subsidiary. For accounting purposes, the Company is treated as the accounting acquirer (legal subsidiary), and Caracara is treated as the accounting acquiree (legal parent) in these financial statements. As the Company was deemed to be the acquirer for accounting purposes, its assets, liabilities and operations since incorporation are included in these financial statements at their historical carrying values. Caracara's results of operations and those of its subsidiary are included from the transaction date, September 11, 2019. The comparative figures are those of the Company prior to the reverse acquisition.

Xtraction Services is a specialty finance company that provides equipment leasing solutions in the United States to owner/operators of cannabis and hemp companies including cultivators, oil processors, manufacturers, testing laboratories, among others and operates in one business segment in one geographic area. Its registered office is located at 1880 Century Park East, Suite 250, Los Angeles, California 90067.

The accompanying financial statements have been approved by the Company's board of directors and are authorized for issuance as of November 27, 2019.

(2) Basis of presentation

Statement of compliance

These interim condensed financial statements have been prepared in accordance with International Accounting Standards ("IAS") 34 Interim Financial Reporting under the International Financial Reporting Standards (IFRS) as issued by the International Accounting

Xtraction Services Holdings Corp.

Notes to Financial Statements

(unaudited)

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Standards Board (IASB). They do not include all disclosures that would otherwise be required in a complete set of financial statements and should be read in conjunction with the 2018 and 2017 audited financial statements.

Critical accounting estimates and judgements

In the application of the Company's accounting policies, the Company's management are required to make judgments, estimates and assumptions about the carrying amounts of assets and liabilities that are not readily apparent from other sources. The estimates and associated assumptions are based on historical experience and other factors that are considered to be relevant. Actual results may differ from these assumptions.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimate is revised if the revision affects only that period, or in the period of the revision and future periods if the revision affects both current and future periods.

(3) Going concern

The financial statements have been prepared on a going concern basis, which assume that the Company will be able to realize its assets and discharge its liabilities in the normal course of business for the foreseeable future. The Company has incurred losses and negative cash flows from operations since inception, and has an accumulated deficit of \$13,504,200 and \$6,214,702 as of September 30, 2019 and December 31, 2018, respectively. These conditions indicate the existence of material uncertainties that casts substantial doubt about the Company's ability to continue as a going concern. The Company's ability to continue as a going concern is dependent upon achieving a profitable level of operations and obtaining additional financing, neither of which is assured. The Company anticipates incurring additional losses until such time that it can generate sufficient revenue from its operations to cover its expenses. Historically, the Company has been successful in obtaining enough funding for operating and capital requirements. The financial statements do not give effect to any adjustments which may be necessary should the Company be unable to continue as a going concern and be required to realize its assets and discharge its liabilities in other than the normal course of business and at amounts different from those reflected in the accompanying financial statements. These adjustments could be material.

The operations of the Company are subject to certain risks and uncertainties including, among others: uncertainty of product development; technological uncertainty; commercial acceptance of any developed products; dependence on collaborative partners; uncertainty regarding patents and proprietary rights; comprehensive government regulations; market risk; and dependence on key personnel.

(4) Significant accounting policies

The Company has applied the same accounting policies and methods of computation in its interim condensed financial statements as in its 2018 and 2017 annual financial statements except for adoption of *IFRS 16 Leases* and *IFRIC 23 Uncertainty over income tax treatments* on January 1, 2019.

Xtraction Services Holdings Corp.

Notes to Financial Statements

(unaudited)

(Expressed in United States Dollars)

Fair value of financial instruments

The following fair value hierarchy table presents information about each major category of the Company's financial assets measured at fair value on a recurring basis:

	Fair Value Measurement at Reporting Date Using			
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total
As of September 30, 2019:				
Liabilities:				
Warrant derivative liabilities (note 15)	\$ -	\$ -	\$ 462,830	\$ 462,830
Embedded derivative liabilities (note 16)	\$ -	\$ -	\$ 646,064	\$ 646,064
	\$ -	\$ -	\$ 1,108,894	\$ 1,108,894
As of December 31, 2018:				
Liabilities:				
Warrant derivative liabilities (note 15)	\$ -	\$ -	\$ 50,031	\$ 50,031
Embedded derivative liabilities (note 16)	-	-	1,091,514	1,091,514
	\$ -	\$ -	\$ 1,141,545	\$ 1,141,545

The estimated fair value of the warrant derivative and embedded derivative liabilities would increase or decrease if the expected volatility and conversion price was higher or lower. The following table shows a reconciliation from January 1, 2019 through September 30, 2019 for Level 3 fair values:

	Warrant derivative liabilities	Embedded derivative liabilities	Total
Balance at January 1, 2019	\$ 50,031	\$ 1,091,514	\$ 1,141,545
Warrants issued to investment advisors, brokers, consultants and service providers (note 15)	1,545,996	-	1,545,996
Sub receipt convertible debt conversion option (note 16)	-	1,044,804	1,044,804
Net change in fair value (unrealized)	(1,133,197)	2,430,521	1,297,324
Reduction in embedded derivative liability as a result of Series C debenture conversion (note 16)	-	(3,920,775)	(3,920,775)
Balance at September 30, 2019	\$ 462,830	\$ 646,064	\$ 1,108,894

New standards and interpretations recently adopted

Effective January 1, 2019, the Company has adopted IFRS 16 Leases ("IFRS 16") using the modified retrospective application method, where the 2018 comparatives are not restated and the cumulative effect of initially applying IFRS 16 has been recorded on January 1, 2019 for any differences identified, including adjustments to opening retained earnings balance. As of January 1, 2019 the Company had one lease as a lessee, which is a short-term operating lease, and one lease as a lessor, which is an operating lease. The Company evaluated both leases and concluded

Xtraction Services Holdings Corp.

Notes to Financial Statements

(unaudited)

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there was no impact on its financial statements and related disclosures upon the adoption of this standard.

The Company has concluded there was no impact on its financial statements and related disclosures upon the adoption of *IFRIC 23 Uncertainty over income tax treatments*.

The Company had no additional new standards adopted that resulted in changes to the Company's accounting policies.

(5) Reverse acquisition

The following table presents the Company's purchase price allocation for the reverse acquisition.

Cash	\$ 698,858
Other receivable	6,048
Accounts payable and accrued expenses	<u>(114,834)</u>
Net assets acquired	590,072
Purchase price paid:	
Fair value of 3,896,598 common shares at \$0.24 per share	<u>\$ 953,167</u>
Excess of purchase price paid over net assets acquired	
allocated to listing expense	<u>\$ 363,095</u>

On March 22, 2019, the Company entered into a definitive merger agreement with Caracara pursuant to which Caracara through a whole-owned subsidiary, incorporated in the State of Delaware, would acquire all of the issued and outstanding common shares of the Company.

On September 11, 2019, the merger became effective via a "reverse triangular merger", pursuant to which Caracara acquired all of the issued and outstanding class A and class B common shares, stock options and warrants of the Company by way of a merger between Caracara and its wholly-owned subsidiary. The resulting issuer changed its name from Caracara to Xtraction Services Holdings Corp. and continued with the business of the Company. Caracara did not meet the definition of a business under IFRS.

The fair value, of the acquisition of 3,896,598 shares of Caracara at a fair value per share of \$0.24 was \$953,167. The purchase price allocation of the merger includes net assets acquired of \$590,072, resulting in a listing expense of \$363,095.

Xtraction Services Holdings Corp.

Notes to Financial Statements

(unaudited)

(Expressed in United States Dollars)

(6) Revenue

The following table presents a disaggregation of revenue by source and timing of revenue recognition:

	Three months ended		Nine months ended	
	September 30,		September 30,	
	2019	2018	2019	2018
Revenue source:				
Equipment sales	\$ 165,931	\$ 12,442	\$ 1,015,529	12,442
Royalty sales	72,247	39,288	173,302	39,288
Financing leases (note 9)	719,949	-	741,321	-
Professional services	-	12,217	-	12,217
Other revenue	1,076	-	1,076	-
	<u>\$ 959,203</u>	<u>\$ 63,947</u>	<u>\$ 1,931,228</u>	<u>\$ 63,947</u>
Timing of revenue recognition under IFRS 15				
from contracts with customers:				
Products and services transferred at a point in time	<u>\$ 165,931</u>	<u>\$ -</u>	<u>\$ 1,015,529</u>	<u>\$ -</u>

The Company's largest source of revenue resulted from the sale of equipment to a single customer. At September 30, 2019 and December 31, 2018 the Company had an unsatisfied performance obligation of \$15,375 and \$1,021,917, respectively, related to this customer deposit received on undelivered servicing equipment, which is reflected as unearned revenue in the statements of financial position. The Company has elected to adopt the practical expedient of IFRS 15 to not disclose information about remaining performance obligations where the contract has an expected duration of less than one year.

The following table presents minimum royalty revenue expected to be recognized in future periods as of September 30, 2019.

Year ended December 31:	
2019	\$ 110,000
2020	600,000
2021	600,000
	<u>\$ 1,310,000</u>

Revenue concentration

All of the Company's revenue is derived from customers in the United States with one customer representing 75% of the Company's recognized revenue in the three months ended September 30, 2019, and two customers representing 52% and 38% of the Company's recognized revenue in the nine months ended September 30, 2019.

Xtraction Services Holdings Corp.

Notes to Financial Statements

(unaudited)

(Expressed in United States Dollars)

(7) Expenses by nature

The following tables presents an analysis of expense by nature:

	Three months ended		Nine months ended	
	September 30,		September 30,	
	2019	2018	2019	2018
Cost of sales:				
Compensation and benefits	\$ 64,894	\$ 46,290	\$ 210,822	\$ 75,372
Depreciation expense	77,447	78,833	294,629	158,914
Amortization of intangible	38,291	38,291	114,874	114,874
Equipment purchases	67,209	(123)	684,128	9,483
Equipment costs	560,960	-	560,960	-
Supplies and materials	24,050	44,066	81,622	44,752
Maintenance and repair costs	4,500	7,000	25,836	8,884
Other expenses	648	27,859	50,239	43,554
	<u>\$ 837,999</u>	<u>\$ 242,216</u>	<u>\$ 2,023,110</u>	<u>\$ 455,833</u>
Administrative expenses:				
Compensation and benefits	\$ 8,870	\$ 135,615	\$ 53,256	\$ 194,620
Incentive compensation	64,553	634,573	463,983	667,648
Contractors and outside services	91,151	211,391	229,553	362,524
Management fee	86,000	-	260,400	-
Professional fees	234,185	357,031	1,651,695	456,063
Office rent, utilities and expenses	9,068	16,589	46,057	40,747
Travel meals and entertainment	3,172	95,642	30,998	164,089
Other expenses	46,121	39,880	192,889	93,320
	<u>\$ 543,120</u>	<u>\$ 1,490,721</u>	<u>\$ 2,928,831</u>	<u>\$ 1,979,011</u>
Sales and marketing expenses:				
Compensation and benefits	\$ 47,122	\$ 36,362	\$ 67,287	\$ 36,362
Contractors and outside services	-	42,400	-	93,817
Professional fees	3,250	23,322	49,083	30,322
Advertising and marketing	31,704	51,370	42,857	92,715
Trade shows	-	56,758	7,209	79,316
Other expenses	313	5,673	1,600	6,022
	<u>\$ 82,389</u>	<u>\$ 215,885</u>	<u>\$ 168,036</u>	<u>\$ 338,554</u>

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(8) Trade and other receivables

The following table presents trade and other receivables:

	September 30, 2019	December 31, 2018
Trade receivables	\$ 129,597	\$ 6,421
Other receivable	-	30,000
	<u>\$ 129,597</u>	<u>\$ 36,421</u>

The \$30,000 receivable due from Khrysos at December 31, 2018 consisted of reimbursements for certain marketing expenditures and was paid in March 2019.

(9) Financing receivables

The Company has entered into lease arrangements as a lessor that are considered to be finance leases. All of the risks and rewards of ownership of the service equipment assets underlying the finance leases are substantially transferred to the lessee.

The Company's net investment in leases is \$626,529 as of September 30, 2019, which, represents finance leases with maturities of less than one year, with an undiscounted lease receivable of \$641,129 and unearned finance income of \$14,600.

(10) Inventories

Inventories primarily consist of spare parts that the Company purchased at cost, which it intends to either sell to customers as part of the installation of servicing equipment for customers or for repair orders. The carrying value of spare parts inventory as of September 30, 2019 and December 31, 2018 was \$95,187 and \$96,166, respectively.

(11) Prepaid and other current assets

The following table presents prepaids and other assets:

	September 30, 2019	December 31, 2018
Prepaid insurance	\$ 30,998	\$ 54,372
Prepaid consulting services	43,750	45,333
Security deposit	9,900	3,500
Other	18,846	6,756
	<u>\$ 103,494</u>	<u>\$ 109,961</u>

(12) Servicing equipment

The following table below presents the change in carrying value of the Company's servicing equipment from January 1, 2019 through September 30, 2019:

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	Balance at January 1, 2019	Additions	Equipment sales	Finance lease sales	Impairment loss	Balance at September 30, 2019
Cost or valuation						
Extraction equipment	\$ 2,046,163	\$ 384,332	\$ -	\$ (723,266)	\$ (206,100)	\$ 1,501,129
Ancillary extraction equipment	6,268	7,627	-	-	-	13,895
Pre-processing equipment	17,118	14,452	-	(2,250)	-	29,320
Post-processing equipment	444,132	129,549	(319,618)	(20,941)	-	233,122
Distillation equipment	176,698	3,333	(180,031)	-	-	-
Isolate equipment	-	3,000	-	-	-	3,000
Analytical equipment	43,661	30,000	(19,759)	-	-	53,902
Vacuums	2,033	4,349	-	-	-	6,382
Total cost or valuation	<u>\$ 2,736,073</u>	<u>\$ 576,642</u>	<u>\$ (519,408)</u>	<u>\$ (746,457)</u>	<u>\$ (206,100)</u>	<u>\$ 1,840,750</u>
Accumulated depreciation	<u>\$ (256,877)</u>	<u>(290,116)</u>	<u>61,639</u>	<u>185,498</u>	<u>-</u>	<u>\$ (299,856)</u>
Net book value	<u>\$ 2,479,196</u>	<u>\$ 286,526</u>	<u>\$ (457,769)</u>	<u>\$ (560,959)</u>	<u>\$ (206,100)</u>	<u>\$ 1,540,894</u>

Equipment sales

The Company sold \$97,597 of previously capitalized equipment directly to a customer in January, 2019. The revenue recognized and net book value of the equipment is included in revenue and cost of sales, respectively, within the condensed statements of comprehensive loss for the three and nine months ended September 30, 2019. Additionally the Company sold \$19,759 and \$402,052 of previously capitalized equipment back to a related party vendor and to third party buyers, respectively, in June and August, 2019. The Company recognized a loss of \$81,352 and \$93,976 on the sales, within the condensed statements of comprehensive loss for the three and nine months ended September 30, 2019, respectively.

The Company sold \$58,329 and \$562,388 in the three and nine months ended September 30, 2019, respectively, of equipment, that was recorded in prepaid servicing equipment, directly to customers prior to the servicing equipment being available for use.

Finance lease sales

The Company is a lessor for lease arrangements considered to be finance leases (note 9). As a result of substantially all of the risks and rewards of ownership of the servicing equipment transferred to the lessee, the Company reduced the net book value of servicing equipment underlying the finance leases.

Impairment loss

The Company recorded an impairment loss of \$206,100 in July 2019 related to a single piece of extraction equipment that was leased to a customer under a financing lease (note 9). The Company determined that net book value of the underlying equipment exceeded the value of lease stream revenue at lease inception.

The cost of servicing equipment includes \$1,046,172 and \$835,605 subject to revenue generated from royalty arrangements at September 30, 2019 and December 31, 2018, respectively.

The carrying value of prepaid service equipment at September 30, 2019 and December 31, 2018 was \$1,540,894 and \$2,770,397, respectively, and represents servicing equipment purchased but

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not yet installed or delivered at a customer site, and servicing equipment that has yet to be allocated to a specific customer site.

Depreciation expense related to servicing equipment is included in cost of sales within the condensed statements of comprehensive loss.

(13) Property, plant and equipment

The following table below presents the change in carrying value of the Company's property plant and equipment from January 1, 2019 through September 30, 2019:

	Balance at January 1, 2019	Additions	Sale	Balance at September 30, 2019
Cost or valuation				
Computers	\$ 11,111	\$ 1,179	\$ (3,997)	\$ 8,293
Machinery and equipment	3,490	-	-	3,490
Vehicles	57,715	-	(57,715)	-
Total cost or valuation	<u>\$ 72,316</u>	<u>\$ 1,179</u>	<u>\$ (61,712)</u>	<u>\$ 11,783</u>
Accumulated depreciation	<u>\$ (6,638)</u>	<u>(4,513)</u>	<u>7,739</u>	<u>\$ (3,412)</u>
Net book value	<u>\$ 65,678</u>	<u>\$ (3,334)</u>	<u>\$ (53,973)</u>	<u>\$ 8,371</u>

Depreciation expense related to property, plant and equipment is included in cost of sales expenses within the condensed statements of comprehensive loss.

(14) Intangible asset

The following table below shows the change in carrying value of the Company's intangible asset from January 1, 2019 through September 30, 2019:

	Balance at January 1, 2019	Additions/ (Dispos als)	Balance at September 30, 2019
Cost or valuation			
Purchase exclusivity and intellectual property rights	\$ 765,830	\$ -	\$ 765,830
Accumulated amortization	<u>\$ (165,930)</u>	<u>(114,874)</u>	<u>\$ (280,804)</u>
Net book value	<u>\$ 599,900</u>	<u>\$ (114,874)</u>	<u>\$ 485,026</u>

Amortization expense for the purchase and intellectual property rights is included in cost of sales within the condensed statements of comprehensive loss.

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(15) Shareholders' equity

Upon the Company's merger with Caracara (note 5) all of the Company's issued and outstanding shares of Class A and Class B common shares were converted to shares of common and proportionate voting shares. The Company has an unlimited number of authorized common and proportionate voting shares with a par value of \$0.0001. Proportionate voting shares can be converted into common shares at the option of the holders at a ratio of 1,000 to 1 upon approval of the Company's Resulting Issuer Board and satisfaction of the condition that greater than 40% of common and proportionate shareholders are US residents. On all voting matters, common shareholders are entitled to one vote and proportionate voting shareholders are entitled to 1,000 votes per proportionate voting share. Generally, in all other matters the proportionate voting shareholders have the same rights as the common shareholders and will be treated as if they were one class of shares. At September 30, 2019, the Company had 29,831,162 issued and outstanding common shares and 18,096 issued and outstanding proportionate voting shares.

At December 31, 2018, the Company had 225,000,000 authorized and 32,580,088 issued and outstanding Class A common shares with a par value of \$0.0001, and 25,000,000 authorized and 678,650 issued and outstanding Class B common shares with a par value of \$0.0001.

Share issuances

In January 2019, the Company entered into an agreement with an investment advisor to issue Class A common shares in exchange for services rendered in raising debt subscriptions. The investment advisor earns shares equal to \$15,000CAD (\$12,300) over a period of 24 months at a price of \$1.10CAD (\$0.82). No shares have been issued as of September 30, 2019 and the Company has recorded \$104,550 as prepaid debt issuance costs with an offset to accrued expenses within the statements of financial position as of September 30, 2019.

In April 2019, the Company issued 620,000 shares of Class A common shares valued based on the fair value of the Company's common shares on the date of grant at \$0.83 per share to investment advisors in connection with services rendered for transaction advisory guidance and structuring and the raise of debt subscriptions. The fair value of the Company's common shares issued was determined based on a market approach using recent equity transactions entered into between the Company and third parties. The Company has recorded \$415,000 as professional fees within the statements of comprehensive loss for the nine months ended September 30, 2019 related to transactional advisory services, and \$99,600 as prepaid debt issuance costs within the statements of financial position related to the debt subscription raise.

In May 2019, the Company issued 92,045 Class A common shares valued based on the fair value of the Company's common shares on the date of grant at \$0.82 per share to third party service provider for services to be rendered in future months. The fair value of the Company's common shares issued was determined based on a market approach using recent equity transactions entered into between the Company and third parties. The Company recorded \$75,000 as a prepaid expense within the statements of financial position and has amortized \$31,250 to professional fees within the statements of comprehensive loss for the three and nine months ended September

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30, 2019. As of September 30, 2019, \$43,750 was reflected as a prepaid expense within the statements of financial position.

In May 2019, the Company sold 45,455 shares of Class A common shares to a service provider at a price of \$1.10CAD (\$0.82), with such proceeds being used to pay another service provider, which is an entity that is a related party to the investor. The fair value of the Company's common shares issued was determined based on a market approach using recent equity transactions entered into between the Company and third parties. The Company has recorded \$37,273 as professional fees within the statements of comprehensive loss in the nine months ended September 30, 2019.

In September 2019, the Company issued 3,896,598 shares of common shares as consideration in connection with the merger with Caracara (note 5) at a price of \$0.24. The fair value of the Company's common shares was based on the closing value of the Company's stock on the first day of trading on the CSE.

In September 2019, the Company issued 10,050,378 shares of common shares and 359 proportionate voting shares common shares on the conversion of the Series B and Series C convertible debentures (note 16). Total shareholders' equity increased \$9,349,312 as a result of these conversions and the related reversal of the embedded derivative liabilities associated with the Series C debentures (note 16).

In September 2019, the Company issued 363,636 shares of common shares on the conversion of Sub Receipt debentures (note 16). Total shareholders' equity increased \$264,697 as a result of this conversion.

Warrant derivative liabilities

The fair value of warrant derivative liabilities at September 30, 2019 and December 31, 2018 was \$462,830 and \$50,031, respectively.

In March and April 2019 the Company issued 774,308 warrants to third party investment advisors and brokers for services rendered in raising debt subscriptions with 374,308 of the warrants having a five year term and a \$1.10CAD (\$0.82) exercise price. Upon being exercised the holders receive a share of common shares and a warrant, which have a \$1.50CAD (\$1.12) exercise price and a five year term. The remaining 400,000 warrants has a two year term and a \$1.10CAD (\$0.82) exercise price. The Company recorded \$561,259 of prepaid debt issuance costs with an offset to warrant derivative liabilities, as a result of the exercise price of the warrants being denominated in a currency different from the Company's functional currency, within the statements of financial position.

In April and May 2019, the Company issued 536,818 warrants to an investment advisor and third party service provider in connection with services rendered for transaction advisory guidance and consulting services to be rendered in future periods, with terms of two or five years and exercise price of \$1.10CAD (\$0.82) per share that vested immediately upon their issuance. The Company recorded \$290,403 of professional fees for transactional advisory services, within the statements

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of comprehensive loss, and \$14,671 of prepaid expenses for future consulting services, within the statements of financial position. Both amounts were reflected as an offset to warrant derivative liabilities, as a result of the exercise price of the warrants being denominated in a currency different from the Company's functional currency, within the statements of financial position.

In July 2019, the Company issued 150,000 warrants to consultants in connection with finance and accounting support services provided to the Company, with terms of two years and exercise price of \$1.10CAD (\$0.82) per share that vested immediately upon their issuance. The Company recorded \$61,321 of contractor costs, within the statements of comprehensive loss with an offset to warrant derivative liabilities, as a result of the exercise price of the warrants being denominated in a currency different from the Company's functional currency, within the statements of financial position.

In September 2019, the Company issued 5,452,134 and 363,636 of warrants related to the conversion of the Series C debentures and a conversion of a Sub Receipt debenture, respectively (note 16). Both warrant issuances had terms of five years and exercise price of \$1.50CAD (\$1.12 - \$1.13) per share that vested immediately upon their issuance. The Company recorded \$618,343 as a component of shareholders' equity with an offset to warrant derivative liabilities, as a result of the exercise price of the warrants being denominated in a currency different from the Company's functional currency, within the statements of financial position.

The grant date fair value of the 7,276,896 warrant issuances in the nine months ended September 30, 2019 was determined using the Black-Scholes option pricing model with the following assumptions:

Expected dividend yield	-
Expected volatility	90.0%
Risk-free interest rate	1.6% - 2.4%
Expected term	2 - 5 years
Exercise price	\$ 0.82 - 1.13

At September 30, 2019 the warrant derivative liabilities were re-valued with the change in fair value of \$1,121,213 and \$1,133,197 reflected in the condensed statements of comprehensive loss for the three and nine months ended September 30, 2019 respectively. The Company performed a black-scholes model while probability weighting the expected exercise price.

The fair value of the warrant derivative liabilities were determined using the following assumptions as of September 30, 2019:

	2019	2018
	Issuances	Issuances
Expected dividend yield	-	-
Expected volatility	90.0%	90.0%
Risk-free interest rate	1.6%	1.8%
Expected term	1.4 - 5.0 years	1.1 - 1.3 years
Exercise price	\$ 0.82 - 1.13	\$ 0.70

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The following table summarizes warrant activity from January 1, 2019 through September 30, 2019:

	Number of warrants	Weighted average exercise price per share
Outstanding at January 1, 2019	1,140,012	\$ 0.81
Granted	<u>7,276,896</u>	\$ 1.06
Outstanding at September 30, 2019	<u>8,416,908</u>	\$ 1.03

The following table presents warrants outstanding at September 30, 2019:

Expiration date	Term (years)	Number of warrants outstanding	Number of warrants exercisable	Exercise price US \$
12-Apr-20	2	275,000	275,000	\$ 0.80
4-May-20	2	325,000	325,000	\$ 0.80
17-May-20	2	91,250	91,250	\$ 0.80
4-May-20	2	10,000	10,000	\$ 0.60
17-May-20	2	111,500	111,500	\$ 0.60
17-May-20	2	27,500	27,500	\$ 0.60
17-Oct-20	2	17,647	17,647	\$ 0.85
17-Oct-20	2	17,647	17,647	\$ 0.85
30-Oct-20	2	30,000	30,000	\$ 0.85
30-Oct-20	2	2,118	2,118	\$ 0.85
28-Nov-20	2	31,765	31,765	\$ 0.85
5-Dec-20	2	26,470	26,470	\$ 0.85
31-Dec-20	2	174,115	174,115	\$ 0.85
22-Mar-21	2	400,000	400,000	\$ 0.82
22-Mar-24	5	344,591	344,591	\$ 0.82
12-Apr-24	5	500,000	500,000	\$ 0.82
26-Apr-24	5	29,717	29,717	\$ 0.82
15-May-21	2	36,818	36,818	\$ 0.82
17-Jul-21	2	125,000	125,000	\$ 0.84
17-Jul-21	2	25,000	25,000	\$ 0.84
11-Sep-24	5	5,452,134	5,452,134	\$ 1.12
20-Sep-24	5	363,636	363,636	\$ 1.13
Total	<u>2 - 5 years</u>	<u>8,416,908</u>	<u>8,416,908</u>	<u>\$ 1.03</u>

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(16) Loans and borrowings

The following table presents loans and borrowings outstanding:

<u>Description</u>	<u>Maturity date</u>	<u>Interest rate</u>	<u>September 30, 2019</u>	<u>December 31, 2018</u>
Term loans:				
Archytas	November 7, 2020	18.0%	\$ 600,000	\$ 600,000
Archytas	December 28, 2019	18.0%	500,000	-
Archytas	February 7, 2020	18.0%	100,000	-
Archytas	February 14, 2020	18.0%	150,000	-
Archytas	September 18, 2019	18.0%	150,000	-
Archytas	October 19, 2019	18.0%	200,000	-
			<u>1,700,000</u>	<u>600,000</u>
Series B convertible debentures:				
Tranche 1	April 12, 2020	8.0%	-	1,100,000
Tranche 2	May 4, 2020	8.0%	-	1,300,000
Tranche 3	May 17, 2020	8.0%	-	365,000
			<u>-</u>	<u>2,765,000</u>
Series C convertible debentures:				
Tranche 1	September 10, 2020	10.0%	-	2,000,000
Tranche 2	September 21, 2020	10.0%	-	785,000
Tranche 3	October 17, 2020	10.0%	-	500,000
Tranche 4	December 27, 2020	10.0%	-	221,000
			<u>-</u>	<u>3,506,000</u>
Convertible debentures	March 22, 2024	10.0%	218,869	-
Sub Receipt convertible debentures	September 11, 2024	10.0%	4,167,965	-
Vehicle loan	July 24, 2024	6.3%	-	49,664
			<u>6,086,834</u>	<u>6,920,664</u>
Less:				
Unamortized discounts, debt issuance costs and prepaid offering costs ⁽¹⁾			<u>(2,565,220)</u>	<u>(2,696,379)</u>
			<u>\$ 3,521,614</u>	<u>\$ 4,224,285</u>
Non-current			<u>\$ 2,421,614</u>	<u>\$ 4,216,627</u>
Current			<u>\$ 1,100,000</u>	<u>\$ 7,658</u>

Note to the table:

- 1) The carrying value of the term loans, Series B and Series C debentures, convertible debentures were adjusted using a discount rate of 50% to reflect the prevailing borrowing rates associated with debt acquired by companies with a similar credit risk profile as Xtraction Services, resulting in debt discounts with an offset to equity. The carrying value of the Sub Receipt convertible debentures were adjusted for the conversion feature denominated in a currency different from the Company's functional currency, resulting in a debt discount with an offset to embedded derivative liabilities. The debt discount will be accreted over the life of the respective debt instruments using the effective interest method.

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The following table below shows the change in carrying value of the Company's loans and borrowings from January 1, 2019 through September 30, 2019:

	<u>Term Loans</u>	<u>Convertible debentures</u>	<u>Vehicle loan</u>	<u>Debt discounts, issuance costs and prepaid offering costs</u>	<u>Total</u>
Balance at January 1, 2019	\$ 600,000	\$ 6,271,000	\$ 49,664	\$(2,696,379)	\$ 4,224,285
Borrowings	1,100,000	-	-	(228,183) ⁽¹⁾	871,817
Repayments	-	-	(49,664)	-	(49,664)
Issuance of convertible debt	-	218,869	-	(163,563) ⁽¹⁾	55,306
Issuance of Sub Receipt convertible debentures	-	4,472,085	-	(1,521,812) ⁽¹⁾	2,950,273
Conversion of Series B and Series C convertible debentures	-	(6,271,000)	-	1,379,143 ⁽²⁾	(4,891,857)
Conversion of Sub Receipt convertible debenture	-	(304,120)	-	-	(304,120)
Prepaid offering costs	-	-	-	(853,276)	(853,276)
Amortization and accretion of debt issuance and debt discount costs	-	-	-	1,518,850	1,518,850
Balance at September 30, 2019	<u>\$ 1,700,000</u>	<u>\$ 4,386,834</u>	<u>\$ -</u>	<u>\$(2,565,220)</u>	<u>\$ 3,521,614</u>

Notes to the table:

- 1) Represents debt discounts of \$1,436,551 for the discount on loan borrowing proceeds and convertible debt issuances, and \$477,007 of debt issuance costs was netted against the gross proceeds of the Sub Receipt debenture issuance.
- 2) Represents the reversal of unamortized debt discounts related to the conversion of the Series B and Series C convertible debentures.

Term loans

In January, February, March and April 2019, the Company received additional funding of \$1,100,000 in the form of term loans ("2019 term loans") from Archytas with maturity dates ranging from September 2019 to February 2020. The 2019 term loans bear interest at a rate of 18% per annum, payable monthly. In November 2019, the Company repaid the 2019 term loans (note 23).

Convertible debentures

In March 2019, the Company amended the conversion feature of the Series C debentures pursuant to which each holder of such debentures will receive upon conversion at price of \$0.94CAD, thereof one share of common shares and a warrant, which has a \$1.50CAD (\$1.12) exercise price and a five year term, upon conversion.

In April 2019, the Company received majority support of the Series B holders to amend the interest payment terms of the Series B debentures. As a result all interest payments payable to the Series B debenture holders are deferred starting in October 2018, and all such interest payments shall be payable-in-kind on the maturity date.

In March and April 2019, the Company issued CAD\$294,000 (\$218,869) of convertible debentures to investment advisors and brokers for services rendered in raising debt subscriptions.

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The convertible debentures mature after 5 years and bear interest at a rate of 10% per annum payable in cash in equal quarterly installments. The convertible debentures convert into common shares and warrants at a conversion price of \$1.10CAD (\$0.82) at the holders' option prior to maturity or upon a change of control. The warrants to be received have an exercise price of a \$1.50CAD (\$1.12) and have a five year term. Upon a change in control the Company is required to purchase the convertible debentures at a price of 105% of the principal balance plus accrued, unpaid interest. The Company has accounted for the fair value of the convertible debt at issuance of \$55,305 as prepaid debt issuance costs, within the statements of financial position. The debt discount of \$163,563 is being amortized to interest expense over the term of the debt under the effective interest rate method.

In March and April 2019, the Company completed a private placement of 5,882 subscription receipts for aggregate gross proceeds of approximately CAD\$5,882,000 (\$4,500,000) and expected closing costs of approximately CAD\$560,000 (\$426,000). The subscription receipts were held in escrow, until satisfaction of the escrow release conditions, at which time the subscription receipts would be convertible into one 10% unsecured convertible debenture of the Company in the principal amount of CAD\$1,000 (Sub Receipt debenture). On September 11, 2019 the escrow conditions were met, and the Company issued CAD\$5,882,000 (\$4,472,085) of Sub Receipt debentures to various investors. The Sub Receipt debentures mature after 5 years and bear interest at a rate of 10% per annum payable in cash in equal quarterly installments. The Sub Receipt debentures convert into common shares and warrants at a conversion price of \$1.10CAD (\$0.82) at the holders' option prior to maturity or upon a change of control. The warrants to be received have an exercise price of a \$1.50CAD (\$1.12) and have a five year term. Upon a change in control the Company is required to purchase the Sub Receipt debentures at a price of 105% of the principal balance plus accrued, unpaid interest. On September 20, 2019, an investor exercised their conversion feature on CAD\$400,000 (\$304,120) of the Sub Receipt debentures and received 363,636 shares of common shares.

The Company incurred debt issuance costs, netted against the gross proceeds of the issuance, of CAD\$627,393 (\$477,229) in connection with the issuance of the Sub Receipt debentures. The debt issuance costs was recorded as a discount on the Sub Receipt debentures carrying value, and is being amortized to interest expense over the life of the sub receipts convertible debentures under the effective interest rate method.

On September 10, 2019, the Series B and Series C convertible debentures outstanding principal balance of \$6,271,000 and unpaid accrued interest balance of \$536,680 automatically converted into 10,050,378 common shares and 359 proportionate voting shares (note 15) as all conditions of the proposed merger between the Company and Caracara were met. Additionally, the unamortized portion of the Series B and Series C debt discounts of \$1,379,143 was reflected against a component of equity within the consolidated statements of financial position, and the unamortized portion of debt issuance costs of \$75,283 was recorded to interest expense within the condensed statements of comprehensive loss.

Embedded derivative liabilities

The conversion feature of the Sub Receipt debenture is considered an embedded derivative liability because the conversion price is denominated in a currency different from the Company's

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functional currency. The Company performed a black-scholes model, resulting in a fair value of \$1,044,804 determined at issuance. The Company has accounted for the embedded derivative liabilities as a long-term liability within the statements of financial position. At September 30, 2019 the embedded derivative liabilities were re-valued at \$646,064 with the change in fair value of \$398,740 reflected in the statements of comprehensive loss for the three and nine months ended September 30, 2019.

The fair value of the embedded derivative liabilities were determined using the following assumptions as of September 30, 2019 and at issuance:

	<u>September 30, 2019</u>	<u>At issuance</u>
Expected dividend yield	-	-
Expected volatility	90.0%	90.0%
Risk-free interest rate	1.1%	1.1%
Expected term	4.9 years	5 years
Conversion price	\$ 0.83 - 1.13	\$ 0.84 - 1.14

Additionally in September 2019, \$3,920,775 of embedded derivative liabilities associated with the Series C conversion feature was reversed and reflected against a component of shareholders' equity within the consolidated statements of financial position in conjunction with the conversion of the Series C debentures. Prior to the Series C debenture conversion the Company had reflected changes in the fair market value of the embedded derivative liabilities of \$2,829,261 in the condensed statements of comprehensive loss for the nine months ended September 30, 2019.

Redeemable common stock

In July 2018, Archytas and a Member exercised the conversion feature of term loans held with the Company and received a combined 6,737,588 shares of Class A common shares. The Company classified \$650,000 of the amount converted as redeemable common shares and a liability as this represents amounts subject to rescission due to an ongoing governmental investigation of the Member's finances. An escrow balance of \$650,000 is maintained by Archytas to satisfy the obligation.

(17) Trade and other payables

The following table presents trade and other payables:

	<u>September 30, 2019</u>	<u>December 31, 2018</u>
Trade payables	\$ 108,969	\$ 182,155
Credit card payable	1,289	28,112
	<u>\$ 110,258</u>	<u>\$ 210,267</u>

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(18) Other current liabilities

The following table presents accrued expenses:

	September 30, 2019	December 31, 2018
Accrued interest	\$ 34,796	\$ 147,059
Accrued professional fees	351,213	7,195
Accrued compensation, benefits and related taxes	1,193	18,988
Accrued insurance	3,742	41,071
Accrued other	11,328	5,105
	<u>\$ 402,272</u>	<u>\$ 219,418</u>

(19) Income taxes

Income tax expense

	Three months ended September 30,		Nine months ended September 30,	
	2019	2018	2019	2018
Current tax:				
Current tax on profits for the year	\$ -	\$ -	\$ 975	\$ -
Income tax expense	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 975</u>	<u>\$ -</u>

Income tax expense is recognized based on management's estimate of the weighted average effective annual income tax rate expected for the full financial year. The estimated average annual tax rate used for the year to September 30, 2019 was 26.53%, compared to 0% for the three and nine months ended September 30, 2018. Prior to the July 19, 2018, the Company was a limited liability company treated as a partnership for federal and state income tax purposes with all income tax liabilities and/or benefits of the Company being passed through to the members. As such, no recognition of federal or state income taxes for the Company have been provided for the three and nine months ending September 30, 2018.

(20) Incentive compensation

In September 2019, in connection with the reverse acquisition with Caracara (note 5) the Company established the Omnibus Incentive Plan ("Incentive Plan") which replaced and governs all options under the Company's 2018 Stock Option Plan. The Incentive Plan provides for the granting of up to 15% of outstanding common shares and is not to exceed a maximum of 10,000,000 share-based equity incentive compensation awards such as stock options and restricted stock awards to directors, officers, employees, contractors, and advisors, as determined by the Company's board of directors.

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The following table summarizes stock option activity under the Option Plan from January 1, 2019 through September 30, 2019:

	<u>Number of shares</u>	<u>Weighted average exercise price per share</u>	<u>Weighted average remaining contractual term (years)</u>
Outstanding at January 1, 2019	3,567,893	\$ 0.60	9.5
Cancelled / forfeited	<u>(1,055,241)</u>	0.60	
Outstanding at September 30, 2019	<u>2,512,652</u>	\$ 0.60	8.8
Exercisable and vested at September 30, 2019	<u>1,408,681</u>	\$ 0.60	8.8

In January, February and June 2019, 1,055,241 of the issued options were forfeited as result of the resignation of certain employees of the Company. Additionally in January 2019 the Company accelerated the vesting of 857,523 options for one individual to allow for immediate vesting.

As of September 30, 2019 there was approximately \$249,000 of unrecognized compensation expense related to unvested stock options, which is expected to be recognized over a weighted average period of 1.8 years.

The Company recorded compensation expense for restricted stock awards and stock options, including non-cash compensation related to cancelled restricted units, of \$64,553 and \$634,573 for the three months ended September 30, 2019 and 2018, respectively, and \$463,983 and \$667,648 for the nine months ended September 30, 2019 and 2018, respectively.

(21) Related party transactions

The following presents balances and transactions between the Company and other related parties as of September 30, 2019 and December 31, 2018, respectively, and for the three and nine month periods ended September 30, 2019 and 2018, respectively.

Key management personnel

Key employees include executive management with the authority and responsibility for planning, directing and controlling the activities of the Company. The following table presents compensation and benefit expenses of key employees:

	<u>Three months ended September 30,</u>		<u>Nine months ended September 30,</u>	
	<u>2019</u>	<u>2018</u>	<u>2019</u>	<u>2018</u>
Salaries, contractor costs, management fees and benefits	\$ 134,581	\$ 212,328	\$ 378,199	\$ 289,353
Incentive compensation	60,851	41,647	376,069	41,647
	<u>\$ 195,432</u>	<u>\$ 253,975</u>	<u>\$ 754,268</u>	<u>\$ 331,000</u>

Related party other receivable

The following table presents related party receivables:

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	<u>September 30, 2019</u>	<u>December 31, 2018</u>
Other receivable (note 8) - Khrysos	\$ -	\$ 30,000

Related party transactions and amounts due to related parties

The following table presents expenses incurred on behalf of the Company and assets purchased from related parties:

	<u>Archytas</u>	<u>Khrysos</u>	<u>Total</u>
Amounts due to related parties at January 1, 2018	\$ 104,035	\$ 92,927	\$ 196,962
Interest expense	105,546	-	105,546
Operating expenses	9,100	10,589	19,689
Inventory purchases	-	291,667	291,667
Prepaid equipment purchases	-	2,240,972	2,240,972
Less payments to related parties	(218,681)	(2,249,278)	(2,467,959)
Amounts due to related parties at September 30, 2018	<u>\$ -</u>	<u>\$ 386,877</u>	<u>\$ 386,877</u>
Amounts due to related parties at January 1, 2019	\$ 13,000	\$ 105,654	\$ 118,654
Interest expense	218,957	-	218,957
Management fee	260,400	-	260,400
Operating expenses	-	86,614	86,614
Prepaid equipment purchases	-	286,083	286,083
Conversion of accrued interest to comon stock	(15,713)	-	(15,713)
Less payments to related parties	-	(3,000)	(3,000)
Amounts due to related parties at September 30, 2019	<u>\$ 476,644</u>	<u>\$ 475,351</u>	<u>\$ 951,995</u>

Effective January 2019 the Company entered into a management services agreement with Archytas at a monthly rate of \$28,667 and a term of five years, with one year automatic renewals, whereby Archytas will provide day-to-day executive management and support to the Company. In conjunction with entering into this agreement the Company's CEO and CMO terminated their employment agreements with the Company. Additionally, Archytas will receive a fee for services provided on a successful acquisition, merger or change of control of the Company valued at 2% of the enterprise value of such transaction. As of September 30, 2019 all amounts earned under the management services agreement are unpaid, and are reflected as a liability within the condensed statements of financial position. In November 2019, the Company repaid the outstanding amounts related to the management services agreement (note 23).

Related party loans and borrowings

The following table presents the Company's loans and borrowings, and related interest, from related parties:

	<u>September 30, 2019</u>	<u>December 31, 2018</u>
Archytas:		
Term loans (note 16)	\$ 1,700,000	\$ 600,000
Series B debentures (note 16)	-	200,000
Accrued interest	207,244	13,000
	<u>\$ 1,907,244</u>	<u>\$ 813,000</u>

The carrying value of the above loans and borrowings were reduced by discounts at September 30, 2019 and December 31, 2018, respectively (see note 16). In November 2019, the Company

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repaid \$1,100,000 of the term loans principal, and all accrued interest due as of September 30, 2019 (note 23).

Related party purchase commitments

The Company has the option to purchase extraction equipment from a related party vendor, Khrysos, and in the past, did so under mutual exclusivity that required minimum purchases to remain in effect. However, the Company has expanded its range of product offerings to include other vendors in order to provide tailored, end-to-end solutions for customers, and accordingly no longer maintains the mutual exclusivity. The mutual exclusivity arrangement calls for a temporary price increase of 5% upon the Company repaying the \$1,900,000 of term loans (Note 16), and until such time the Company has \$16,000,000 (equivalent of \$800,000) of cumulative equipment purchases from Khrysos. The term loans were subsequently modified to convertible debentures and converted to equity in July 2018, however, no price increases are currently effective and the timing of such increases will be determined between the Company and Khrysos at a future undetermined date.

Related party sales

In March and April 2019, the Company entered into rental lease agreements with CBD LLC to lease extraction machines and other ancillary processing equipment to CBD LLC. CBD LLC is a related party to the Company as a result of a shareholder of the Company also being an owner of CBD LLC. As part of the March lease agreement, CBD LLC has paid \$100,000 to this related party.

(22) Financial instrument risk exposures

Financial risk management

The Company is exposed in varying degrees to a variety of financial instrument related risks. The Board mitigates these risks by assessing, monitoring and approving the Company's risk management processes:

Credit risk

Credit risk is the risk of a potential loss to the Company if a customer or third party to a financial instrument fails to meet its contractual obligations. The maximum credit exposure is the carrying amount of cash. The Company does not have significant credit risk with respect to customers. All cash is placed with recognized U.S. financial institutions. The Company provides credit to its customers in the normal course of business and has established credit evaluation and monitoring processes to mitigate credit risk but has limited risk as the majority of sales are transacted with cash.

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Liquidity risk

Liquidity risk is the risk that the Company will not be able to meet its financial obligations associated with financial liabilities. The Company manages liquidity risk through the management of its capital structure. The Company's approach to managing liquidity is to ensure that it will have sufficient liquidity to settle obligations and liabilities when due.

At September 30, 2019, the Company had current assets of \$5,897,958 and current liabilities of \$3,692,730. All current liabilities are due within one year. At September 30, 2019 the Company also has loans and borrowings of \$6,088,768 of which \$850,000 are due in 2019, \$850,000 are due in 2020 and \$4,388,768 are due in 2024. In November 2019, the Company repaid \$1,100,000 of the loans and borrowings due in 2019 and 2020 (note 23).

Market risk

Currency risk

The Company has determined its functional currency to be the U.S. dollar. The operating results and financial position of the Company are reported in U.S. dollars. The Company has minimal financial transactions denominated in currencies other than the U.S. dollar. The Company has no hedging agreements in place with respect to foreign exchange rates.

Interest Rate Risk

Interest rate risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates. The Company's financial debts have fixed rates of interest and therefore expose the Company to a limited interest rate fair value risk.

(23) Events after the reporting date

Related party transactions

In November 2019, the Company repaid Archytas \$1,100,000 of outstanding terms loans, and \$207,244 and \$260,400 of accrued term loans and accrued management fees, respectively, that were outstanding as of September 30, 2019.

Sub receipt debenture conversion

In November 2019, the Company issued 50,000 common shares and warrants related to the conversion of a Sub Receipt debenture. The warrant issuance had a term of five years and exercise price of \$1.50CAD (\$1.14) per share that vested immediately upon their issuance.

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Lease Portfolio Updates

In November 2019, the Company reached a mutual agreement with an existing customer to terminate a lease arrangement due to the customer experiencing financial hardship. XS excluded revenues from this customer in the third quarter. Working with the customer, XS made arrangements to collect all service equipment previously held at the customer location and has sold, redeployed or recovered all equipment related to this engagement. The Company notes that approximately 95% of the associated equipment was sold or redeployed as at November 27, 2019.

On November 26, 2019, the Company announced announce that it has entered into a sale-leaseback agreement “**Leaseback agreement**”, with Halo Labs Inc., a leading cannabis extraction company that develops and manufactures quality cannabis oils and concentrates operating in California, Oregon and Nevada. The Leaseback Agreement was provided against a variety of existing equipment including but not limited to; extraction, pre and post processing, freezers and security equipment, for USD\$600,000. The Leaseback agreement is payable over a 3-year term with invoicing commencing immediately.

Option Issuance & Debt Settlement

XS has entered into debt settlement agreements with certain consultants where pursuant to these agreements, the Company has agreed to issue an aggregate of 727,273 Common Shares in the capital of the Company at a deemed price ranging from of CAD\$0.20-\$1.10 per Common Share to settle CAD\$440,000 of outstanding debt. As well, the Company issued 1,955,000 incentive stock options to acquire common shares of the Company to certain directors, management and consultants, pursuant to the Company’s stock option plan, at an exercise price of CAD\$0.34 and which expire five (5) years from the date of issuance.