SOURCE ENERGY SERVICES

CONSOLIDATED FINANCIAL STATEMENTS

AS AT AND FOR THE YEARS ENDED DECEMBER 31, 2021 AND 2020

www.sourceenergyservices.com
500, 1060 – 7th Street SW, Calgary, AB Canada T2R 0C4 | Telephone 403-262-1312

INDEPENDENT AUDITOR'S REPORT

To the shareholders of Source Energy Services Ltd.

Opinion

We have audited the consolidated financial statements of Source Energy Services Ltd. and its subsidiaries (the Company), which comprise the consolidated statement of financial position as at December 31, 2021, and the consolidated statement of operations and comprehensive loss, consolidated statement of changes in equity and consolidated statement of cash flows for the year then ended, and notes to the consolidated financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the consolidated financial position of the Company as at December 31, 2021, and its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards (IFRS).

Other matter

The consolidated financial statements of the Company for the year ended December 31, 2020 were audited by another auditor who expressed an unmodified opinion on those consolidated financial statements on March 18, 2021.

Basis for opinion

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

Key audit matters

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

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

Key audit matter	**How our audit addressed the key audit matter**
Assessment of indicators of impairment or impairment reversal of non-financial assets For the year ended December 31, 2021, no impairment or impairment reversal was recorded with respect to the Company's non-financial assets. Refer to Note 3 *Significant Accounting Policies* of the consolidated financial statements for a description of the Company's accounting policy for impairment of non-financial assets. Refer to Note 7 *Property, Plant and Equipment* of the consolidated financial statements for the Company's impairment disclosures. For purposes of assessing impairment, non-financial assets are grouped into cash-generating units ("CGUs"), which are reviewed for indicators of impairment or impairment reversal at each reporting period. No indicators of impairment or impairment reversal were identified as of December 31, 2021. Auditing the Company's assessment of indicators of impairment or impairment reversal requires significant judgment due to uncertainties caused by the effects of commodity price volatility. The assessment relied on significant assumptions and estimates concerning commodity price forecasts, overall financial performance of the Company, macroeconomic conditions, and industry and market considerations.	To test the Company's assessment of indicators of impairment or impairment reversal, we performed the following procedures, among others: • Assessed the Company's historical forecasting accuracy by comparing actual earnings to prior period forecasts; • Evaluated the Company's current period forecast in comparison to historical results, third-party commodity price forecasts, analyst reports and industry publications; • With the assistance of our internal valuations specialist, evaluated metrics based on the Company's enterprise value relative to its carrying amount and to comparable peer companies; and • Evaluated the adequacy of the impairment note disclosure included in Note 7 of the accompanying financial statements in relation to this matter.

Other information

Management is responsible for the other information. The other information comprises Management's Discussion & Analysis.

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

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

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

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

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

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

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

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

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

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

- Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Company's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Company to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

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

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

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

The engagement partner on the audit resulting in this independent auditor’s report is Kim Wiggins.

Ernst + Young LLP

Calgary, Alberta
March 9, 2022

SOURCE ENERGY SERVICES LTD.

Consolidated Statements of Financial Position

(All amounts are in thousands of Canadian dollars, unless otherwise noted)

	Note		December 31, 2021		December 31, 2020
Assets					
Current assets					
Accounts receivable	4(d)	$	43,499	$	33,644
Prepaid expenses			5,728		4,436
Derivative asset	4(c)		1,181		—
Inventories	6		56,337		53,467
Total current assets			106,745		91,547
Derivative asset	4(c)		537		—
Property, plant and equipment	7		131,935		140,927
Right-of-use assets	8		26,814		33,787
Total assets		$	266,031	$	266,261
Liabilities and equity					
Current liabilities					
Accounts payable and accruals	4(e)	$	29,336	$	33,219
Contract liabilities	16		94		776
Lease liabilities	11		12,358		11,036
Current portion of long-term debt	10		7,500		—
Decommissioning provision	12		1,020		1,006
Total current liabilities			50,308		46,037
Lease liabilities	11		26,078		31,293
Long-term debt	10		175,531		147,281
Decommissioning provision	12		7,588		8,963
Total liabilities		$	259,505	$	233,574
Shareholders' equity					
Shareholders' equity	13(a)	$	410,632	$	410,632
Contributed surplus			2,459		2,459
Accumulated deficit			(413,025)		(388,622)
Cumulative translation adjustment			6,460		8,218
Total equity		$	6,526	$	32,687
Total liabilities and equity		$	266,031	$	266,261

See accompanying notes to the consolidated financial statements.

Commitments and contingencies (Note 18)

Approved on behalf of the Board of Directors:

signed "Stew Hanlon"
Stew Hanlon
Director

signed "Brad Thomson"
Brad Thomson
Director

SOURCE ENERGY SERVICES LTD.

Consolidated Statements of Operations and Comprehensive Loss

(All amounts are in thousands of Canadian dollars, unless otherwise noted)

	Note		2021		2020
Sales					
Sand revenue	16	$	258,545	$	210,021
Wellsite solutions	16		57,621		36,644
Terminal services	16		3,695		3,213
Total sales			319,861		249,878
Cost of sales	17	$	259,429	$	193,033
Cost of sales - depreciation			21,102		32,188
Gross margin		$	39,330	$	24,657
Operating expense	17	$	16,514	$	12,485
General & administrative expense	17		9,283		9,379
Depreciation			9,873		13,860
Income (loss) from operations		$	3,660	$	(11,067)
Other expense (income):					
Finance expense	19	$	30,320	$	29,689
Share-based compensation expense (recovery)	14		643		(14)
Gain on asset disposal			(63)		(150)
Unrealized gain on derivative assets	4(c)		(247)		—
Other income	10(d)		(3,200)		(1,625)
Other expense	18		203		298
Impairment expense	7		—		143,656
Loss on sublease	8		1,159		—
Gain on debt extinguishment	13(b)		—		(27,690)
Foreign exchange gain			(752)		(1,115)
Total other expense			28,063		143,049
Loss before income taxes		$	(24,403)	$	(154,116)
Income taxes					
Deferred tax expense	9	$	—	$	31,350
Total income taxes			—		31,350
Net loss		$	(24,403)	$	(185,466)
Net loss attributable to shareholders			(24,403)		(182,675)
Net loss attributable to non-controlling interests	13(a)		—		(2,791)
Total net loss		$	(24,403)	$	(185,466)
Other comprehensive loss					
Foreign currency translation adjustment (subject to recycling)			(1,758)		6,214
Comprehensive loss		$	(26,161)	$	(179,252)
Loss per share (in dollars)					
Basic and diluted	15	$	(1.80)	$	(36.81)

See accompanying notes to the consolidated financial statements.

SOURCE ENERGY SERVICES LTD.

Consolidated Statements of Changes in Equity

(All amounts are in thousands of Canadian dollars, unless otherwise noted)

	Note	Common share capital		Contributed Surplus	Cumulative Translation Adjustment	Accumulated Deficit	Total Equity
		Number of Shares	$				
Balance at December 31, 2020		**13,545,055**	**$ 410,632**	**$ 2,459**	**$ 8,218**	**$ (388,622)**	**$ 32,687**
Net loss						(24,403)	**(24,403)**
Unrealized foreign exchange loss					(1,758)		**(1,758)**
Balance at December 31, 2021		**13,545,055**	**$ 410,632**	**$ 2,459**	**$ 6,460**	**$ (413,025)**	**$ 6,526**

	Note	Common share capital		Contributed Surplus	Cumulative Translation Adjustment	Accumulated Deficit	Non-controlling interests	Total Equity
		Number of Shares	$					
Balance at December 31, 2019		**5,079,388**	**$ 397,911**	**$ 7,910**	**$ 2,004**	**$ (205,947)**	**$ (2,569)**	**$ 199,309**
Elimination of NCI through conversion of Class B shares	13(a)		91	(5,451)			5,360	—
Share issuance due to Recapitalization Transaction(1)	13(a)	8,465,667	12,630					**12,630**
Net loss						(182,675)	(2,791)	**(185,466)**
Unrealized foreign exchange income					6,214			**6,214**
Balance at December 31, 2020		**13,545,055**	**$ 410,632**	**$ 2,459**	**$ 8,218**	**$ (388,622)**	**—**	**$ 32,687**

Note:

(1) Net of transaction costs related to share issuance as part of the Recapitalization Transaction (as defined in Note 13).

See accompanying notes to the consolidated financial statements.

SOURCE ENERGY SERVICES LTD.

Consolidated Statements of Cash Flows

(All amounts are in thousands of Canadian dollars, unless otherwise noted)

	Note		2021		2020
Cash Flows Provided by Operating Activities					
Net loss		$	(24,403)	$	(185,466)
Adjusted for the following:					
Depreciation			30,975		46,048
Share-based compensation	14		643		(14)
Gain on asset disposal			(63)		(150)
Finance expense	19		30,320		29,689
Impairment	7		—		143,656
Gain on debt extinguishment	13(b)		—		(27,690)
Deferred income taxes	9		—		31,350
Unrealized gain on derivative assets	4(c)		(247)		—
Loss on sublease	8		1,159		—
Satisfaction of performance obligations, net of proceeds on contract liabilities	16		(748)		(2,081)
Payments for share-based compensation			(117)		(15)
Payments made for decommissioning provision	12		(1,818)		(1,575)
Net changes in non-cash working capital	5		(21,690)		5,619
Cash flows provided by operating activities		$	14,011	$	39,371
Investing Activities					
Capital expenditures			(6,517)		(3,683)
Proceeds on disposal of property, plant and equipment			75		155
Net changes in non-cash working capital	5		442		(1,428)
Cash flows used in investing activities		$	(6,000)	$	(4,956)
Financing Activities					
Proceeds (repayments) on long-term debt	5		13,110		(5,613)
Recapitalization Transaction debt issuance costs			—		(7,804)
Recapitalization Transaction equity issuance costs			—		(69)
Proceeds from the US Paycheck Protection Program			—		2,931
Repayment of lease obligations	11		(13,224)		(15,526)
Financing expense paid			(7,897)		(8,334)
Cash flows used in financing activities		$	(8,011)	$	(34,415)
Increase (decrease) in cash		$	—	$	—
Cash and cash equivalents, beginning of year			—		—
Cash and cash equivalents, end of year		$	—	$	—
Supplementary information for cash flows from operating activities					
Interest paid			(7,255)		(7,874)

See accompanying notes to the consolidated financial statements.

1. GENERAL DESCRIPTION OF BUSINESS

Source Energy Services Ltd. and its subsidiaries ("Source" or the "Company") is a company that focuses on the integrated production and distribution of high quality Northern White frac sand, as well as the distribution of other bulk completion materials not produced by Source. Source provides its customers with an end-to-end solution for frac sand supported by its Wisconsin mines and processing facilities, its Western Canadian terminal network and its "last mile" logistics capabilities. Source also provides storage and logistics services for other bulk oil and gas well completion materials and has developed Sahara, a proprietary wellsite mobile sand storage and handling system.

The Company is incorporated under the Alberta Business Corporations Act and the head and principal office is located at 500, 1060 - 7th Street SW, Calgary, Alberta, T2R 0C4.

2. BASIS OF PRESENTATION

Statement of compliance

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

The policies applied in the consolidated financial statements are based on IFRS issued and outstanding as at December 31, 2021. The consolidated financial statements were authorized for issuance by the Board of Directors (the "Board") on March 9, 2022.

Basis of measurement

The consolidated financial statements have been prepared on a historical cost basis, except for the revaluation of certain financial assets and liabilities to estimated fair value.

Use of estimates and judgments

The preparation of the consolidated financial statements in conformity with IFRS requires management to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates. Estimates and judgments are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. Revisions to accounting estimates are recognized in the period in which the estimates are revised and in any future years affected.

Allowance for doubtful accounts

The Company performs ongoing credit evaluations of its customers and grants credit based on a review of historical collection experience, current aging status, the customer's financial condition and anticipated industry conditions. Customer payments are regularly monitored. A provision for doubtful accounts is established based on the expected credit loss model under IFRS 9.

Inventories

The Company evaluates its inventory to ensure it is carried at the lower of average cost and net realizable value. Allowances are made against obsolete or damaged inventories and charged to cost of sales. The reversal of any write-down of inventory arising from an increase in net realizable value would be recognized as a reduction in cost of sales in the period in which the reversal occurred.

Depreciation

The amounts recorded for depreciation of property and equipment are based on estimates of the useful lives of the assets and residual values. The estimated residual value and useful lives of property and equipment are reviewed at the end of each reporting period and adjusted if required.

Decommissioning liabilities

The amounts recorded for decommissioning liabilities are based on the Company's mining activities and the estimated costs to abandon and reclaim the land and facilities, the estimated time period in which these costs will be incurred in the future and the discount and inflation rates. Any changes to these estimates could change the amount of decommissioning liability and may materially impact the consolidated financial statements in future periods.

Income taxes

The amounts recorded for deferred income taxes are based on estimates regarding the timing of the reversal of temporary differences and tax rates currently substantively enacted. Legislation and regulations in the various jurisdictions that the Company operates in are subject to change and differing interpretations require management judgment. Income tax filings are subject to audits, re-assessments and changes in facts, circumstances and interpretations of the standards could result in a material change in the Company's provision for income taxes. As such, income taxes are subject to measurement uncertainty including judgment regarding the recognition or derecognition of deferred tax assets.

Share-based compensation

The Company's compensation plans include the following award types: stock option, restricted share unit ("RSU"), performance share unit ("PSU"), deferred share unit ("DSU") and share appreciation right ("SAR"). DSUs and SARs are cash-settled awards and RSUs and PSUs may be settled in common shares but are expected to be settled for cash. As such, these awards are considered liability-settled awards for accounting purposes. The fair value of stock options and SARs are estimated using the Black-Scholes option pricing model, which includes underlying assumptions related to the risk-free interest rate, average expected unit life, estimated forfeitures and estimated volatility of Source's share price.

Cash-generating units

The determination of a cash-generating unit ("CGU") is based on management's judgment regarding geographical proximity, shared equipment and mobility of equipment. Management has determined that the Company's operations represent one CGU.

Impairment of non-financial assets

Assets that are subject to depreciation are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognized for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs of disposal and value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are largely independent cash inflows (CGUs). The recoverable amount of a CGU is determined using an approach which considers a discounted cash flow model and an earnings multiple approach. The discounted cash flow model incorporates significant assumptions including a revenue growth rate and discount rate. The earnings multiple approach uses earnings before interest, taxes, depreciation and amortization less corporate expenses and comparable market multiples to determine the recoverable amount of the CGU. Prior impairments of non-financial assets are reviewed for possible reversal at each reporting date.

Embedded derivatives

An embedded derivative is a component of a contract that modifies the cash flows of the contract. Embedded derivatives are separated from the contract and accounted for as derivative liabilities or assets. Embedded derivatives are measured at fair value through profit or loss. The fair value of the derivatives may be based on prices or valuation techniques that require inputs that are not based on observable market data.

Revenue recognition

Contractual arrangements for revenue may have multiple contractual elements within them, resulting in complex recognition in the financial statements. The contractual elements which require significant consideration may include embedded derivatives, contract liabilities, take-or-pay commitments and leasing arrangements. Significant judgement is required in identifying and assessing the appropriate accounting recognition for each contractual element identified within these contractual arrangements.

Impact of COVID-19

In March 2020, the coronavirus ("COVID-19") outbreak was declared a global pandemic by the World Health Organization. Measures enacted to prevent the spread of the virus resulted in global business disruption with significant economic repercussions and caused uncertainty and extraordinary volatility in the oil and gas industry, particularly in the Western Canadian Sedimentary Basin.

In 2020, Source undertook numerous initiatives to enhance liquidity and address the challenges resulting from the significant downturn in the Western Canadian oil industry, further impacted by COVID-19. Source completed its Recapitalization Transaction (as defined in Note 13) and implemented operational cost reduction measures to mitigate the impact of the volatile operating environment. The extent to which COVID-19 will impact the Company's operating environment remains uncertain and cannot be predicted, but adverse impacts may result in decreased revenues, increased counterparty credit risk and uncertainties with respect to debt covenant compliance and liquidity. Source continues to assess the potential impact of COVID-19 on the estimates and judgements used in determining the value of its assets, liabilities and equity. The following discussion sets forth management's most critical estimates and assumptions in determining these values.

3. SIGNIFICANT ACCOUNTING POLICIES

Inventories

Inventories represent unprocessed mined sand, work in progress and sand available for shipment, as well as spare parts and supplies. The Company values inventory at the lower of cost or net realizable value.

Cost is determined using the weighted average cost method. Cost includes the cost of mining of the sand as well as the direct labor costs, utility costs, transportation costs and other processing costs to wash and dry the sand, as well as depreciation directly attributable to production equipment and depreciation of capitalized stripping activities.

Net realizable value is the estimated selling price less applicable selling expenses. When the weighted average cost of inventories exceeds the net realizable value, inventory is written down to the net realizable value. All write-downs are charged to cost of goods sold. The amount of the write-down may be reversed (up to original amount of the write-down) when there is a change in economic circumstances.

Foreign currency translation

The consolidated financial statements are presented in Canadian dollars, which is the Company's presentation currency. Each entity of the consolidated financial statements is measured using the currency of the primary economic environment in which the entity operates (the "functional currency"). The financial statements of the entities that have a different functional currency are translated into Canadian dollars. Assets and liabilities are translated at the rate of exchange at the statement of financial position date, revenue and expenses are translated at the average exchange rate for the period (as this is considered a reasonable approximation of actual rates), and gains and losses in translation are recognized in shareholders' equity as a cumulative translation adjustment.

Transactions in currencies that differ from an entity's functional currency are translated into the functional currency using the exchange rate prevailing on the transaction date. Foreign exchange gains and losses resulting from the settlement of foreign currency translation and from the translation at period-end exchange rates of monetary assets and liabilities denominated in currencies other than an entity's functional currency are recognized in the consolidated statements of operations and comprehensive income (loss)**.**

Property, plant and equipment

All costs directly associated with the purchase and development of property, plant and equipment are capitalized and reflected at cost less accumulated depreciation and net impairment losses. Costs of replacing parts of property, plant and equipment are capitalized only when they increase the future economic benefits embodied in the specific assets to which they relate. All other expenditures are recognized in income as incurred. The carrying amount of any replaced or sold component is derecognized. The costs of the day-to-day servicing of property and equipment are recognized in the consolidated statements of operations and comprehensive income (loss) as incurred.

Exchanges or swaps of property, plant and equipment are measured at fair value unless the transaction lacks commercial substance or neither the fair value of the asset received nor the asset given up can be reliably estimated. When fair value is not used, the cost of the acquired asset is measured at the carrying amount of the asset given up. Any gains or losses from the divestiture of property and equipment are recognized in the consolidated statements of operations and comprehensive income (loss).

Depreciation of property, plant and equipment is provided using the straight line method at the following annual rates approximating their estimated useful lives in years:

Buildings	20
Equipment	7 - 20
Vehicles	5 - 7
Computer hardware and software	3 - 5

Depreciation of an asset or an asset under construction begins when it is available for use. Depreciation of an asset ceases at the earlier of the date that the asset is classified as held for sale and the date that the asset is derecognized. Depreciation does not cease when the asset becomes idle or is retired from active use unless the asset is fully depreciated.

The Company allocates the amount initially recognized in respect of an item of property and equipment to its significant components and depreciates separately each such component where applicable.

The Company adheres to IFRIC 20 "stripping costs in the production phase of a surface mine". During the production phase of the mine, stripping costs incurred that provide access to a component of reserves that will be produced in future periods and that would not have otherwise been accessible are capitalized. The costs qualifying for capitalization are those costs directly incurred to perform the stripping activity that improves access to the resource body. The stripping activity asset is included as part of the carrying amount of the mining property. Capitalized stripping costs are amortized on a straight-line basis over the production period to which they relate.

Impairment of non-financial assets

The carrying amounts of the Company's non-financial assets, other than deferred tax assets, are reviewed for indicators of impairment at each reporting period. If indicators of impairment exist, the recoverable amount of the assets is estimated. For purposes of assessing impairment, property, plant and equipment are grouped into CGUs, defined as the lowest levels for which there are separately identifiable independent cash inflows.

The recoverable amount of a CGU is the greater of its fair value less costs to dispose and its value in use. Fair value is determined to be the amount for which the asset would be sold in an arm's length transaction between knowledgeable and willing parties. Value in use is determined by estimating the present value of the future net cash flows to be derived from the continued use of the CGU in its present form. These cash flows are discounted at a rate based on the time value of money and risks specific to the CGU.

An impairment loss is recognized if the carrying amount of an asset or its CGU exceeds its recoverable amount. An impairment loss recognized in respect of a CGU is allocated to reduce the carrying amounts of the assets in the CGU on a pro rata basis. Impairment losses are recognized in the consolidated statements of operations and comprehensive income (loss).

Impairment losses recognized in prior years are assessed at each reporting date for any indications that the loss has decreased or no longer exists. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortization, if no impairment loss had been recognized.

Leases and right-of-use assets

Lessee

At the commencement of a lease, the Company recognizes a right-of-use ("RoU") asset and a lease liability. The lease liability is measured at the present value of the lease payments, which are discounted using the Company's incremental borrowing rate when the interest rate implicit in the lease cannot be readily determined. Each lease payment is allocated between the liability and finance expense. Lease payments included in the measurement of the lease liability are comprised of the following:

- fixed payment less any lease incentives;
- variable lease payments that depend on an index or rate;
- amounts expected to be paid for residual value guarantees;
- exercise price of a purchase option if the Company is reasonably certain to exercise; and
- penalties for termination if the lease term reflects the exercise of the option to terminate.

RoU assets are measured at cost which includes the following:

- the amount of the initial measurement of the lease liability;
- lease payments made at or before the commencement date, less any lease incentives received; and
- initial direct costs.

RoU assets are depreciated over the shorter of an asset's useful life and the lease term on a straight-line basis. The Company's lease contracts may contain termination, renewal and/or purchase options which are evaluated by the Company on a regular basis. The majority of renewal options available extend lease terms from one to five years and are accounted for when the Company is reasonably certain that it will exercise one of these options.

The Company enters into short-term and long-term lease arrangements for rail cars and locomotives, vehicles and equipment and real estate. The Company determines whether or not the contract contains a lease at inception. Payments associated with short-term leases for certain classes of assets and leases of low-value assets are recognized on a straight-line basis in the consolidated statements of operations and comprehensive income (loss) in the period in which they are incurred.

Lessor

At the commencement of a lease, the Company performs an assessment to determine if the lease qualifies as a finance lease or an operating lease. A lease that transfers substantially all risks and rewards is classified as a finance lease and a lease that does not transfer substantially all risks and rewards is classified as an operating lease. For a finance lease, a receivable equal to the net investment in the lease is measured as the present value of the lease payments using the implicit rate in the lease.

In instances when the Company is an intermediate lessor, an assessment is performed to determine the classification of the sublease with reference to the RoU asset arising from the lease rather than reference to the underlying asset. For a sublease that transfers substantially all risks and rewards, it is classified as a finance lease; otherwise it is classified as an operating lease and rental income is recognized on a straight-line basis over the lease term.

A sublease classified as a finance lease is recognized as a receivable equal to the net investment in the lease. The RoU asset is derecognized and the difference between the RoU asset and the net investment is recognized in the consolidated statements of operations and comprehensive income (loss). At inception of the sublease, the net investment is measured at the present value of the lease payments using the interest rate implicit in the sublease. If the implicit rate cannot be determined, the discount rate used for the head lease is used to measure the net investment in the sublease. Finance income is recognized over the lease term at a constant rate of return on the net investment in the lease.

Provisions and contingent liabilities

Provisions are recognized by the Company when all of the following apply: (i) it has a legal or constructive obligation as a result of past events, (ii) it is probable that an outflow of economic resources will be required to settle the obligation and (iii) a reliable estimate can be made of the amount of that obligation. The obligation is not recorded and is disclosed as a contingent liability if any of the following apply: (i) it is not probable that an outflow will be required, (ii) the amount cannot be estimated reliably, or (iii) the existence of the outflow can only be confirmed by the occurrence of a future event.

Decommissioning provision

Decommissioning provision is recognized for decommissioning and restoration obligations associated with the Company's mining reserves. The best estimate of the expenditure required to settle the present obligations at the statement of financial position date is recorded on a discounted basis using the pre-tax risk-free interest rate at each reporting date. The future cash flow estimates are adjusted to reflect the risks specific to the liability. The value of the provision is added to the carrying amount of the associated property, plant and equipment asset and is depreciated over the useful life of the asset. The provision is accreted over time through charges to finance expenses. Changes in the future cash flow estimates resulting from revisions to the estimated timing or amount of undiscounted cash flows or the discount rate are recognized as changes in the decommissioning provision and related assets. Actual decommissioning expenditures up to the recorded liability at the time are charged against the provision as the costs are incurred. Any differences between the recorded liability and the actual costs incurred are recorded as a gain/loss in the consolidated statements of operations and comprehensive income (loss).

Income taxes

Current and deferred income tax expenses are recognized in the consolidated statements of operations and comprehensive income (loss) except to the extent that it relates to items recognized directly in equity or other comprehensive income.

Current income taxes for current and prior periods are measured at the amount expected to be payable or recoverable from the taxation authorities based on the income tax rates enacted at the end of the period.

Deferred income tax is recognized using the liability method, providing for temporary differences between the carrying amounts of assets and liabilities and the carrying amounts used for taxation purposes. Deferred income tax liabilities are generally recognized for all taxable temporary differences. Deferred tax assets are recognized for all temporary differences deductible to the extent future recovery is probable. The carrying amount of deferred income tax assets is reviewed at the end of each reporting period and reduced to the extent that it is no longer probable that sufficient taxable income will be generated to allow for all or part of the asset to be recovered. Deferred income tax balances are calculated using enacted or substantively enacted tax rates. Deferred income tax balances are adjusted to reflect changes in income tax rates that are enacted or substantively enacted with the adjustment being recognized in the period the change occurs, except items recognized in equity.

Deferred tax assets and liabilities are offset if both of the following thresholds are met: (i) there is a legally enforceable right to offset and (ii) the deferred tax assets and liabilities either relate to income taxes levied by the same taxation authority on the same taxable entity, or the deferred tax assets and liabilities relate to income taxes levied by the same taxation authority on different taxable entities where such different taxable entities either intend to settle current tax liabilities and assets on a net basis, or will have their tax assets and liabilities realized simultaneously.

Revenue recognition

The Company's revenue, which is comprised principally of sand sales and other services, is generally subject to contractual arrangements, which specify price and general terms and conditions. The Company recognizes sand sales when the contractual obligations are satisfied (typically when control of the product is transferred), while also considering if it has retained any material involvement in the sand being sold and if the revenue and costs related to the sale can be measured reliably. Revenue for third-party sand and chemical distribution is recognized based on contractual arrangements or when services have been completed. Revenue for wellsite solutions is recognized when services are provided. Revenue for rental of storage facilities is recognized on a monthly basis.

The Company offers certain arrangements whereby customers can purchase products and services together. Where such bundled arrangements exist, the amount of the transaction price allocated to each performance obligation is based upon the relative stand-alone selling prices of each distinct product or service in the contract. The best evidence of a stand-alone selling price is the observable price of a product or service when the Company sells that product or service separately in similar circumstances and to similar customers.

When a stand-alone selling price is not directly observable, the Company estimates using the residual approach method to determine a value that most reasonably reflects the selling price that might be achieved in a stand-alone contract with a customer.

Finance income and expenses

Finance income, consisting of interest income, is recognized as it accrues in the consolidated statements of operations and comprehensive income (loss), using the effective interest method.

Finance expense comprises interest expense on borrowings, costs incurred to obtain financing and impairment losses recognized on financial assets. Amounts paid to financial institutions for the purpose of borrowing funds are capitalized upon recognition and are offset against the outstanding obligation to the financial institution. These costs are amortized over the remaining term of the facility placed.

Earnings (loss) per share

Earnings (loss) per share is calculated by dividing the profit or loss attributable to common and Class B shareholders of the Company by the weighted average number of common shares and Class B shares outstanding during the period. Diluted earnings per share is calculated by adjusting the earnings and number of shares for the effects of dilutive options and other dilutive potential shares. The effects of anti-dilutive potential shares are ignored in calculating diluted earnings per share. All options are considered anti-dilutive when the Company is in a loss position. As at December 31, 2021, no options or Class B shares were outstanding.

Basis of consolidation

The consolidated financial statements include the accounts of Source Energy Services Ltd. and its subsidiaries, which are entities over which Source has control. Control exists when the Company is exposed to, or has right to, variable returns from its involvement with an entity and has the ability to affect those returns through its power over the entity. Subsidiaries are consolidated from the date of acquisition, being the date on which the Company obtains control, and continue to be consolidated until the date that such control ceases. The financial statements of the subsidiaries are prepared for the same reporting period as Source, and the accounting policies are aligned with the policies adopted by Source. All intercompany balances and income and expenses have been eliminated upon preparation of the consolidated financial statements. As at December 31, 2021, all subsidiaries are 100% owned. Prior to 2021, Source Energy Services Canada LP had a 3.74% non-controlling interest which was eliminated upon the conversion of the Class B shares prior to completion of the Recapitalization Transaction.

Non-controlling interests

Non-controlling interests represent equity interests in subsidiaries owned by outside parties. The share of net assets of subsidiaries attributable to non-controlling interests is presented as a component of equity. Losses applicable to the non-controlling interests in a subsidiary are allocated to the non-controlling interests, even if doing so causes the non-controlling interests to have a deficit balance.

Share-based payments

The Company has various share-based compensation plans for employees, including an option plan, renewed as of March 18, 2021, which is available to directors, officers and certain employees as determined by the Company's Board. The option plan allows for the granting of options to purchase common shares to a maximum number equal to 10% of the issued and outstanding common shares of the Company. The price of each share purchase option granted is set by the Company's Board based on the market value of the Company's shares on the date of the grant.

During the year, the Company authorized a share appreciation rights plan which is available to certain employees, effective March 18, 2021. A SAR gives the employee the right to receive a cash payment equal to the difference between fair market value of the Company's common shares at the time of exercise and the dollar amount set out in the SAR agreement. The SARs are settled for cash payment and accordingly are considered liability-settled awards for accounting purposes.

Under these plans, any cumulative expense is calculated at each statement of financial position date before vesting, representing the extent to which the vesting period has expired and management's best estimate of the number of awards that will ultimately vest.

The fair values of options and SARs are measured using the Black-Scholes valuation model. The model requires the input of assumptions including historical forfeiture rates and expected volatility based on the historical stock price of the Company. The expected term of options and SARs represents the period of time that awards granted are expected to be outstanding. The risk-free rate is based on the Government of Canada bond yields with a remaining term equal to the expected life of the awards used in the Black-Scholes valuation model. The fair value of the options is measured at the grant date. The fair value of the SARs is measured at the grant date and subsequently remeasured at each reporting period.

The Company also has share-based compensation plans that allow for DSUs, RSUs and PSUs to be granted to directors and certain employees. The DSUs, RSUs and PSUs are expected to be settled for cash payment and accordingly are considered liability-settled awards for accounting purposes.

Financial Instruments

The Company determines the classification of its financial instruments at initial recognition and records the instruments at their fair value plus, for those instruments not subsequently measured at fair value, directly attributable transaction costs. Financial assets and financial liabilities are recognized on the Company's consolidated statement of financial position when the Company becomes party to the contractual provisions of the instrument. Financial assets are derecognized when the contractual rights to the cash flows from the financial asset expire or when the contractual rights to those assets are transferred. Financial liabilities are derecognized when the obligation specified in the contract is discharged, cancelled or expired.

The Company considers whether a contract contains an embedded derivative when it first becomes a party to it. Embedded derivatives are separated from the host contract which is not measured at fair value through profit and loss when the analysis shows that the economic characteristics and risks of embedded derivatives are not closely related to those of the host contract.

Financial assets

Subsequent measurement of financial assets depends on the Company's business model for managing the asset and the cash flow characteristics of the asset:

a. Amortized cost: Assets that are held for collection of contractual cash flows where those cash flows represent solely payments of principal and interest are measured at amortized cost. Interest income from these financial assets is included in finance income using the effective interest rate method. Any gain or loss arising on derecognition is recognized directly in profit or loss and presented together with foreign exchange gains and losses;

b. Fair value through profit or loss: Assets that do not meet the criteria for amortized cost or fair value through other comprehensive income are measured at fair value through profit or loss. A gain or loss on a financial asset that is subsequently measured at fair value through profit or loss is recognized in profit or loss and presented net within other gains or losses in the period in which it arises; and

c. Fair value through other comprehensive income: Instruments that are held for collection of contractual cash flows and for selling the financial instruments, where the instruments' cash flows represent solely payments of principal and interest, are measured at fair value through other comprehensive income. When the financial instrument is derecognized, the cumulative gain or loss previously recognized in other comprehensive income is reclassified from equity to profit or loss and recognized in other gains and losses.

Financial asset impairment

Financial assets are assessed for impairment using an expected credit loss model as required by IFRS 9. The Company has applied the simplified approach to recognize lifetime expected credit losses for its financial assets measured at amortized cost. As such, the loss allowance for a financial asset is recorded at an amount based on the lifetime expected credit loss at each reporting period.

Financial liabilities

Financial liabilities are subsequently measured at amortized cost using the effective interest method, other than derivative financial instruments.

Derivative financial instruments

The Company enters into derivative financial instruments to mitigate its exposure to foreign exchange fluctuations. Derivative financial instruments are classified as fair value through profit or loss.

Government assistance

Claims for assistance under various government grant programs are recorded as a reduction of the cost of the related expenses in the period in which the eligible expenditures are incurred. Where government grants are provided in the form of a forgivable loan, proceeds are recorded as a financial liability and not recognized as a reduction of the cost of the related expenses incurred until reasonable assurance of forgiveness has been obtained. When forgiveness is obtained subsequent to the year in which the related expenses were incurred, the amount forgiven is recognized in other income.

(All amounts are in thousands of Canadian dollars, unless otherwise noted)

Newly Adopted Accounting Policies

The following amendments have been issued by the IASB and were adopted by the Company effective for the fiscal year beginning January 1, 2021:

Standard	Description of change
Interest rate benchmark reform - Phase 2 (Amendments to IFRS 9, IAS 39, IFRS 7, IFRS 4 and IFRS 16)	The amendments introduce a practical expedient to account for a change in the basis for determining the contractual cash flows of financial instruments that are affected by IBOR reform.
COVID-19 related rent concessions (Amendment to IFRS 16)	The amendment provides a practical expedient that relieves a lessee from determining whether a COVID-19 rent-related concession is a lease modification.

The Company completed its assessment of the impact of the amendments and concluded that they do not have a material impact on the consolidated financial statements.

Future Accounting Policy Changes

The following amendments to accounting standards, issued by the IASB, are effective for fiscal years beginning on or after January 1, 2022:

Standard	Description of change
Classification of Liabilities as Current or Non-current (Amendment to IAS 1)	This amendment clarifies the classification requirements for non-current liabilities.
Deferred Tax related to Assets and Liabilities arising from a Single Transaction (Amendment to IAS 12)	This amendment changes the deferred tax initial recognition exemption, which does not apply to transactions in which both deductible and taxable temporary differences arise on initial recognition that result in the recognition of deferred tax assets and liabilities in the same amount.
Property, Plant and Equipment - Proceeds before intended use (Amendment to IAS 16)	This amendment states that deducting proceeds from selling items produced while bringing an asset to its intended use from the cost of the asset is prohibited and shall be recognized in profit or loss.
Provisions, Contingent Liabilities and Contingent Assets - Onerous Contracts (Amendment to IAS 37)	This amendment clarifies the costs that shall be included in determining the cost of fulfilling a contract when assessing whether a contract is onerous.
Disclosure of Accounting Policies (Amendment to IAS 1)	This amendment states that a complete set of financial statements shall disclose material, rather than significant, accounting policy information.
Definition of Accounting Estimates (Amendment to IAS 8)	This amendment introduces a new definition for accounting estimates.

The Company intends to adopt the amendments on their respective effective dates and the revisions are not expected to have a material impact on the consolidated financial statements.

4. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT

(a) Risk management overview

The Company's activities expose it to a variety of financial risks including credit risk, liquidity risk and market risk. Further quantitative disclosures are included throughout the consolidated financial statements. The Company employs risk management strategies and polices to ensure that any exposures to risk are in compliance with the Company's business objectives and risk tolerance levels. While the Board has the overall responsibility for the Company's risk management framework, the Company's management has the responsibility to administer and monitor these risks.

(b) Classification of financial instruments

The Company categorizes the following financial instruments at amortized cost:

	December 31, 2021	December 31, 2020
Financial instruments at amortized cost		
Trade and other receivables	43,499	33,644
Trade and other payables	29,430	33,995
Lease liabilities	38,436	42,329
Long-term debt (includes current portion)	183,031	147,281

Refer to Note 4(c) for financial instruments carried at fair value through profit and loss.

(All amounts are in thousands of Canadian dollars, unless otherwise noted)

(c) Fair value of financial instruments

The fair values of accounts receivable and accounts payable approximate their carrying values due to the short-term maturity of those instruments. The fair value of the credit facilities approximates their carrying value as they bear interest at floating market rates consistent with market rates for similar debt.

The Company analyzes financial instruments carried at fair value by valuation method. The different levels have been defined as follows:

Level 1: Values based on unadjusted quoted prices in active markets for identical assets or liabilities, accessible at the measurement date.

Level 2: Values based on quoted prices in markets that are not active or model inputs that are observable either directly or indirectly for substantially the full term of the asset or liability.

Level 3: Values based on prices or valuation techniques that require inputs for the asset or liability that are not based on observable market data (unobservable inputs).

A financial instrument is classified as Level 3 if one or more of its unobservable inputs may significantly affect the measurement of its fair value. Appropriate inputs are chosen so that they are consistent with market evidence or management judgment. Due to the unobservable nature of the inputs, there may be uncertainty about the value of Level 3 financial instruments.

December 31, 2021	Carrying amount	Fair Value Level 1	Fair Value Level 2	Fair Value Level 3
Financial assets at fair value through profit and loss:				
Derivative asset(1)	$ 1,718	$ —	$ 1,718	$ —
Financial liabilities at amortized cost:				
Senior secured notes(1)	$ 147,350	$ —	$ 90,325	$ —

Note:
(1) In October 2021, the Company entered into currency derivative agreements (refer to Note 4(f) for additional information).

December 31, 2020	Carrying amount	Fair Value Level 1	Fair Value Level 2	Fair Value Level 3
Financial assets at fair value through profit and loss:				
Derivative asset	$ 1,471	$ —	$ —	$ 1,471
Financial liabilities at amortized cost:				
Senior secured notes	$ 125,493	$ —	$ —	$ 126,044

(d) Credit risk

Credit risk is the risk of financial loss to the Company if a customer or counterparty to a financial instrument fails to meet its contractual obligations. Substantially all of the Company's trade and other accounts receivable are due from purchasers of proppants and logistics services and are subject to normal industry credit risk. Significant changes in industry conditions will increase the risk of not collecting receivables. Management believes the risk is materially mitigated by the size and reputation of the companies to which they extend credit.

The Company's revenues are generally derived from a group of large and reputable oilfield exploration and production companies and oilfield services customers. Orders for proppants are subject to guidelines established by the Company's credit and collection programs. The Company's five largest customers account for 80% of the revenue for the year ended December 31, 2021, with the three largest making up 66% of revenue (year ended December 31, 2020, five customers accounted for 84%, three customers accounted for 71%). Two of those customers (three for the year ended December 31, 2020) account for 10% or more of total revenue individually in the year ended December 31, 2021.

As at December 31, 2021, the Company's trade and other receivables, net of loss allowances, were comprised of the following:

As at	December 31, 2021	December 31, 2020
Not yet due	$ 41,853	$ 19,712
0 – 30 days	1,616	13,891
31 – 60 days	30	40
61 – 90 days	—	1
91+ days	—	—
Total trade and other receivables	**$ 43,499**	**$ 33,644**

(All amounts are in thousands of Canadian dollars, unless otherwise noted)

The Company performs ongoing credit evaluations of its customers and establishes an allowance for doubtful accounts based on the lifetime expected credit loss provision. The Company uses an allowance matrix to estimate the credit losses of trade receivables which considers historical default rates as well as the days past due.

A loss allowance of $73 was recorded as at December 31, 2021:

As at		**December 31, 2021**		**December 31, 2020**
Balance, beginning of year		272	$	80
Increase (decrease) in loss allowance		10		(17)
Specific provision for receivables deemed uncollectible		(209)		209
Balance, end of year	**$**	**73**	**$**	**272**

The Company's maximum exposure to credit risk is the carrying amount of trade and other receivables, cash and cash equivalents and derivative assets, if applicable. The Company is also exposed to counterparty credit risk with respect to cash and cash equivalents as well as foreign exchange forward contracts. These financial instruments are held with major financial institutions and management believes the investment grade credit ratings of these institutions minimizes this risk.

(e) Liquidity risk

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they become due. The Company's approach to managing liquidity risk includes preparing operating and capital budgets and forecasts and monitoring performance against the budgets and forecasts. The Company may seek additional financing based on the results of these processes. The Company's ongoing liquidity is impacted by various external events and conditions, including foreign currency fluctuations and commodity price fluctuations as well as global economic conditions.

The financial liabilities on the consolidated statements of financial position consist of accounts payable and accrued liabilities, lease liabilities, credit facilities and senior secured notes. The Company manages this risk through detailed monitoring of budgeted and projected operating results and cash requirements.

The Company expects to repay its financial liabilities in the normal course of operations and to fund future operational and capital requirements through operating cash flow, as well as future debt and equity financings. The Company has an amended and restated credit facility to facilitate the management of liquidity risk.

The Company's contractual cash outflows relating to financial liabilities are outlined in the table below:

As at December 31, 2021		**Total**		**2022**		**2023**		**2024**		**2025**		**2026**		**2027 and beyond**
Accounts payable and accruals	$	29,336	$	29,336	$	—	$	—	$	—	$	—	$	—
Lease liabilities(1)	$	39,277	$	13,549	$	9,277	$	6,981	$	4,130	$	1,648	$	3,692
Credit facilities(2)	$	36,406	$	7,500	$	28,906	$	—	$	—	$	—	$	—
Notes payable(3)	$	216,264	$	15,047	$	17,160	$	17,169	$	166,888	$	—	$	—

Notes:
(1) Includes interest for future periods.
(2) The timing and amount of interest payments on such balances will fluctuate depending on balances outstanding and applicable interest rates.
(3) Includes interest for future periods and assumes the Company will pay interest in kind at a rate of 12.5% through February 15, 2022 and subsequently pay interest in cash at 10.5% (refer to Note 10 for additional information).

(f) Market risk

Market risk is the risk that changes in market prices, foreign exchange rates and interest rates will affect the Company's net earnings or the value of financial instruments and are largely outside the control of the Company. The objective of the Company is to manage and mitigate market risk exposures within acceptable limits while maximizing returns. Primary market risks are as follows:

Foreign currency risk

The Company is exposed to currency price risk on sales denominated in United States ("US") dollars to the extent that the receipt of payment of the US denominated accounts receivable are subject to fluctuations in the related foreign exchange rate. In addition, foreign currency risk exists on the cost of manufacturing of inventory for sale to the extent that the payment of those costs are foreign denominated accounts payable and are subject to fluctuations in the foreign exchange rate. Included in accounts receivable and accounts payable and accrued liabilities at December 31, 2021 are $14,696 (December 31, 2020 - $18,490) and $11,065 (December 31, 2020 - $14,924) denominated in foreign currency, respectively. The net effect of each 1% change in foreign exchange would impact net income (loss) by $1,507 for the year ended December 31, 2021 ($849 in 2020).

(All amounts are in thousands of Canadian dollars, unless otherwise noted)

In order to manage exposure to fluctuations in the Canadian to US dollar exchange rate, the Company's policy is to hedge up to certain prescribed maximum amounts of its net US dollar exposure on a monthly basis, as determined by the Company's foreign currency risk management policy, through the purchase of various instruments. As at December 31, 2021, the Company had US dollar foreign exchange forward contracts outstanding that mature during 2022, with notional amounts ranging from US$4,000 per month to US$8,000 per month at 1.2473 to 1.2532 per Canadian dollar. The Company also has contracts in place from January through October 2023, with a notional value of US$2,000 per month at rates of 1.2440 to 1.2446 per Canadian dollar.

Interest rate risk

Interest rate risk is the risk that future cash flows will fluctuate as a result of changes in market interest rates. The Company is exposed to interest rate risk to the extent that changes in market interest rates impact its borrowings under the floating rate credit facility and the senior secured term loan. The Company is exposed to interest rate price risk on the long-term debt that bears interest at floating rates. The net effect of each 1% change in market interest rates would impact the related interest expense (income) for the Company's floating rate borrowings by $364 at December 31, 2021 ($236 at December 31, 2020). The Company had no derivative contracts in place as at or during the years ended December 31, 2021 and 2020 with respect to managing interest rate risk.

(g) Capital management

The Company's capital management policy is to maintain a strong capital base that optimizes the Company's ability to grow, maintain shareholder and creditor confidence and to provide a platform to create value for its common shareholders. The Company's management is responsible for managing the Company's capital and does so through regular reviews of financial information including budgets and forecasts. The Company's directors are responsible for overseeing this process. The Company considers its capital structure to include equity, senior secured notes, credit facilities and leases.

The Company monitors capital based on its current working capital, available bank line, projected cash flow from operations and anticipated capital expenditures. In order to manage its capital structure, the Company prepares annual capital expenditure and operating budgets, which are updated as necessary. The annual and updated budgets are prepared by the Company's management and approved by the Company's Board.

In order to maintain or adjust the capital structure, the Company may issue share capital, seek debt financing and adjust its capital spending to manage its current and projected capital structure. The Company's ability to raise additional debt or equity financing is impacted by external conditions, including global economic conditions. The Company continually monitors economic and general business conditions.

The Company's share capital is not subject to external restrictions; however, the amount of the bank operating facility available for use is determined by levels of accounts receivable and inventory. Pursuant to the amended and restated credit agreement, the Company is subject to externally imposed capital requirements for the asset backed loan ("ABL") facility. Refer to Note 10(b) for additional information.

The Company's capital management policy has not changed during the years ended December 31, 2021 and 2020.

5. SUPPLEMENTAL CASH FLOW INFORMATION

Changes in non-cash operating assets and liabilities for the years ended December 31, 2021 and 2020 were as follows:

		2021		2020
Accounts receivable	$	(9,076)	$	15,680
Prepaid expenses and deposits		(1,320)		(1,914)
Inventory		(6,238)		3,144
Accounts payable and accrued liabilities		(5,056)		(11,291)
Changes in non-cash working capital	**$**	**(21,690)**	**$**	**5,619**

Changes in non-cash investing assets and liabilities for the years ended December 31, 2021 and 2020 were as follows:

		2021		2020
Accounts payable and accrued liabilities	$	442	$	(1,428)
Changes in non-cash working capital	**$**	**442**	**$**	**(1,428)**

(All amounts are in thousands of Canadian dollars, unless otherwise noted)

		Senior secured notes		ABL facility and senior secured term loan
As at December 31, 2019	$	150,028	$	28,657
Cash changes:				
Proceeds		—		61,031
Repayments		—		(66,644)
Non-cash and other changes:				
Extinguishment of debt		(29,100)		—
Interest(1)		97		—
Accretion		3,655		365
Unrealized foreign exchange (gain) loss		—		303
Financing costs incurred		(658)		(1,546)
As at December 31, 2020	$	124,022	$	22,166
Cash changes:				
Proceeds		—		103,279
Repayments		—		(90,169)
Non-cash and other changes:				
Interest(1)		18,680		—
Accretion		3,221		631
Unrealized foreign exchange (gain) loss		—		(440)
Financing costs incurred		(44)		(188)
As at December 31, 2021	**$**	**145,879**	**$**	**35,279**

Note:
(1) The Company has paid interest in kind, at a rate of 12.5%, for all quarterly interest payments in 2021. Refer to Note 10 for additional information.

6. INVENTORIES

Inventory consists of three main classifications:

As at		**December 31, 2021**		**December 31, 2020**
Unprocessed sand and work in progress	$	32,613	$	28,519
Sand available for shipment		20,386		21,706
Spare parts and supplies		3,338		3,242
Total inventories	**$**	**56,337**	**$**	**53,467**

Spare parts and supplies are for routine facilities maintenance. Included in the inventory balance is depreciation expense related to sand-producing properties of $8,722 as at December 31, 2021 (December 31, 2020 - $10,021). The total amount of inventory expensed through cost of sales during the year ended December 31, 2021 was $207,272 (year ended December 31, 2020 - $158,791). No inventory write-downs or reversals of prior write-downs were recorded during the year ended December 31, 2021.

(All amounts are in thousands of Canadian dollars, unless otherwise noted)

7. PROPERTY, PLANT AND EQUIPMENT

	Land & Building	Equipment & Vehicles	Other	Construction in Progress	Mine Preparation Costs	Total
Cost						
Balance as at December 31, 2019	$ 205,901	$ 197,016	$ 6,287	$ 22,586	$ 13,287	$ 445,077
Additions	559	150	—	2,256	1,341	4,306
Disposals	—	(268)	(4)	(248)	—	(520)
Completed construction in progress	4	1,930	137	(2,071)	—	—
Transfers[1]	—	(1,171)	—	—	—	(1,171)
Exchange differences	(3,167)	(2,807)	(74)	(119)	(331)	(6,498)
Balance as at December 31, 2020	$ 203,297	$ 194,850	$ 6,346	$ 22,404	$ 14,297	$ 441,194
Additions	385	77	—	3,110	3,330	6,902
Disposals	(34)	(158)	—	—	—	(192)
Completed construction in progress	257	2,141	19	(2,417)	—	—
Exchange differences	(633)	(575)	(15)	(21)	(17)	(1,261)
Balance as at December 31, 2021	**$203,272**	**$196,335**	**$6,350**	**$23,076**	**$17,610**	**$446,643**

Note:
(1) Reflects transfers of RoU assets.

	Land & Building	Equipment & Vehicles	Other	Construction in Progress	Mine Preparation Costs	Total
Accumulated depreciation						
Balance as at December 31, 2019	$ (58,101)	$ (73,363)	$ (5,365)	$ —	$ (11,315)	$ (148,144)
Depreciation	(8,029)	(9,497)	(448)	—	(3,144)	(21,118)
Impairment	(75,371)	(67,565)	(409)	—	—	(143,345)
Disposals	—	263	2	—	—	265
Transfers[1]	—	166	—	—	—	166
Exchange differences	5,844	5,598	83	—	384	11,909
Balance as at December 31, 2020	$ (135,657)	$ (144,398)	$ (6,137)	$ —	$ (14,075)	$ (300,267)
Depreciation	(5,416)	(7,063)	(101)	—	(2,819)	(15,399)
Disposals	30	150	—	—	—	180
Exchange differences	366	369	14	—	29	778
Balance as at December 31, 2021	**$ (140,677)**	**$ (150,942)**	**$ (6,224)**	**$ —**	**$ (16,865)**	**$ (314,708)**
Carrying amounts						
December 31, 2020	$ 67,640	$ 50,452	$ 209	$ 22,404	$ 222	$ 140,927
December 31, 2021	**$ 62,595**	**$ 45,393**	**$ 126**	**$ 23,076**	**$ 745**	**$ 131,935**

Note:
(1) Reflects transfers of RoU assets.

Assets under construction represent facilities that are being built at year end and are not amortized until the asset is deemed to be ready for use. Once deemed ready for use, the assets under construction will be allocated to their corresponding capital asset group and commence depreciating. In 2020, as a result of the weakening economic climate due to COVID-19 and the decrease in global demand for crude oil, the Company carried out an assessment of the recoverable value of its operations and recognized an impairment expense of $143,656. No indicators of impairment or impairment reversal were noted as at December 31, 2021.

(All amounts are in thousands of Canadian dollars, unless otherwise noted)

8. RIGHT-OF-USE ASSETS

	Land & Building	Equipment & Vehicles	Rail cars	Total
Cost				
Balance as at December 31, 2019	$ 8,168	$ 14,520	$ 54,650	$ 77,338
Additions(1)	1,126	7,748	(11,117)	(2,243)
Expired leases	(772)	(5,781)	(1,358)	(7,911)
Transfers(2)	—	1,171	—	1,171
Exchange differences	(12)	(393)	(521)	(926)
Balance as at December 31, 2020	$ 8,510	$ 17,265	$ 41,654	$ 67,429
Additions(3)	(164)	7,223	528	7,587
Expired leases	(1,721)	(717)	(263)	(2,701)
Exchange differences	(3)	(58)	(177)	(238)
Balance as at December 31, 2021	**$ 6,622**	**$ 23,713**	**$ 41,742**	**$ 72,077**

Notes:
(1) Includes lease modifications for certain leases completed in the prior year (refer to Note 11 for additional information related to the modifications).
(2) Reflects transfers of RoU assets from property, plant, and equipment.
(3) On November 15, 2021, the Company entered into a sublease agreement with a third party to lease the Company's previous head office location. The Company has classified the sublease as a finance lease due to the sublease term being equal to the remaining term of the head lease. As a result, the $1,963 net book value of the original RoU asset was derecognized and a lease receivable of $803 was recorded, resulting in a loss of $1,159.

	Land & Building	Equipment & Vehicles	Rail cars	Total
Accumulated depreciation				
Balance as at December 31, 2019	$ (1,583)	$ (7,279)	$ (12,340)	$ (21,202)
Depreciation	(2,638)	(7,285)	(11,186)	(21,109)
Expired leases	772	5,781	1,358	7,911
Transfers(1)	—	(166)	—	(166)
Exchange differences	9	188	727	924
Balance as at December 31, 2020	(3,440)	(8,761)	(21,441)	(33,642)
Depreciation	(2,159)	(5,593)	(6,596)	(14,348)
Expired leases	1,721	717	263	2,701
Exchange differences	—	(3)	29	26
Balance as at December 31, 2021	**$ (3,878)**	**$ (13,640)**	**$ (27,745)**	**$ (45,263)**
Carrying amounts				
December 31, 2020	$ 5,070	$ 8,504	$ 20,213	$ 33,787
December 31, 2021	**$ 2,744**	**$ 10,073**	**$ 13,997**	**$ 26,814**

Note:
(1) Reflects transfers of RoU assets from property, plant and equipment.

(All amounts are in thousands of Canadian dollars, unless otherwise noted)

9. INCOME TAXES

During 2020, the Government of Alberta enacted new legislation to accelerate the reduction of the provincial corporate income tax rate from 12% to 8%, resulting in a combined federal and provincial corporate tax rate of 23% in 2021. Deferred income tax benefits have not been recognized in respect of temporary differences.

The following table reconciles the Company's expected income tax expense relative to the current effective Canadian statutory rate of 23% (2020 - 24%) for the years indicated:

		2021		2020
Loss before income taxes	$	(24,403)	$	(154,116)
Statutory income tax rate		23.00 %		24.00 %
Expected income taxes		(5,613)		(36,988)
Increase (decrease) in taxes from:				
Non-taxable income		(719)		—
Non-deductible expenses		443		(5,325)
Share-based compensation		40		3
Unrealized foreign exchange and derivatives		(112)		—
Prior period adjustments		(2,443)		1,762
Unrecognized deferred tax assets		10,982		70,490
Provincial tax rate change		—		740
Rate differential on foreign activities		(2,487)		351
Other		(91)		317
Total income tax expense (recovery)	**$**	**—**	**$**	**31,350**

Significant components of deferred income tax include:

As at		**December 31, 2021**		**December 31, 2020**
Difference between tax and reported amounts for depreciable assets	$	20,119	$	21,019
Finance fees		1,433		2,155
Foreign exchange on loans		13,590		9,742
Tax loss carryforwards recognized		35,366		26,380
Decommissioning provision		2,163		2,535
Mine development costs		688		709
Unrecognized deferred tax assets		(74,652)		(64,039)
Other		1,293		1,499
Deferred income tax asset	**$**	**—**	**$**	**—**

The movements in deferred tax balances during the year are as follows:

As at		**December 31, 2021**		**December 31, 2020**
Opening deferred tax asset	$	—	$	30,574
Recognized in net income		—		(31,350)
Exchange differences		—		776
Closing deferred tax asset	**$**	**—**	**$**	**—**

The Company has Canadian and foreign non-capital losses as at December 31, 2021 of $117,903 (December 31, 2020 - $94,990) and $30,136 (December 31, 2020 - $13,757), respectively. Canadian and foreign losses begin to expire in 2037.

(All amounts are in thousands of Canadian dollars, unless otherwise noted)

10. LONG-TERM DEBT

As at		December 31, 2021		December 31, 2020
Senior secured notes, due March 15, 2025, bearing interest at 10.5% per annum (a)	$	147,350	$	125,493
Derivative asset for senior secured notes prepayment options (a)		—		(1,471)
ABL facility maturing September 2023. Interest is based on floating rates dependent upon the form of advance drawn (b)		18,406		3,736
Senior secured term loan due September 2023, bearing interest at prime plus 6.0% per annum (c)		18,000		20,000
Unamortized debt issuance costs for the credit facilities (b)		(1,127)		(1,570)
Other long-term debt (d)		402		1,093
Total long-term debt	**$**	**183,031**	**$**	**147,281**
Less: current portion		(7,500)		—
Long-term portion	**$**	**175,531**	**$**	**147,281**

(a) Senior secured notes

i. Senior secured notes due 2025

On December 30, 2020, as part of the Recapitalization Transaction, Source issued $142,238 in aggregate principal of new senior secured notes (the “Notes”), which bear interest at 10.5% and mature March 15, 2025. The Company has the option to defer payment of interest owed in cash and pay interest in kind, at a rate of 12.5%, for all quarterly interest payments due on or before February 15, 2022, through the issuance of additional notes. For the year ended December 31, 2021, the Company paid interest in kind resulting in $16,227 of additional Notes issued. The Notes are secured by a fixed and floating charge over all assets of the business, except for an amount up to a maximum of amounts committed under the senior secured term loan, as outlined below, plus accrued interest and fees. The Notes also have a second charge on accounts receivable and inventory.

The Notes contain prepayment options, whereby the Company may redeem all or a part of the Notes at any time at the applicable percentage (2022 - 101%, 2023 and thereafter - 100%), plus accrued and unpaid interest. The Notes also contain a mandatory redemption feature for each fiscal year commencing December 31, 2021, whereby Source shall redeem the portion of outstanding principal and accrued interest for the Notes that equals 50% of excess cash flows greater than $10,000 in the applicable fiscal year. Excess cash flows are defined as cash flows provided by operating activities, less maintenance capital expenditures, amounts paid for lease obligations, taxes and amounts of interest or principal prepayments on the credit facilities or Notes incurred in the applicable fiscal year.

Interest on the Notes was $18,680 for the year ended December 31, 2021 (2020 - $97).

ii. Senior secured notes due 2021

In December 2016, the Company issued $130,000 senior secured notes and an additional $50,000 senior secured notes in May 2018 (collectively, the “Old Notes”), which bore interest at 10.5% per annum and would have matured December 15, 2021. The Old Notes were secured by a fixed and floating charge over all assets of the business except accounts receivable and inventory, over which the Old Notes had a second charge. Pursuant to the terms of the Recapitalization Transaction, the Old Notes were extinguished and exchanged for the Notes and new common shares of Source.

Interest on the Old Notes was $16,521 for the year ended December 31, 2020.

(b) ABL facility

On December 30, 2020, as part of the Recapitalization Transaction, the Company’s ABL facility was amended to extend the term to mature on September 30, 2023. The facilities bear interest based on the bank’s prime lending rate and CDOR or LIBOR rates, plus an applicable margin. The ABL is secured by a floating first lien charge on the accounts receivable and inventory of the Company under a general business security agreement and a second lien charge on all other assets of the business. The amount available under the general operating facility is subject to a borrowing base formula applied to accounts receivable and inventories. At December 31, 2021, $18,406 was drawn under the ABL facility (less unamortized finance costs of $1,127 for a net balance of $17,279) (December 31, 2020 - $2,166). Any excess cash on hand is applied against amounts drawn on the ABL.

The ABL facility includes a US$5,000 standby letter of credit facility that does not affect the facility’s borrowing base. In March 2021, the standby letter of credit facility was increased to US$8,500, thereby reducing amounts committed to supporting letters of credit under the ABL facility by US$3,500. As per the terms of the senior secured term loan and concurrent with the increase to the standby letter of credit facility, a $2,000 repayment was completed on the senior secured term loan, as noted below. The amount committed to supporting letters of credit under the facility was $9,963 at December 31, 2021 (December 31, 2020 - $14,560). The borrowing base is updated monthly, with $12,496 of availability at December 31, 2021 (December 31, 2020 - $17,302).

(All amounts are in thousands of Canadian dollars, unless otherwise noted)

The revised ABL facility includes the following key financial covenants:

- a minimum level of excess availability of $5,000;
- a minimum level of the average of the prior three months trailing twelve months of earnings before interest, tax, depreciation and amortization ending at predetermined dates through December 31, 2022 and calculated at each fiscal calendar month, equal to a range of $8,500 to $12,000 for 2021 and $12,000 to $25,000 for 2022;
- maximum capital expenditures totaling $6,000 for each of the fiscal calendar years ended 2021 and 2022 and increased to $8,000 for 2023, plus additional permitted 2021 capital expenditures of $568;
- payment of interest in kind for the Notes until February 15, 2022; and
- commencing June 30, 2022, a springing fixed charge ratio of 1.10:1 which shall increase to 1.25:1 on September 30, 2022 and all time thereafter. The fixed charge coverage ratio is defined as the ratio of (i) earnings before interest, tax, depreciation and amortization for the twelve calendar months ending at each fiscal calendar month end less unfinanced capital expenditures, cash taxes and distributions to shareholders and (ii) the interest expense paid in cash plus accrued and unpaid interest related to the senior secured notes for the twelve calendar months ending at such fiscal calendar month.

As of December 31, 2021, Source was in compliance with all of its covenants. Interest on the above facility amounted to $2,580 for the year ended December 31, 2021 (2020 - $3,860).

(c) Senior secured term loan

As part of the Recapitalization Transaction, Source obtained access to an additional credit facility in the form of a senior secured term loan (the “Term Loan”) with an initial principal amount of up to $20,000. The Term Loan bears interest at Canadian prime plus 6% and matures on September 30, 2023, provided that the Term Loan shall be reduced to $10,500 on March 31, 2022 and further reduced to $5,000 on March 31, 2023. The Term Loan is secured by a fixed and floating first charge over all assets of the business. In March 2021, a $2,000 repayment was completed, as noted above, reducing the amount drawn on this facility to $18,000. As at December 31, 2021, $7,500 is presented as a current liability.

Interest on the Term Loan was $1,557 for the year ended December 31, 2021 (2020 - $4).

(d) Other long-term debt

In April 2020, the Company applied for the Paycheck Protection Program of the Coronavirus Aid, Relief, and Economic Security Act, or CARES Act (the “PPP Loan”), administered by the US Small Business Administration. Under the PPP Loan the Company received US$2,097 on April 28, 2020, which bore interest at a rate of 1.00% per annum with a maturity date of April 18, 2022. In June 2021, the Company was approved for forgiveness for the full amount of the outstanding obligation. During the year ended December 31, 2021, a recovery of US$2,097 was recognized in other income. Other long-term debt includes amounts related to the Company’s share-based compensation plan.

The effective interest rate realized on long-term debt for the year ended December 31, 2021 was 12.7% (2020 - 12.1%).

11. LEASE LIABILITIES

As at	**December 31, 2021**	**December 31, 2020**
Balance, beginning of year	$ 42,329	$ 60,025
Additions during year	6,038	10,960
Lease modifications	3,514	(12,774)
Lease payments	(13,224)	(15,526)
Exchange differences	(221)	(356)
Balance, end of year	**$ 38,436**	**$ 42,329**
Less: current portion	(12,358)	(11,036)
Long-term portion	**$ 26,078**	**$ 31,293**

The Company enters into lease arrangements related to rail cars, equipment and vehicles, office buildings and surface leases. Lease liabilities are measured at the present value of the remaining lease payments at the incremental borrowing rate of 8%. Leases with a lease term of twelve months or less for certain classes of assets and low-value assets of $177, respectively, were expensed to cost of sales or operating expense in the year ended December 31, 2021 (2020 - $341). During 2020, the Company completed the renegotiation of lease contracts with certain of its lessors, resulting in a reduction to lease obligations and a modification to the related RoU assets. The Company recognized $2,792, respectively, of interest on lease liabilities for the year ended December 31, 2021 (2020 - $4,042).

12. DECOMMISSIONING PROVISION

As at	December 31, 2021	December 31, 2020
Balance, beginning of year	$ 9,969	$ 11,249
Liabilities incurred	678	548
Liabilities settled	(1,818)	(1,575)
Accretion	141	108
Changes in estimate	(318)	(143)
Exchange differences	(44)	(218)
Balance, end of year	**$ 8,608**	**$ 9,969**
Less: current portion	(1,020)	(1,006)
Long-term portion	**$ 7,588**	**$ 8,963**

The Company's decommissioning provision relates to reclamation of land and facilities where its mines operate. Management estimates the costs to abandon and reclaim its properties based on current reclamation technology, acres disturbed and the estimated time period in which these costs will be incurred in the future. The total future estimate of undiscounted cash flows required to settle the provision has been discounted using risk-free rates of 1.47% for expenditures planned within the next ten years and 1.75% for longer-term expenditures at December 31, 2021 (December 31, 2020 - 0.70% and 1.13%, respectively). The economic lives of the underlying assets are currently estimated to be between 8 and 38 years.

13. SHAREHOLDERS' EQUITY

(a) Share capital

The Company is authorized to issue an unlimited number of common shares.

During 2020, 1,300,154 Class B shares outstanding were held by SES Sand Holdings US, a subsidiary of TriWest Capital Partners which is a related party, who owned 3.74% of the shares of Source Energy Services Canada LP, a subsidiary of Source. In October 2020, the Class B shares were converted into common shares of Source on a one-for-one basis and SES Sand Holdings US became a wholly-owned subsidiary of Source.

The following table outlines the issued and outstanding common shares as at December 31, 2021:

(stated in thousands, except share amounts)	Number of shares	Amount
Balance as at December 31, 2019	5,079,388	$ 397,911
Class B shares converted to common shares	—	91
Shares issued(1)	8,465,667	12,630
Balance as at December 31, 2021 and 2020	**13,545,055**	**$ 410,632**

Note:
(1) Pursuant to the Recapitalization Transaction, 8,465,667 common shares were issued at $1.50 per share, net of $69 of issue costs.

(b) Recapitalization Transaction

In December 2020 Source completed a comprehensive process, undertaken in response to the ongoing downturn in the Western Canadian oil and gas industry, to improve the Company's capital structure and better position the Company for future growth (the "Recapitalization Transaction"). The Recapitalization Transaction was completed through a plan of arrangement under the Canada Business Corporations Act, and included the following:

- the consolidation of outstanding common shares of Source on a twelve-for-one basis;
- the extinguishment of outstanding Old Notes in exchange for the Notes in the aggregate principal amount of $142,238, which mature March 15, 2025, and the issuance of new common shares of Source;
- an amendment to the ABL facility which extended the maturity of the facility to September 30, 2023; and
- a Term Loan in the amount of $20,000 (refer to Note 10 for additional information related to the new and revised debt commitments).

The Recapitalization Transaction resulted in a net gain of $27,690 on extinguishment of debt comprised of the difference between the carrying value of the Old Notes and the Notes, offset in part by the fair value of the equity issuance and net of transaction costs recognized as expense.

(All amounts are in thousands of Canadian dollars, unless otherwise noted)

14. SHARE-BASED COMPENSATION

(a) Option plan

The Company's option plan allows for the granting of options to purchase common shares to a maximum number equal to 10% of the issued and outstanding common shares of the Company. Options vest over three years and expire after five years. As at December 31, 2021, no options were outstanding.

(b) Other share-based compensation plans

The Company has share-based compensation plans that allow for DSUs, RSUs and PSUs to be granted to directors and certain employees. The RSUs vest 1/3 on the anniversary date of the grant over a three-year period. Subject to achievement of performance criteria set out by the Board, the PSUs awarded vest 1/3 on the anniversary date of the grant over a three-year period. The RSUs and PSUs may be settled in cash or shares and accordingly are considered a liability-settled award for accounting purposes as they are expected to be settled for cash payment. At December 31, 2021, a liability of $457 has been recorded for these units, of which $297 has been classified as current (December 31, 2020 - $139 and $87, respectively).

The DSUs vest and are expensed over the earlier of five years or when a director or other participant ceases in their role and are payable only when a director or participant leaves the Company. The DSUs are expected to be settled for cash payment and accordingly are considered a liability-settled award for accounting purposes. At December 31, 2021, a liability of $143 has been recorded for these units, of which $60 has been classified as current (December 31, 2020 - $49 and $nil, respectively).

The fair value of the RSUs, PSUs and DSUs was determined using the Company's share price at period end. The following table provides a summary of the status of the Company's liability-settled compensation plans and changes during the year ended December 31, 2021:

(number of units)	**RSU**	**PSU**	**DSU**
Balance as at December 31, 2019	80,515	36,178	38,187
Granted	93,757	51,894	46,302
Exercised	(30,317)	(1,799)	—
Forfeited	(7,099)	(12,659)	—
Balance as at December 31, 2020	136,856	73,614	84,489
Granted	174,666	392,500	110,231
Exercised	(57,700)	(3,449)	(28,986)
Forfeited	(5,795)	(87,088)	—
Balance as at December 31, 2021	**248,027**	**375,577**	**165,734**
Vested as at December 31, 2021	**—**	**7,378**	**—**

(c) Share appreciation rights

In 2021, the Company authorized a SAR plan for certain employees. These units vest 1/3 on the anniversary date of the grant over a three-year period and are settled for cash payment. The SARs are considered a liability-settled award for accounting purposes and were valued using the Black-Scholes option pricing model, using the following inputs:

Forfeiture rate (%)		7 %
Volatility (%)		127 %
Risk free interest rate (%)		0.25 %
Dividend yield (%)		— %
Option life (years)		2.21
Exercise price	$	1.54
Share price(1)	$	1.66

Note:
(1) Share price is based on the volume weighted average share price for the twenty days preceding the measurement date.

(All amounts are in thousands of Canadian dollars, unless otherwise noted)

At December 31, 2021, a liability of $112 has been recorded for the number of SARs outstanding:

	SARs Outstanding		Weighted Average Exercise Price
Balance as at December 31, 2020	—	$	—
Granted	252,500	$	1.54
Forfeited	(28,500)	$	1.54
Balance as at December 31, 2021	**224,000**	**$**	**1.54**
Vested as at December 31, 2021	**—**	**$**	**—**

Total share-based compensation expense (recovery) for the share-based payment plans for the year ended December 31, 2021 was $643 (2020 - $(14)).

15. EARNINGS (LOSS) PER SHARE

Basic earnings (loss) per share

The calculation of basic earnings (loss) per share for the year ended December 31, 2021 was based on the losses available to holders of common shares of $(24,403) (2020 - $(185,466)), and a weighted average number of common shares outstanding for the year ended December 31, 2021 of 13,545,055 (2020 - 5,038,320).

	2021	2020
Common shares outstanding, beginning of year	13,545,055	4,971,042
Weighted average Class B shares converted to common shares	—	21,018
Weighted average shares issued due to Recapitalization Transaction	—	46,260
Weighted average common shares outstanding, end of year	**13,545,055**	**5,038,320**

Diluted earnings (loss) per share

Diluted earnings per share is calculated by adjusting the earnings and number of shares for the effects of dilutive options and other dilutive potential shares. The effects of anti-dilutive options as well as exchangeable shares are ignored in calculating diluted earnings per share. As at December 31, 2021 and 2020, no options remain outstanding and all issued and outstanding Class B shares were converted to common shares in October 2020.

16. REVENUE

The following table presents the Company's sales, disaggregated by revenue source for the years ended December 31:

		2021		2020
Revenue from contracts with customers:				
Sand revenue	$	258,545	$	210,021
Wellsite solutions		56,121		35,144
Terminal services		2,752		2,186
Total revenue from contracts with customers	$	317,418	$	247,351
Storage facilities[1]		2,443		2,527
Total revenue	**$**	**319,861**	**$**	**249,878**

Note:
(1) Storage facilities includes revenue for proppant storage at terminals as well as longer term Sahara rentals.

(All amounts are in thousands of Canadian dollars, unless otherwise noted)

Contract Liabilities

The following table provides a summary of the contract liabilities as at December 31, 2021:

As at	**December 31, 2021**	**December 31, 2020**
Balance, beginning of year	$ 776	$ 3,160
Cash proceeds	119	536
Satisfaction of performance obligations	(867)	(2,617)
Non-cash interest income	(35)	(303)
Exchange differences	101	—
Balance, end of year	**$ 94**	**$ 776**
Less: current portion	(94)	(776)
Long-term portion	**$ —**	**$ —**

Revenue estimated to be recognized based on minimum volume commitments in a long-term terminal services contract as at December 31, 2021:

2022	526
2023	600
2024	300
Total	**$ 1,426**

17. OPERATING AND GENERAL & ADMINISTRATIVE COSTS

The Company presents its expenses on the consolidated statements of operations and comprehensive loss using the function of expense method whereby expenses are classified according to their function within the Company. This method was selected as it is more closely aligned with the Company's business structure. The Company's functions under IFRS are as follows:

- Cost of sales;
- Operating; and
- General & administrative.

Cost of sales includes direct operating costs (including product costs, direct labour and overhead costs) and depreciation on assets relating to operations. Additional information on the nature of expenses is as follows:

	2021				**2020**			
	COS	**OPEX**	**G&A**	**Total**	**COS**	**OPEX**	**G&A(2)**	**Total**
Direct material	$207,272	$ —	$ —	$207,272	$158,791	$ —	$ —	$158,791
Salary costs(1)	10,627	8,420	6,533	25,580	7,085	4,920	4,385	16,390
Equipment costs	2,327	1,435	1	3,763	1,950	1,056	—	3,006
Transportation costs	38,743	—	—	38,743	24,415	—	—	24,415
Facility costs	460	1,379	33	1,872	792	1,319	51	2,162
Selling costs	—	5,280	(151)	5,129	—	5,190	1,772	6,962
Administration costs	—	—	2,867	2,867	—	—	3,171	3,171
Total	**$259,429**	**$ 16,514**	**$ 9,283**	**$285,226**	**$193,033**	**$ 12,485**	**$ 9,379**	**$214,897**

Notes:

(1) Included in 2021 cost of sales, operating and general & administrative salary costs are wage subsidies of $1,438 received as part of the Canada Emergency Wage Subsidy program (2020 - $2,841).

(2) Prior year selling costs include an amount written off for receivables deemed uncollectible.

(All amounts are in thousands of Canadian dollars, unless otherwise noted)

18. COMMITMENTS AND CONTINGENCIES

The Company has commitments regarding physical natural gas contracts which expire in March and October 2023 as well as various IT software subscriptions through 2026. Estimated annual commitments are as follows:

2022	$	2,627
2023		1,396
2024		20
2025		16
2026 and beyond		12
Total	**$**	**4,071**

In the ordinary course of conducting business, the Company occasionally becomes involved in legal proceedings relating to contracts, environmental issues or other matters. While the amount of any proceeding or litigation is inherently uncertain, management of the Company believes that the outcome of any pending or threatened actions will not have a material adverse effect on the business or financial condition of the Company, except as noted below:

The Company is currently pursuing claims against certain organizations in respect of damages related to the structural failure of assets at its Fox Creek terminal facility. In relation to these claims, the Company incurred costs of $203 recorded as other expense for the year ended December 31, 2021 (2020 - $298). The Company intends to pursue this matter for which the damages, if awarded to the Company in their entirety, could be a material amount. However, litigation is inherently uncertain and a favourable outcome cannot be assured.

19. FINANCE EXPENSE

		2021		**2020**
Interest expense	$	25,677	$	25,052
Accretion		3,993		4,127
Other		650		510
Total	**$**	**30,320**	**$**	**29,689**

20. SEGMENT AND GEOGRAPHICAL INFORMATION

The Company has determined that it operates in a single operating and reportable segment. Total external revenues and assets by geographical location are summarized in the table below:

Sales for the year ended December 31,		**Canadian Operations**		**US Operations**		**Corporate[(1)]**		**Total**
2021	**$**	**318,512**	**$**	**1,349**	**$**	**—**	**$**	**319,861**
2020	$	249,491	$	387	$	—	$	249,878

Total Assets		**Canadian Operations**		**US Operations**		**Corporate[(1)]**		**Total**
December 31, 2021	**$**	**106,519**	**$**	**151,959**	**$**	**7,553**	**$**	**266,031**
December 31, 2020	$	102,068	$	158,803	$	5,390	$	266,261

Note:
(1) Corporate operations are included for informational purposes only.

21. RELATED PARTY TRANSACTIONS

Key management personnel are comprised of the Company's directors and executive officers. Key management personnel compensation is comprised of:

	2021	**2020**
Short-term employment benefits	2,723	1,724
Share-based payments	120	23
Post-employment benefits	16	16
Total	2,859	1,763

Aside from compensation to key management personnel, there were no related party transactions during the years ended December 31, 2021 and 2020.

22. SUBSEQUENT EVENTS

In March 2022, Source executed an amendment to its ABL facility which resulted in the replacement of the existing financial covenant in respect of permitted capital expenditures. The revised financial covenant increases the amount of permitted capital expenditures, now allowing for maximum capital expenditures totaling $10,000 for each of the fiscal calendar years ended 2022 and 2023 and, when certain prescribed conditions have been met, additional permitted capital expenditures in the aggregate amount of $2,000 during each of these fiscal years.

SOURCE ENERGY SERVICES

MANAGEMENT'S DISCUSSION AND ANALYSIS

FOR THE THREE AND TWELVE MONTHS ENDED DECEMBER 31, 2021

www.sourceenergyservices.com

500, 1060 – 7th Street SW, Calgary, AB Canada T2R 0C4 |Telephone 403-262-1312

MANAGEMENT'S DISCUSSION AND ANALYSIS

The following Management's Discussion and Analysis ("MD&A"), dated March 9, 2022, reflects the operating and financial results of Source Energy Services Ltd. and its subsidiaries, collectively ("Source" or the "Company"), as at and for the three and twelve months ended December 31, 2021 compared with the corresponding periods in the prior year. The MD&A is provided to assist readers in understanding the Company's financial performance and position during the periods presented and significant trends that may impact the future performance of Source.

This discussion should be read in conjunction with Source's audited consolidated financial statements for the years ended December 31, 2021 and 2020, together with the accompanying notes (the "Financial Statements"). The Financial Statements and other information relating to Source, including the Annual Information Form ("AIF"), are available under the Company's SEDAR profile at www.sedar.com. The Financial Statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board. Unless otherwise stated, all amounts are expressed in Canadian dollars.

Certain financial measures referred to in this MD&A are not prescribed by IFRS. "Adjusted EBITDA" is, among other things, used by management as a representation of earnings generated to fund capital investments and meet financial obligations, and "Adjusted Gross Margin" is used by management in measuring pricing and operating cost performance relative to other publicly listed competitors. "Free Cash Flow" is generally used to assess the ability to generate cash flows that can be used to pay down long-term debt or provide other forms of returns to investors. Refer to 'Non-IFRS Measures' for further information regarding the following non-IFRS measures used in this MD&A: "Adjusted EBITDA", "Adjusted Gross Margin" and "Free Cash Flow", as well as a reconciliation to IFRS measures of the Company.

This MD&A contains "forward-looking statements" or "forward-looking information" within the meaning of applicable Canadian securities laws (collectively, "forward-looking statements") based on Source's current expectations and projections. For information on the material factors and assumptions underlying such forward-looking statements, refer to 'Forward-Looking Statements' included at the end of this MD&A.

About Source

Source is a company that focuses on the integrated production and distribution of high quality Northern White frac sand, as well as the distribution of other bulk completion materials not produced by Source. Source provides its customers with an end-to-end solution for frac sand supported by its Wisconsin mines and processing facilities, its Western Canadian terminal network, its "last mile" logistics capabilities and Sahara, a proprietary wellsite mobile sand storage and handling system.

Source's full-service approach allows customers to rely on its logistics platform to increase reliability of supply and to ensure the timely delivery of frac sand and other bulk completion materials at the wellsite.

2021 Performance Highlights

Economic recovery in 2021 led to a rebound in the demand for crude oil and natural gas, driving strong commodity prices and increasing industry activity levels. As a result, Source approached record levels of activity for the year, nearly achieving its historical high for total sand sales volumes. Key achievements for the year ended December 31, 2021 included the following:

- realized sand sales volumes of 2,483,362 MT and sand revenue of $258.5 million;
- distributed 2,578,444 MT of proppants and chemicals through Source's Western Canadian Sedimentary Basin ("WCSB") terminal network;
- executed three new customer contracts and secured contract extensions with two major Montney exploration and production ("E&P") companies;
- achieved multiple records including new service records that saw the largest daily and the largest monthly sand sales volume in Source's history;
- increased utilization of the Sahara fleet by 25%, resulting in overall utilization for the year of 65%, including the deployment of a Sahara unit in the US through the entire fourth quarter of the year;
- realized gross margin of $39.3 million and Adjusted Gross Margin(1) of $60.4 million;
- reported net loss of $24.4 million, an improvement of $161.1 million from the same period last year; and
- realized Adjusted EBITDA(1) of $38.6 million.

Note:

(1) Adjusted Gross Margin (including on a per MT basis) and Adjusted EBITDA are not defined under IFRS, refer to 'Non-IFRS Measures' below.

Results Overview

	Three months ended December 31,		Year ended December 31,	
($000's, except MT and per unit amounts)	**2021**	2020	**2021**	2020
Sand volumes (MT)[(1)]	**528,977**	474,345	**2,483,362**	1,968,511
Sand revenue	**54,989**	48,936	**258,545**	210,021
Wellsite solutions	**11,913**	9,582	**57,621**	36,644
Terminal services	**648**	451	**3,695**	3,213
Sales	**67,550**	58,969	**319,861**	249,878
Cost of sales	**59,290**	42,650	**259,429**	193,033
Cost of sales – depreciation	**4,071**	5,253	**21,102**	32,188
Cost of sales	**63,361**	47,903	**280,531**	225,221
Gross margin	**4,189**	11,066	**39,330**	24,657
Operating expense	**4,142**	3,198	**16,514**	12,485
General & administrative expense	**1,990**	1,203	**9,283**	9,379
Depreciation	**2,426**	2,647	**9,873**	13,860
Income (loss) from operations	**(4,369)**	4,018	**3,660**	(11,067)
Other expense (income):				
Finance expense	**7,809**	7,747	**30,320**	29,689
Share-based compensation expense (recovery)	**476**	77	**643**	(14)
Gain on asset disposal	**—**	—	**(63)**	(150)
Unrealized loss (gain) on derivative assets	**173**	—	**(247)**	—
Other income	**(109)**	228	**(3,200)**	(1,625)
Other expense[(2)]	**108**	112	**203**	298
Impairment expense	**—**	—	**—**	143,656
Loss on sublease	**1,159**	—	**1,159**	—
Gain on debt extinguishment	**—**	(27,690)	**—**	(27,690)
Foreign exchange loss (gain)[(3)]	**581**	(471)	**(752)**	(1,115)
Total other expense (income)	**10,197**	(19,997)	**28,063**	143,049
Income (loss) before income taxes	**(14,566)**	24,015	**(24,403)**	(154,116)
Deferred tax expense	**—**	—	**—**	31,350
Net income (loss)	**(14,566)**	24,015	**(24,403)**	(185,466)
Net earnings (loss) per share ($/share)	**(1.08)**	4.58	**(1.80)**	(36.81)
Diluted net earnings (loss) per share ($/share)	**(1.08)**	4.58	**(1.80)**	(36.81)
Adjusted EBITDA[(4)]	**1,656**	12,161	**38,587**	37,721
Sand revenue sales/MT	**103.95**	103.17	**104.11**	106.69

	December 31, 2021	December 31, 2020
Total assets	**266,031**	266,261
Total non-current financial liabilities	**209,197**	187,537

Notes:

(1) One metric tonne ("MT") is approximately equal to 1.102 short tons.

(2) Expenses related to the incident at the Fox Creek terminal facility, refer to 'Contractual Obligations' below.

(3) The average Canadian to United States ("US") dollar exchange rate for the three and twelve months ended December 31, 2021 was $0.7935 and $0.7978, respectively (2020 - $0.7675 and $0.7454, respectively).

(4) Adjusted EBITDA is not defined under IFRS, refer to 'Non-IFRS Measures' below. Includes recovery of US$2.1 million related to forgiveness for the Paycheck Protection Program loan during the year ended December 31, 2021 and the receipt of proceeds from the CEWS (as defined below) program of $0.2 million and $1.4 million, respectively, during the three and twelve months ended December 31, 2021 (three and twelve months ended December 31, 2020 - $0.6 million and $2.8 million, respectively).

Despite ongoing challenges created by the COVID-19 pandemic that continued through much of 2021, oil and natural gas prices strengthened through the year with benchmark oil prices hitting the highest levels since 2014. This resulted in improved activity levels in the WCSB, allowing Source to set new daily and monthly sales records, add new customers and realize a 26% increase in sales volumes over 2020, generating $258.5 million of sand revenue. Total revenue from wellsite solutions and terminal services grew 54% over last year, as the demand for greater volumes of frac sand over shorter periods of time highlighted Source's logistics capabilities and the importance of Sahara units in customer frac programs.

Cost of sales, excluding depreciation, benefited from the continuation of certain operational cost reduction initiatives implemented by Source last year, as well as a focus on maintaining lower costs and improving production efficiencies. However, Source's results for the year were impacted by lower proceeds from the Canada Emergency Wage Subsidy ("CEWS") program of $0.7 million, the impact of sales mix changes and higher costs for transportation and freight, due to increased prices for fuel and a tighter trucking market. These costs were partially offset by the impact of a stronger Canadian dollar on US dollar denominated costs.

Gross Margin	**Year ended December 31,**	
($000's, except MT and per unit amounts)	**2021**	2020
Gross margin	**39,330**	24,657
Cost of sales – depreciation	**21,102**	32,188
Adjusted Gross Margin(1)	**60,432**	56,845
Gross margin/MT	**15.84**	12.53
Adjusted Gross Margin/MT(1)	**24.33**	28.88
Percentage of mine gate sand volumes	**—%**	1%
Percentage of sand volumes sold in the WCSB	**100%**	99%

Note:
(1) Adjusted Gross Margin (including on a per MT basis) is not defined under IFRS, refer to 'Non-IFRS Measures' below.

Gross margin was favorably impacted by lower cost of sales - depreciation realized, attributed to a lower asset base resulting from the impairment recognized early last year and the benefit realized from the renegotiation of certain lease contracts in 2020, while Adjusted Gross Margin on a per MT was impacted by higher cost of sales, as discussed above. The majority of Source's sales continue to be under long-term contracts; however, strong activity levels also drove higher spot sale activities for the year which benefited average sand price realized, partially offsetting the impact of a stronger Canadian dollar on revenue denominated in US dollars.

An increase in employee compensation expense, the direct result of improved activity levels leading to higher incentive compensation, combined with lower proceeds from the CEWS program, drove higher operating expense for 2021 compared to last year, while general and administrative expense remained relatively flat to 2020. Adjusted EBITDA was $38.6 million for 2021, a reflection of the strong sand sales volumes realized; however, Adjusted EBITDA was unfavorably impacted by the higher costs incurred for diesel and freight, particularly in the latter half of the year.

ESG Overview

Source is committed to operating in a sustainable manner, continually looking to implement efficiencies to lessen the impact of Source's activities on the environment and specifically to reduce greenhouse gas emissions. Source works closely with its stakeholders to go above and beyond current regulatory requirements through initiatives such as voluntary enrollment with the Department of Natural Resources Sustainable Growth Program and Managed Forest Program, as well as Source's production water recycling process.

Source has formally adopted the Sustainability Accounting Standards Board ("SASB") framework that provides sector-specific guidelines against which Source will benchmark itself in environment, social and governance ("ESG") categories. Late last year, Source completed its benchmarking and materiality assessment which will align the Company's upcoming annual ESG performance report, expected to be released in spring of 2022, with the relevant SASB performance indicators.

To view Source's complete 2021 ESG report, please visit www.sourceenergyservices.com.

Business Outlook

The growing demand for oil and natural gas globally, coupled with the under investment in supply over the past few years, resulted in higher crude oil and natural gas prices in 2021 and into 2022. This operating environment allowed Source's customers to generate strong 2021 cash flows which in turn is expected to result in expanded drilling and completion programs in 2022. With the increased activity levels across North America the frac sand supply and demand fundamentals have been, and are expected to remain, tight for 2022. These fundamentals, coupled with Source's leading service offerings and logistics capabilities, have translated into meaningful pricing gains early in 2022, a trend that is expected to continue for the balance of the year.

In the longer-term, Source believes the increased demand for natural gas, driven by the conversion of coal-fired power generation facilities, increased natural gas pipeline export capabilities and liquefied natural gas ("LNG") exports will drive incremental demand for Source's services in the WCSB. Source continues to see increased demand from customers that are primarily focused on the development of natural gas properties in the Montney, Duvernay and Deep Basin. This trend is consistent with Source's view that natural gas will be an important transitional fuel that's critical for the successful movement to a less carbon intensive world.

In support of the move to a less carbon intensive world, Source has begun focusing on exploring and developing economic growth opportunities which transition from traditional fossil fuels to less carbon intense energy solutions. As a pathway to diversifying Source's business, and to participate in the decarbonization of the economy, Source is advancing opportunities in its own operations as well as at the well site and at its terminals. Source also continues to focus on increasing its involvement of the provision of logistics services for other items needed at the wellsite in response to customer requests to expand its service offerings and to further utilize its existing Western Canadian terminals to provide additional services. Over the longer-term, it is anticipated that these opportunities will be a meaningful part of Source's business.

Review of Operations

Sand revenue is predominately comprised of sand sales into the WCSB at a Source terminal or to a customer at the wellsite utilizing Source's integrated logistics business model. This is referred to as "In Basin" sales and it represents Source's core business.

Sand revenue may also include mine gate sand sales, which include the sale of products that are in lower demand in the WCSB and sold at the mine sites in the US. Mine gate sand sales are undertaken to maximize production efficiencies and sand volumes but are not considered Source's core business and are typically at a lower sales price than In Basin sales and provide a comparatively lower margin per MT sold.

Wellsite solutions revenue is comprised of revenue from "last mile" logistics (i.e., from a Source terminal to the wellsite), and wellsite service offerings including Sahara units. Source believes its "last mile" services benefit customers by managing overall trucking activity, increasing reliability of supply at the wellsite and increasing operational efficiencies. Source also provides terminal services for certain well-completion products that are not produced by Source. These products primarily consist of hydrochloric acid, chemicals and resin-coated proppants. The magnitude of terminal services revenue realized by Source generally follows completion activity trends in the WCSB.

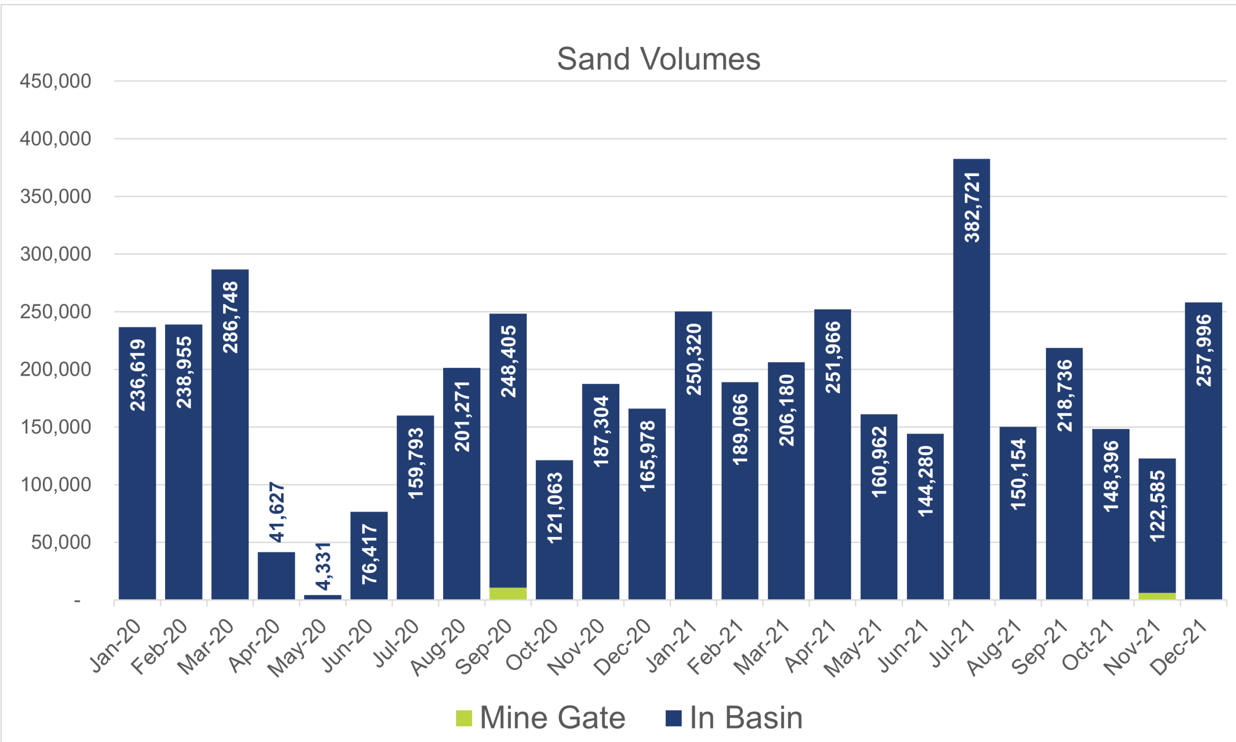
Source's business is seasonal in nature, with the majority of activity normally being in the first and third quarters of the year. As a result, Source's operating results may vary on a quarterly basis. Lower activity levels are usually realized in the fourth quarter, as E&P companies evaluate remaining capital spend for the year, and in the second quarter due to spring break-up. Spring break-up occurs for a period of approximately eight weeks between March and June as the frost comes out of the roads in Western Canada and hauling weight restrictions are put in place. The severity of the winter snowfalls and the amount of moisture received during this period impact the length of spring break-up. In addition, some exploration and production areas in Northern Canada are accessible only in the winter months when the ground is frozen. There are other factors that will impact the Company's activities from quarter-to-quarter including commodity prices and completion activity levels of E&P companies.

Consistent with general industry practice, Source mines and washes more sand than current delivery requirements during the warmer months when Source's processing facilities are more efficient. The excess sand is placed in stockpiles that feed drying operations throughout the year. Frac sand washing facilities in Wisconsin are generally not operated during the winter months; however, Source's sand washing facility at its Sumner facility is fully enclosed and heated, making it capable of operating year-round. Winter operations at the Sumner facility are an important aspect of Source's business, as the WCSB is seasonally busiest in the winter months. Source's wash plants at the Blair and Preston facilities are not enclosed and therefore are generally not operated during the winter months, but the dry plants are operated year-round.

Annual Results Review

Sand Revenue

For the year ended December 31, 2021 sand revenue was $258.5 million, an increase of $48.5 million or 23%, compared to the year ended 2020. The increase was due to overall improved industry activity levels compared to 2020, resulting in higher sand volumes from contracted customers, increased sand volumes realized with other non-contracted E&P and pressure pumping customers and the addition of three new customer contracts in the year. On a year-over-year basis, Canadian dollar denominated average realized sand price increased by 11.3%, driven by favorable customer mix. However, this improvement in average realized sand price was offset by the strengthening of the Canadian dollar, relative to last year, with 54% of sand revenue denominated in US dollars during 2021. Revenue realized from mine gate sales also contributed to the lower average realized sand price for the year ended December 31, 2021. Last year, sand revenue was materially impacted by the impact of COVID-19 and the collapse of commodity prices, which caused customers to either cut or defer the bulk of their completion activities during the first half of 2020.



Wellsite Solutions and Terminal Services Revenue

Wellsite solutions revenue was $57.6 million for the year ended December 31, 2021, an increase of 57% or $21.0 million compared to 2020. Wellsite solutions revenue improved primarily as a result of a 52% increase in sand volumes that were trucked to wellsite compared to last year, attributed to improved activity levels as well as the addition of three new customers during the year. Sahara-related revenue increased 55% on a year-over-year basis, due to a 58% increase in days utilized across the eight-unit fleet, the addition of new customers as noted above, the deployment of a fully utilized Sahara unit in the US late in the year and overall higher activity levels. Wellsite Solutions revenue was negatively impacted in 2020 by the significant slowdown in industry activity levels resulting from the weakened economic climate and the decline in demand for crude oil, attributed primarily to the spread of COVID-19.

For the year ended December 31, 2021, terminal services revenue was $3.7 million, an increase of $0.5 million, or 15%, from 2020. The increase is the result of higher chemical elevation and sand elevation volumes, driving higher proppant storage revenue and hydrochloric acid transloading revenue, partially offset by lower revenue from pipe and magnetite transloading, compared to last year.

Cost of Sales

($000's)	Year ended December 31, 2021	2020
Direct materials	**207,272**	158,791
People costs	**10,627**	7,085
Equipment costs	**2,327**	1,950
Transportation costs	**38,743**	24,415
Facility costs	**460**	792
Cost of sales	**259,429**	193,033
Cost of sales - depreciation	**21,102**	32,188

Cost of sales, excluding depreciation, increased by $66.4 million for the year ended December 31, 2021, compared to last year, primarily driven by higher sand sales volumes realized. During the year an increase in transportation and freight costs, driven by higher prices for fuel and trucking and supply constraints, contributed to the increase in cost of sales, excluding depreciation. Cost of sales, excluding depreciation, was impacted by increased compensation expense due to costs incurred for incentive compensation and lower proceeds received from the CEWS program for the year of $0.8 million, compared to proceeds of $1.5 million received in 2020. Source was impacted by a change of sales mix in 2021 compared to 2020, as well as certain one-time operational issues at its processing facilities which led to higher costs in the year. In 2020, due to the sharp contraction in industry activity levels resulting from the impact of COVID-19, Source implemented operational cost reductions, including reductions to operating staff levels and hours of operations, which favorably impacted cost of sales.

Significant components of cost of sales are denominated in US dollars, including sand processing and rail freight, and are therefore subject to exchange rate fluctuations. For the year ended December 31, 2021, a strengthening of the Canadian dollar on US dollar denominated components of cost of sales of 6.6% partially offset the increased cost of sales described above.

Gross Margin

($000's, except MT and per unit amounts)	Year ended December 31, 2021	2020
Gross margin	**39,330**	24,657
Cost of sales – depreciation	**21,102**	32,188
Adjusted Gross Margin(1)	**60,432**	56,845
Gross margin/MT	**15.84**	12.53
Adjusted Gross Margin/MT(1)	**24.33**	28.88
Percentage of mine gate sand volumes	**—%**	1%
Percentage of sand volumes sold in the WCSB	**100%**	99%

Note:
(1) Adjusted Gross Margin (including on a per MT basis) is not defined under IFRS, refer to 'Non-IFRS Measures' below.

For the year ended December 31, 2021, gross margin increased by $14.7 million compared to the prior year, primarily due to lower cost of sales - depreciation. Lower cost of sales - depreciation for the year is attributed to the impairment recognized in the first quarter of 2020 and the benefits realized from rail car lease negotiations completed late last year, resulting in a lower asset base. Adjusted Gross Margin increased by $3.6 million for the year, compared to 2020, due to higher volumes realized and the continued benefit from certain operational efficiencies achieved, partially offset by the increase in cost of sales, excluding depreciation, as discussed above.

Operating and General & Administrative Expense

	Year ended December 31, 2021		2020	
($000's)	**OPEX**	**G&A**	OPEX	G&A
People	**8,420**	**6,533**	4,920	4,385
Equipment	**1,435**	**1**	1,056	—
Facility	**1,379**	**33**	1,319	51
Selling and administrative	**5,280**	**2,716**	5,190	4,943
Operating and General & Administrative Expense	**16,514**	**9,283**	12,485	9,379

For the year ended December 31, 2021 total operating and general and administrative expense increased $3.9 million to $25.8 million. Compared to the year ended December 31, 2020, operating expense increased $4.0 million in 2021 primarily due to higher people costs incurred. A significant improvement in activity levels realized during the year resulted in higher compensation expense, including variable incentive compensation, and lower proceeds received from the CEWS program of $0.4 million. Higher costs incurred for repairs and maintenance expense, attributed to the increase in production activities at the facilities, also impacted the year relative to 2020.

For the year ended December 31, 2021, general and administrative expense was $9.3 million, a decrease of $0.1 million from the prior year. Higher variable incentive compensation expense related to increased activity levels and lower proceeds of $0.4 million received from the CEWS program led to increased people costs compared to 2020. This increase was offset by lower selling and administrative expense realized for the year, including lower amounts for professional fees and not incurring the large write-off for uncollectible receivables related to a pressure pumper who filed for creditor protection last year.

Depreciation

Depreciation expense decreased by $4.0 million for the year ended December 31, 2021, compared to 2020, the result of depreciation calculated on a lower asset base due to the impairment recognized in the first quarter of 2020.

Finance Expense

Finance expense increased by $0.6 million for the year ended December 31, 2021 compared to last year. The increase in finance expense was primarily due to higher interest on the Notes resulting from interest paid in kind at a higher rate, as well as interest expense for the senior secured term loan disbursed on December 30, 2020. These increases were partially offset by lower interest expense resulting from lower draws on the ABL facility and decreased interest expense incurred for lease liabilities due to the renegotiation of certain rail car and equipment lease contracts executed in the third quarter of 2020.

Share-based Compensation

Share-based compensation expense increased $0.7 million for 2021, compared to 2020, attributed to the movement in Source's share price relative to last year, as well as expense associated with units granted in the current year, including units for the share appreciation rights ("SARs") compensation plan introduced in 2021. Share-based compensation expense is attributed to deferred share units ("DSUs"), restricted share units ("RSUs"), performance share units ("PSUs") and SARs.

Unrealized Gain on Derivative Assets

Source recorded an unrealized gain of $0.2 million for the year ended December 31, 2021 compared to $nil for the prior year. During 2021, Source entered into foreign exchange forward contracts to further mitigate risk associated with the fluctuation in US dollar to Canadian dollar exchange rates.

Other Income

Other income was $3.2 million, an increase of $1.6 million, for the year ended December 31, 2021 compared to 2020. The increase is primarily due to the approval for full forgiveness of Source's outstanding Paycheck Protection Program loan, a total of US$2.1 million, issued by the US Small Business Association during the second quarter of 2021. Other income also includes $0.3 million of proceeds from the Canada Emergency Rent Subsidy program received during the year.

Other Expense

Other expense decreased by $0.1 million compared to 2021, reflecting lower professional fees associated with the incident that occurred at the Fox Creek terminal facility in 2019, as discussed below.

Impairment Expense

No impairment expense was recorded for the for the year ended December 31, 2021, compared to $143.7 million realized during 2020. In the first quarter of 2020, as a result of the weakening economic climate and demand for crude oil, Source carried out an assessment of the recoverable value of its operations which resulted in an impairment loss being recognized.

Loss on Sublease

During the year, Source entered into a sublease agreement for its previous head office. As a result, the Company recognized a $1.2 million loss for the year ended December 31, 2021.

Income Tax

Source recorded no income tax expense during the year, compared to an expense of $31.4 million for 2020. The decrease in income tax expense was due to the reversal of the cumulative deferred tax asset recognized in the first quarter of 2020.

Summary of Quarterly Results

($000's, except MT and per unit amounts)	2020				2021			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Sand volumes (MT)	*762,322*	*122,375*	*609,469*	*474,345*	*645,566*	*557,208*	*751,611*	*528,977*
Sand revenue	83,019	12,826	65,240	48,936	66,115	58,098	79,343	54,989
Wellsite solutions	12,113	2,313	12,636	9,582	14,121	14,033	17,554	11,913
Terminal services	1,331	762	669	451	1,653	605	789	648
Sales	96,463	15,901	78,545	58,969	81,889	72,736	97,686	67,550
Cost of sales	76,656	12,485	61,242	42,650	63,619	56,526	79,994	59,290
Cost of sales - depreciation	13,430	3,241	10,264	5,253	7,582	4,528	4,921	4,071
Cost of sales	90,086	15,726	71,506	47,903	71,201	61,054	84,915	63,361
Gross margin	6,377	175	7,039	11,066	10,688	11,682	12,771	4,189
Operating expense	4,297	2,237	2,753	3,198	3,718	4,048	4,606	4,142
General & administrative expense	2,557	3,399	2,220	1,203	2,604	2,390	2,299	1,990
Depreciation	4,257	3,798	3,158	2,647	2,785	2,326	2,336	2,426
Income (loss) from operations	(4,734)	(9,259)	(1,092)	4,018	1,581	2,918	3,530	(4,369)
Other expense (income):								
Finance expense	7,246	7,045	7,651	7,747	7,463	7,410	7,638	7,809
Share-based compensation expense (recovery)	(96)	27	(22)	77	186	(16)	(3)	476
Loss (gain) on asset disposal	5	—	(155)	—	—	(9)	(54)	—
Unrealized loss (gain) on derivative assets	—	—	—	—	—	(420)	—	173
Other income (loss)	(1,344)	(382)	(127)	228	(162)	(2,760)	(169)	(109)
Other expense(1)	108	12	66	112	44	—	51	108
Impairment expense	143,656	—	—	—	—	—	—	—
Loss on sublease	—	—	—	—	—	—	—	1,159
Gain on debt extinguishment	—	—	—	(27,690)	—	—	—	—
Foreign exchange loss (gain)	(312)	230	(562)	(471)	(564)	(415)	(354)	581
Total other expense (income)	149,263	6,932	6,851	(19,997)	6,967	3,790	7,109	10,197
Income (loss) before income taxes	(153,997)	(16,191)	(7,943)	24,015	(5,386)	(872)	(3,579)	(14,566)
Deferred tax expense	31,350	—	—	—	—	—	—	—
Net income (loss)	(185,347)	(16,191)	(7,943)	24,015	(5,386)	(872)	(3,579)	(14,566)
Net earnings (loss) per share ($/share)	(36.91)	(3.16)	(1.53)	4.58	(0.40)	(0.06)	(0.26)	(1.08)
Diluted net earnings (loss) per share ($/share)	(36.91)	(3.16)	(1.53)	4.58	(0.40)	(0.06)	(0.26)	(1.08)
Net income (loss)	(185,347)	(16,191)	(7,943)	24,015	(5,386)	(872)	(3,579)	(14,566)
Interest	6,175	5,890	6,373	6,615	6,362	6,265	6,456	6,594
Income taxes	31,350	—	—	—	—	—	—	—
Depreciation	4,257	3,798	3,158	2,647	2,785	2,326	2,336	2,426
Cost of sales - depreciation	13,430	3,241	10,264	5,253	7,582	4,528	4,921	4,071
Impairment expense	143,656	—	—	—	—	—	—	—
Gain on debt extinguishment	—	—	—	(27,690)	—	—	—	—
Finance expense	1,071	1,155	1,278	1,132	1,101	1,145	1,182	1,215
Share-based compensation expense (recovery)	(96)	27	(22)	77	186	(16)	(3)	476
Loss (gain) on asset disposal	5	—	(155)	—	—	(9)	(54)	—
Unrealized loss (gain) on derivative assets	—	—	—	—	—	(420)	—	173
Loss on sublease	—	—	—	—	—	—	—	1,159
Other expense(1)	108	12	66	112	44	—	51	108
Adjusted EBITDA(2)	14,609	(2,068)	13,019	12,161	12,674	12,947	11,310	1,656
Sand revenue sales/MT	108.90	104.81	107.04	103.17	102.41	104.27	105.56	103.95
Gross margin	6,377	175	7,039	11,066	10,688	11,682	12,771	4,189
Cost of sales - depreciation	13,430	3,241	10,264	5,253	7,582	4,528	4,921	4,071
Adjusted Gross Margin(2)	19,807	3,416	17,303	16,319	18,270	16,210	17,692	8,260
Gross margin/MT	8.37	1.43	11.55	23.33	16.56	20.97	16.99	7.92
Adjusted Gross Margin/MT(2)	25.98	27.91	28.39	34.40	28.30	29.09	23.54	15.62

Notes:
(1) Expenses related to the incident at the Fox Creek terminal facility, refer to 'Contractual Obligations' below.
(2) Adjusted EBITDA and Adjusted Gross Margin (including on a per MT basis) are not defined under IFRS, refer to 'Non-IFRS Measures' below.

Fourth Quarter Results Review

Sand Revenue

Source sold sand volumes of 528,977 MT for the three months ended December 31, 2021, generating sand revenue of $55.0 million, an increase in revenue of $6.1 million from the fourth quarter of 2020. Sand revenue was favorably impacted by higher sand volumes realized with other non-contracted E&P and pressure pumping customers, in addition to increased sand volumes resulting from new customer contracts, including the execution of a new contract in the fourth quarter of 2021. Average realized sand price, excluding mine gate sales and the impact of the strengthening Canadian dollar on US dollar denominated revenue, increased by $1.67 per MT for the fourth quarter compared to the same period last year.

Wellsite Solutions and Terminal Services Revenue

Wellsite solutions revenue was $11.9 million for the fourth quarter of 2021, an increase of 24% or $2.3 million compared to the fourth quarter of 2020. The increase in wellsite solutions revenue was due to a 6% increase in sand volumes trucked to wellsite, partly attributed to the addition of a new customer in the fourth quarter of 2021, compared to the same period last year. Sahara-related revenue benefited from a 58% improvement in days utilized across the eight-unit fleet compared to the fourth quarter of 2020, including a fully utilized Sahara unit in the US, attributed to the addition of new customers through 2021 and overall higher activity levels.

Terminal services revenue was $0.6 million for the fourth quarter, an increase of $0.2 million compared with the same period last year. The increase is the result of higher chemical and sand elevation volumes realized, compared to the fourth quarter of 2020.

Cost of Sales

	Three months ended December 31,	
($000's)	**2021**	2020
Direct materials	**47,961**	33,928
People costs	**2,728**	1,742
Equipment costs	**622**	468
Transportation costs	**7,884**	6,395
Facility costs	**95**	117
Cost of sales	**59,290**	42,650
Cost of sales - depreciation	**4,071**	5,253

Cost of sales, excluding depreciation, increased by $16.6 million for the three months ended December 31, 2021, compared to the same period last year, primarily driven by higher sand volumes realized. Cost of sales, excluding depreciation, was impacted by an increase in transportation and freight costs during the quarter, driven by higher volumes and increasing fuel costs, as noted above. Higher production costs were recorded during the fourth quarter of 2021, attributed to several factors including the impact of one-time repair costs and mine yield changes experienced during the year, as well as extreme weather during December which resulted in a slowdown in rail service, driving higher logistics costs and less operating time at production facilities, compared to the same period last year. A strengthening of the Canadian dollar on US dollar denominated components of cost of sales favorably impacted cost of sales for the quarter, partially offsetting the increases noted above. Lower proceeds received from the CEWS program of $0.3 million also increased cost of sales for the period, compared to the same period last year. The fourth quarter of 2020 benefited from warmer weather realized, resulting in increased efficiencies and lower energy costs for the period.

Gross Margin

	Three months ended December 31,	
($000's, except MT and per unit amounts)	**2021**	2020
Gross margin	**4,189**	11,066
Cost of sales – depreciation	**4,071**	5,253
Adjusted Gross Margin(1)	**8,260**	16,319
Gross margin/MT	**7.92**	23.33
Adjusted Gross Margin/MT(1)	**15.62**	34.40
Percentage of mine gate sand volumes	**1%**	—%
Percentage of sand volumes sold in the WCSB	**99%**	100%

Note:
(1) Adjusted Gross Margin (including on a per MT basis) is not defined under IFRS, refer to 'Non-IFRS Measures' below.

Gross margin decreased by $6.9 million on a quarter-over-quarter basis, primarily due to the impact of higher production costs, as discussed above, and higher transportation and freight costs. Adjusted Gross Margin decreased by $8.1 million for the quarter, impacted by increased costs for the period as well as lower cost of sales - depreciation realized for the period, attributed to a lower asset base, as discussed above.

Operating and General & Administrative Expense

	Three months ended December 31,			
	2021		2020	
($000's)	**OPEX**	**G&A**	OPEX	G&A
People	**1,800**	**1,538**	1,088	461
Equipment	**397**	**—**	279	—
Facility	**368**	**14**	341	1
Selling and administrative	**1,577**	**438**	1,490	741
Operating and General & Administrative Expense	**4,142**	**1,990**	3,198	1,203

For the fourth quarter of 2021, total operating and general and administrative expense was $6.1 million, an increase of $1.7 million, or 39%, from the fourth quarter of 2020. Operating expense increased by $0.9 million for the fourth quarter of 2021 due to higher compensation resulting from increased activity levels and lower proceeds from the CEWS program of $0.1 million, resulting in higher people costs. Selling costs increased due to higher royalty costs incurred driven by higher sand volumes sold compared to the fourth quarter of last year.

General and administrative expense for the fourth quarter was $2.0 million, an increase of $0.8 million compared to the same period last year. As previously noted, higher variable incentive compensation related to increased activity levels and lower proceeds of $0.1 million received from the CEWS program contributed to the increase. Higher people costs were partly offset by a reduction in selling and administrative costs, due to an increase in the provision for doubtful accounts recorded in the fourth quarter of 2020.

Finance Expense

Finance expense remained relatively flat on a quarter-over-quarter basis, as higher interest expense for the Notes was partially offset by a decrease in other finance charges, compared to the fourth quarter of 2020.

Share-based Compensation

Share-based compensation expense increased $0.4 million compared to the fourth quarter of 2020, attributed to the movement in Source's share price relative to the prior period as well as expense associated with units granted in the current year, including units for the SARs compensation plan introduced in 2021.

Other Income

Other income was $0.1 million for the quarter, compared to an expense of $0.2 million for the fourth quarter last year. The increase is attributed to an adjustment made in the fourth quarter of 2020 for the amount to be recovered for certain sales and use taxes incurred at the US operating facilities.

Liquidity and Capital Resources

Free Cash Flow

	Year ended December 31,	
($000's)	**2021**	2020
Cash flows provided by (used in) operating activities	**14,011**	39,371
Financing expense paid	**(7,897)**	(8,334)
Maintenance and sustaining capital spend	**(4,297)**	(2,155)
Repayment of lease obligations	**(13,224)**	(15,526)
Satisfaction of performance obligations, net of proceeds on contract liabilities	**748**	2,081
Free Cash Flow [(1)]	**(10,659)**	15,437

Note:
(1) Free Cash Flow is not defined under IFRS, refer to 'Non-IFRS Measures' below. The reconciliation to the comparable IFRS measure can be found in the table above.

Source generated negative Free Cash Flow of $10.7 million for the year ended December 31, 2021, compared with $15.4 million generated in 2020. The change in Free Cash Flow, compared to last year, was driven by a $27.3 million change non-cash working capital. Activity levels through 2021 were significantly stronger relative to 2020, resulting in a large buildup of working capital at the end of the year, driven by higher balances for accounts receivable and inventory. Expenditures for maintenance and sustaining capital during 2021 were higher than the prior year, as increased overburden removal was required to accommodate the growth in sand sales volume. Offsetting these reductions to Free Cash Flow was lower lease obligation repayments, due to the renegotiation of certain long-term leases for rail cars and equipment completed in 2020 which lowered the related financing expense paid through the year, and lower interest expense paid on the ABL facility, relative to 2020.

Source funded its capital spend during 2021 and 2020 through amounts available under the Credit Facility (as defined below) and cash flows from operations. Free Cash Flow generated will be used to lower amounts outstanding on the ABL facility, which fluctuates with the movement in working capital balances, as well as funding requirements of the operations of the business. Source continues to focus on expenditure levels to ensure that it can generate free cash flows which can be used to continue to deleverage the business.

Source operates in a working capital and capital expenditure intensive industry where capital is required to fund working capital growth and maintenance capital expenditures for the Company. In December 2020, Source completed a restructuring transaction as a result of the prolonged slowdown in the Western Canadian oil and gas industry (the "Recapitalization Transaction"). The Recapitalization Transaction provided the Company with a stronger long-term capital structure, including the issuance of new senior secured notes (the "Notes"). The Company has a banking operating facility comprised of the ABL facility, a standby letter of credit facility and, as a result of the Recapitalization Transaction, a senior secured term loan (collectively, the "Credit Facility"). Source intends to fund future working capital and capital expenditures using cash flows from operating activities, amounts available under the existing Credit Facility and additional debt or equity issuances as may be required. The availability of any additional future funding beyond that provided by the Recapitalization Transaction will depend on, among other things, operating performance and the current state of the equity and debt capital markets.

Capital Expenditures

	Three months ended December 31,		Year ended December 31,	
($000's)	**2021**	2020	**2021**	2020
Terminal	**—**	—	**232**	43
Wellsite solutions	**1,021**	943	**1,896**	1,613
Production	**48**	58	**919**	582
Overburden removal	**791**	137	**3,330**	1,341
Other	**140**	—	**140**	104
Capital expenditures	**2,000**	1,138	**6,517**	3,683
Growth capital	**1,113**	1,001	**2,220**	1,722
Maintenance and sustaining capital	**887**	137	**4,297**	1,961
Capital expenditures	**2,000**	1,138	**6,517**	3,683

Source's capital expenditures fall into three main categories: capital expenditures at existing terminals and mine facilities to make improvements and maintain operations, including overburden removal, and growth capital expenditures to expand production and distribution capabilities across its infrastructure.

Capital expenditures for the fourth quarter of 2021 were $2.0 million, an increase of $0.9 million for the same period last year. The increase was due primarily to an increase in overburden removal for mining operations, resulting from increased sand sales volume. For the year ended December 31, 2021, capital expenditures increased by $2.8 million, driven by an increase in overburden removal, as noted above, and expenditures for Sahara enhancements, providing increased unloading capacity. In 2021, Source also invested in production equipment that will generate increased yields in Source's sand processing activities. Additional capital expenditures for this production equipment were permitted under the amended and restated credit agreement, as outlined below.

Source's capital management policy is to maintain a strong capital base that optimizes its ability to grow, maintain investor and creditor confidence and to provide a platform to create value for its stakeholders. Source considers its capital structure to include Source's equity, the Notes and Credit Facility and manages its capital structure through various means including monthly management meetings and quarterly Board meetings to review financial information. Source evaluates and monitors its capital based on its current working capital, available bank line, projected cash flows provided by operating activities and anticipated capital expenditures. Source's management prepares annual capital expenditure and operating budgets which are approved by the Board and are regularly reviewed and updated as necessary.

As noted above, Source completed the Recapitalization Transaction in late 2020 which resulted in a stronger long-term capital structure. Source's ability to fund future operating expenses and capital expenditures, to make scheduled payments of interest on the Notes and the Credit Facility and to satisfy any of Source's other present or future debt obligations will depend on Source's future operating performance which will be affected by general economic, financial and other factors.

The Company's share capital is not subject to external restrictions; however, the amount of the ABL facility available for use is determined by levels of accounts receivable and inventory. Pursuant to the amended and restated credit agreement, the Company is subject to externally imposed capital requirements as follows:

- a minimum level of excess availability of $5,000;
- a minimum level of the average of the prior three months trailing twelve months of earnings before interest, tax, depreciation and amortization ending at predetermined dates through December 31, 2022 and calculated at each fiscal calendar month, equal to a range of $8,500 to $12,000 for 2021 and $12,000 to $25,000 for 2022;
- maximum capital expenditures totaling $6,000 for each of the fiscal calendar years ended 2021 and 2022 and increased to $8,000 for 2023, plus additional permitted 2021 capital expenditures of $568;
- payment of interest in kind for the Notes until February 15, 2022; and
- commencing June 30, 2022, a springing fixed charge ratio of 1.10:1 which shall increase to 1.25:1 on September 30, 2022 and all time thereafter. The fixed charge coverage ratio is defined as the ratio of (i) earnings before interest, tax, depreciation and amortization for the twelve calendar months ending at each fiscal calendar month end less unfinanced capital expenditures, cash taxes and distributions to shareholders and (ii) the interest expense paid in cash plus accrued and unpaid interest related to the senior secured notes for the twelve calendar months ending at such fiscal calendar month.

As of December 31, 2021, Source was in compliance with all of its covenants. Source's capital management policy has not changed during the year ended December 31, 2021.

In March 2022, Source executed an amendment to its ABL facility which resulted in the replacement of the existing financial covenant in respect of permitted capital expenditures. The revised financial covenant increases the amount of permitted capital expenditures, now allowing for maximum capital expenditures totaling $10,000 for each of the fiscal calendar years ended 2022 and 2023 and, when certain prescribed conditions have been met, additional permitted capital expenditures in the aggregate amount of $2,000 during each of these fiscal years.

Long-term Debt

($000's)	**December 31, 2021**	**December 31, 2020**
Senior secured notes	**147,350**	124,022
ABL facility	**18,406**	3,736
Senior secured term loan, long-term portion	**10,500**	20,000
Other long-term debt, including unamortized debt issue costs	**(725)**	(477)
Total long-term debt	**175,531**	147,281
Standby letter of credit facility	***9,963***	*14,560*

As at December 31, 2021, Source had long-term debt outstanding of $175.5 million, excluding the current portion of the Term Loan (as defined below), compared to $147.3 million as at December 31, 2020. The change in long-term debt outstanding was due to $16.2 million of additional Notes issued as a result of the Company electing to pay its quarterly interest payments in kind, and accrued interest for the Notes to the end of the year. A build in working capital contributed to an increase in draws on the ABL facility during the fourth quarter, partly attributed to the movement of large quantities of sand into the WCSB in preparation for the first quarter of 2022. These increases were offset by lower amounts outstanding for the Term Loan, including a reclass to current liabilities for a portion of the Term Loan.

Senior Secured Notes

On December 30, 2020, Source issued $142.2 million in aggregate principal amount of new senior secured notes (as defined above), thereby replacing the previously issued senior secured notes. The Notes bear interest at 10.5% and mature on March 15, 2025. The Company has the option to defer payment of interest owed in cash and pay interest in kind, at a rate of 12.5%, for all quarterly interest payments due on or before February 15, 2022 through the issuance of additional notes. For the three and twelve months ended December 31, 2021, Source elected to pay interest in kind resulting in $4.8 million and $16.2 million of additional Notes issued, respectively. At December 31, 2021, the aggregate principal amount of Notes outstanding was $158.5 million. The Notes are secured by a fixed and floating charge over all assets of the business, except for an amount up to a maximum of amounts committed under the senior secured term loan, as outlined below, plus accrued interest and fees, for amounts committed under the senior secured term loan, as outlined below. The Notes also have a second charge on accounts receivable and inventory.

The Notes contain prepayment options, whereby the Company may redeem all or a part of the Notes at any time at the applicable percentage (2022 - 101%, 2023 and thereafter - 100%), plus accrued and unpaid interest.

Credit Facility

The Company has an ABL facility which matures on September 30, 2023 and bears interest based on the bank's prime lending rate and CDOR or LIBOR rates, plus an applicable margin. The ABL is secured by a floating first lien charge on the accounts receivable and inventory of the Company under a general business security agreement and a second lien charge on all other assets of the business. The amount available under the general operating facility is subject to a borrowing base formula applied to accounts receivable and inventories. As of December 31, 2021, $18.4 million (excluding unamortized transaction costs) was drawn under this facility (December 31, 2020 - $3.7 million).

The ABL facility includes a standby letter of credit facility that does not affect the facility's borrowing base. In March 2021, this facility was increased by US$3.5 million, thereby reducing amounts committed to supporting letters of credit under the ABL facility by the same amount. Concurrent with the facility reduction and as per the terms of the senior secured term loan, a $2.0 million repayment was completed (see below). The Credit Facility was also being used to support $10.0 million of letters of credit (December 31, 2020 - $14.6 million) leaving $12.5 million of available liquidity (December 31, 2020 - $17.3 million). Source is subject to externally imposed capital requirements for the Credit Facility, requiring the Company to maintain the financial covenants as outlined above.

Source has an additional credit facility in the form of a senior secured term loan (the "Term Loan") with an initial principal amount of up to $20 million. The Term Loan bears interest at Canadian prime plus 6% and matures on September 30, 2023, provided that the Term Loan shall be reduced to $10.5 million on March 31, 2022 and further reduced to $5.0 million on March 31, 2023. The Term Loan is secured by a fixed and floating first charge over all assets of the business. In March 2021, a $2.0 million repayment was completed reducing the amount drawn on this facility to $18.0 million as at December 31, 2021, as outlined above.

Cash and Net Working Capital

($000's)	**December 31, 2021**	**December 31, 2020**
Current assets	106,745	91,547
Current liabilities	(50,308)	(46,037)
Net working capital	56,437	45,510

Total current assets less total current liabilities (net working capital) as at December 31, 2021 was $56.4 million, compared to $45.5 million as at December 31, 2020. The increase in net working capital was due primarily to an increase in accounts receivable as a result of higher sales volumes and higher levels of inventory on hand at the end of the year to accommodate first quarter sales volumes. Lower levels of trade accounts payable at the end of 2021 also contributed to the build in net working capital, compared to greater amounts of trade accounts payable outstanding prior to the closing of the Recapitalization Transaction last year, partially offset by an increase in current liabilities related to the current portion of the Term Loan, payable in March of 2022.

Foreign Currency Risk

Source is exposed to currency price risk on sales denominated in US dollars to the extent that the receipt of payment of the US denominated accounts receivable are subject to fluctuations in the related foreign exchange rate. In addition, foreign currency risk exists on the cost of manufacturing and transporting inventory for sale to the extent that the payment of those costs are foreign denominated accounts payable and are subject to fluctuations in the foreign exchange rate. Source monitors its net foreign currency exposure on a regular basis. Included in accounts receivable and accounts payable and accrued liabilities at December 31, 2021 are $14.7 million (December 31, 2020 - $18.5 million) and $11.1 million (December 31, 2020 - $14.9 million) denominated in foreign currency, respectively. The net effect of each 1% change in foreign exchange would have an impact on net income of $0.4 million for the three months ended December 31, 2021 (three months ended December 31, 2020 - $0.2 million).

In order to manage exposure to fluctuations in the Canadian to US dollar exchange rate, the Company's policy is to hedge up to certain prescribed maximum amounts of its net US dollar exposure on a monthly basis, as determined by the Company's foreign currency risk management policy, through the purchase of various instruments. As of March 9, 2022, Company has US dollar foreign exchange forward contracts outstanding that mature during 2022, with notional amounts ranging from US$4,000 per month to US$14,000 per month at 1.2473 to 1.2532 per Canadian dollar. The Company also has contracts in place from January through October 2023, with a notional value of US$2,000 per month at rates of 1.2440 to 1.2446 per Canadian dollar.

Contractual Obligations

Source has various commitments regarding lease agreements, various IT software subscriptions and physical natural gas contracts. The leases expire between January 2022 and March 2032, the IT software subscriptions expire between January 2023 and September 2026 and the natural gas contracts expire in March 2023. The financial liabilities on Source's consolidated statements of financial position consist of the Notes, Credit Facility and leases. Source's planned cash outflows relating to lease commitments and financial liabilities are outlined in the table below:

($000's)	**Total**	**2022**	**2023**	**2024**	**2025**	**2026**	**2027 and beyond**
Lease liabilities	39,277	13,549	9,277	6,981	4,130	1,648	3,692
Other commitments	4,071	2,627	1,396	20	16	12	—
Credit Facility(1)	36,406	7,500	28,906	—	—	—	—
Notes(2)	216,264	15,047	17,160	17,169	166,888	—	—

Notes:
(1) Interest payments on such balances have been excluded from the above table as the amount and timing of any interest payments will fluctuate depending on balances outstanding and applicable interest rates. Based on December 31, 2021 balances and interest rates, and assuming amounts remain outstanding until maturity, estimated total interest expense would be $7.2 million.
(2) Includes interest for future periods and assumes the Company will elect to pay interest in kind at a rate of 12.5% through February 15, 2022 and subsequently pay interest in cash at 10.5%, refer to 'Long-term Debt' above for additional information.

Source is a party to contracts with numerous customers. Source's customers consist primarily of E&P companies and pressure pumping companies operating in the WCSB. Source has structured contracts with customers outlining fixed pricing, the terms of which vary from one to three years. This mitigates the impact of any non-payment or non-performance or significant reduction in purchases by any of these contracted customers. Source's customers are also serviced on a spot basis where volume thresholds are not set, and orders are serviced on an as-available basis at prevailing market prices.

In the ordinary course of conducting business, Source occasionally becomes involved in legal proceedings relating to contracts, environmental issues or other matters. While any proceeding or litigation has an element of uncertainty, management of Source believes that the outcome of any pending or threatened actions will not have a material adverse effect on the business or on the financial condition of Source, except as follows:

Source is currently pursuing claims against certain organizations in respect of damages related to the structural failure of assets at its Fox Creek terminal facility. Source intends to pursue this matter for which the damages, if awarded to the Company in their entirety, could be a material amount. However, litigation is inherently uncertain and a favorable outcome cannot be assured.

Off-Balance Sheet Arrangements

Source does not have any off-balance sheet arrangements at this time.

Outstanding Shares

As at December 31, 2021 and March 9, 2022, Source had issued and outstanding 13,545,055 common shares (December 31, 2020 - 13,545,055).

Transactions between Related Parties

During the three and twelve months ended December 31, 2021 there were no related party transactions.

Proposed Transactions

Source does not have any proposed transactions other than those occurring in the ordinary course of business.

Selected Annual Information

($000's, except per unit amounts)	2021	2020	2019
Total assets	266,031	266,261	496,665
Senior secured notes	147,350	125,493	150,028
Other non-current liabilities(1)	61,847	62,044	79,902
Total revenue	319,861	249,878	332,956
Net loss	(24,403)	(185,466)	(89,955)
Net loss per share, basic and diluted(2)	(1.80)	(36.81)	(17.68)

Notes:
(1) 2019 includes $40.3 million of liabilities related to leases recognized as a result of the adoption of IFRS 16.
(2) 2019 net loss per share, basic and diluted has been restated to reflect the 12:1 share consolidation pursuant to the Recapitalization Transaction.

Controls and Procedures

The Company is required to comply with National Instrument 52-109 - *Certification of Disclosure in Issuers' Annual and Interim Filings*. The certificate for annual filings requires the Chief Executive Officer and the Chief Financial Officer to certify the design of Source's disclosure controls and procedures ("DC&P") and internal control over financial reporting ("ICFR") as at December 31, 2021. There were no material weaknesses in the design of the DC&P and the ICFR at December 31, 2021, and no changes in ICFR during the period beginning on January 1, 2021 and ended on December 31, 2021 that have materially affected or are reasonably likely to materially affect Source's ICFR. The control framework used to design the Company's ICFR is the framework in Internal Control – Integrated Framework (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission. While the Company's certifying officers believe that the Company's DC&P and ICFR provide a reasonable level of assurance with regard to their effectiveness, a control system, no matter how well conceived or operated, can provide only reasonable, not absolute, assurance that the objectives of the control system will be met and it should not be expected that the control system will prevent all errors or fraud.

Business Risks

The following business risks are not a complete list of risks and for additional information regarding the risks that Source is exposed to, see the disclosure provided under the heading "Risk Factors" in the Company's AIF.

All of Source's frac sand is currently produced from the Sumner Facility, the Blair Facility, and the Preston Facility, and the delivery of that frac sand to Source's customers is primarily served by one rail line. Any adverse developments at a facility or on the rail line could have a material adverse effect on Source's business, financial condition and results of operations

All of Source's sand is currently derived from the Sumner Facility, the Blair Facility, and the Preston Facility which are served primarily by a single Class I rail line owned by Canadian National Railway Company. Any adverse development at the Sumner Facility, the Blair Facility, or the Preston Facility or on the rail line due to catastrophic events or weather, or any other event that would cause Source to curtail, suspend or terminate operations at its facilities, could result in Source being unable to meet its sand deliveries. Although Source maintains insurance coverage to cover a portion of these types of risks, there are potential risks associated with Source's operations not covered by insurance. There also may be certain risks covered by insurance where the policy does not reimburse Source for all of the costs related to a loss. Downtime or other delays or interruptions to Source's operations that are not covered by insurance could have a material adverse effect on Source's business, results of operations and financial condition. In addition, since Sumner Facility, the Blair Facility, and the Preston Facility are all served by a single Class I rail line, any adverse changes to the existing rail rates, rail car leases, or other logistics costs would adversely affect Source's business operations and financial position.

Source's indebtedness could adversely affect its financial flexibility and its competitive position

Source's indebtedness under the Credit Facilities and the Secured Notes could have significant effects on its business. For example, it could:

- increase Source's vulnerability to adverse changes in general economic, industry and competitive conditions;
- require Source to dedicate a substantial portion of its cash flow from operations to make payments on its indebtedness, thereby reducing the availability of its cash flow to fund working capital, capital expenditures and other general corporate purposes;
- limit its flexibility in planning for, or reacting to, changes in Source's business and the industry in which Source operates;
- restrict Source from exploiting business opportunities;
- make it more difficult to satisfy its financial obligations, including payments on its indebtedness;

- place Source at a disadvantage compared to its competitors that have less debt; and
- limit Source's ability to borrow additional funds for working capital, capital expenditures, acquisitions, debt service requirements, execution of its business strategy or other general corporate purposes.

Source's business and financial performance depend on the level of activity in the oil and natural gas industry

Substantially all of Source's revenues are derived from the sale of proppant to companies in the oil and natural gas industry in the WCSB. As a result, Source's operations are dependent on the levels of activity in oil and natural gas exploration, development and production primarily in the WCSB. More specifically, the demand for the proppants Source produces is closely related to the number of oil and natural gas wells completed in geological formations that Source serves and where sand-based proppants are used in hydraulic fracturing activities. These activity levels are affected by both short and long-term trends in oil and natural gas prices, among other factors. Historically, oil and natural gas prices have been volatile and are subject to fluctuations in response to changes in supply and demand, market uncertainty and a variety of additional factors that are beyond the Company's control. Oil and natural gas prices and, therefore, the level of exploration, development and production activity, have decreased significantly since mid-2014. Oil and natural gas prices remain unstable because of market uncertainties over the supply and the demand of these commodities due to the current state of the world economy, OPEC actions, sanctions imposed on certain oil producing nations by other countries, ongoing credit and liquidity concerns, and the impact of protectionist measures on foreign trade. For instance, during the first quarter of 2020, OPEC and Russia failed to agree on a plan to cut production of oil and related commodities. Subsequently, Saudi Arabia announced plans to increase production and reduce the prices at which they sell oil. In response to the oversupply of crude oil caused by COVID19 and the actions of OPEC, Saudi Arabia and Russia, certain state regulators in the U.S. are considering prorating production of hydrocarbons. These events, combined with the outbreak of COVID-19 that has reduced economic activity and the related demand for oil, contributed to a sharp drop in prices for crude oil, natural gas and NGLs in the first half of 2020. While COVID-19 vaccines have started to be administered in many countries and oil and natural gas prices have partially recovered from the first half of 2020, new variants of COVID-19 could impact the pace of any recovery of demand for oil and natural gas, and the timing of widespread lockdowns being lifted is uncertain. If conditions continue to deteriorate and persist, this will adversely impact Source's operations as could conditions such as economic, environment, regulatory and pipeline egress issues in Canada. Furthermore, the availability of key resources that impact drilling activity has experienced significant fluctuations and could impact demand for the Company's products. A prolonged reduction in oil and natural gas prices would generally depress the level of oil and natural gas exploration, development, production and well completion activity and would result in a corresponding decline in the demand for the proppants Source produces. Such a decline would have a material adverse effect on Source's business, results of its operations, and its financial condition. Furthermore, the commercial development of economically viable alternative energy sources (such as wind, solar, geothermal, tidal, fuel cells and biofuels) could have a similar effect. Any future decreases in the rate at which oil and natural gas reserves are discovered or developed, whether due to the passage of legislation, increased governmental regulation leading to limitations, or prohibitions on exploration and drilling activity, including hydraulic fracturing, or other factors, could have a material adverse effect on Source's business and financial condition, even in a stronger oil and natural gas price environment.

Source's business may be adversely affected by changing economic conditions beyond its control, including decreases in oil and natural gas development

Source's revenue is closely tied to conditions in the oil and natural gas industry in which its customers operate, and more broadly to general economic conditions. Source's product and services are used primarily in oil and gas exploration and production in Western Canada and the United States. Consequently, economic downturns and particularly weakness in the oil and natural gas market may lead to a significant decrease in demand for Source's products and services or depress utilization rates and the prices for the products and services Source sells. During periods of expansion in Source's respective end markets, Source generally has benefited from increased demand for its products and services. However, during recessionary periods in Source's end markets, Source may be adversely affected by reduced demand for its products and services. Weakness in Source's end markets, such as a decline in oil and natural gas exploration and production, may in the future lead to a decrease in the demand for Source's products and services or the price Source can charge for its products and services, which could adversely affect Source's operating results by decreasing revenues and profit margins. Deterioration in the oil and natural gas industry could have a material adverse effect on Source's business, financial position, results of operations and cash flows in the future.

Source relies on a small number of customers for the majority of its revenue

Source relies on a small number of large customers for most of its revenue, and the loss of one or more such customers would adversely affect Source's results of operations and cash flows. Source's five largest customers accounted for 80% of its revenue for the year ended December 31, 2021. Although a significant percentage of Source's customers are under contract, certain contracts do not provide for guaranteed volumes and can be terminated on short notice and, on occasion, certain customers may demand to renegotiate a contract prior to the end of its term. There can be no assurance that Source's current customers will continue their relationships with Source or that contracts that come up for renewal will be renewed or, if they are renewed, that customers will contract for the same amounts or that they will pay the same prices as they have in the past. The loss of one or more major customers, the failure to renew customer contracts, or any decrease in products or services purchased or prices paid or any other changes to the terms of service under renewed contracts could have a material adverse effect on Source's business, financial position, results of operations and cash flows. A substantial portion of Source's customer contracts, including contract renewals, are subject to competitive tender processes, and there can be no assurance that Source will be successful in acquiring new business or retaining existing business subject to competitive tender. As a result of the limited number of customers that Source currently serves, Source's operations are subject to counterparty risk. The ability or willingness of each of Source's customers to perform its obligations under an agreement with Source will depend on a number of factors that are beyond Source's control and may include, among other things, the overall financial condition of the counterparty, the condition of the Canadian and US oil and natural gas exploration and production industry, the continuing use of frac sand in hydraulic fracturing operations and general economic conditions. In addition, in depressed market conditions, Source's customers may no longer need the amount of frac sand for which they have indicated or agreed to, or may be able to obtain comparable products at a lower price. If Source's customers experience a significant downturn in their business or financial condition, they may attempt to renegotiate Source's agreements. In addition, as agreements expire, depending on market conditions at the time, Source's customers may choose not to extend, or to adjust the terms of, these agreements which could lead to a significant reduction of sales volumes and corresponding revenues cash flows and financial condition if Source is not able to replace these expected sales volumes with new sales volumes. Additionally, even if Source were to replace any lost volumes, under current market conditions, lower prices for its product could materially reduce its revenues, cash flow and financial condition.

The Company's information assets and critical infrastructure may be subject to cyber security risks

The Company is subject to a variety of information technology and system risks as a part of its normal course operations, including potential breakdown, user errors, invasion, virus, computer viruses, cyber-attack, cyber-fraud, hackers or malicious actors, security or data breach, and destruction or interruption of the Company's information technology systems by third parties or insiders.

Despite Source's security measures and controls, which are designed to mitigate these risks, a breach of its security measures and/or a loss of information could occur and result in a loss of material and confidential information and reputation, breach of privacy laws and a disruption to the Company's business activities by limiting its capacity to effectively monitor and control Source's operations and adjust to changing market conditions. Source's failure to appropriately maintain the security of the data Source holds, whether as a result of Source's own error or the malfeasance or errors of others, could harm Source's reputation or give rise to legal liabilities leading to lower revenues, increased costs and other adverse effects on Source's results of operations. Any future cyber security attacks that affect Source's facilities, communications systems, Source's customers or any of Source's financial data could have a material adverse effect on Source's business. In addition, cyber-attacks on Source's customer and employee data may result in a financial loss and may negatively impact Source's reputation. Third-party systems on which Source relies could also suffer operational system failure. The significance of any such event is difficult to quantify but may in certain circumstances be material to the Company and could have adverse effects on the Company's business, reputation, financial condition and results of operations.

Although Source maintains specialized insurance for possible liability resulting from a cyber-attack on Source's assets that may shut down all or part of Source's business, there may be certain risks covered by insurance where the policy does not reimburse Source for all of the costs related to a loss. Such events, unauthorized access or other interruptions to Source's operations could result in the loss of confidential information, intellectual property, litigation, remediation costs, damage to our reputation and may negatively impact our ability to service our customers as such this could have a material adverse effect on Source's business, reputation, operations and financial condition.

Source's operations are subject to operating risks that are often beyond its control and could adversely affect production levels and costs

Source's mining, processing and production facilities, its logistics operations and any future properties it develops or may acquire in the future are and will be subject to risks normally encountered in the frac sand industry. These risks include:

- changes in the price and availability of transportation;
- inability to obtain necessary production equipment or replacement parts;
- inclement or hazardous weather conditions, including flooding, and the physical impacts of climate change;
- unanticipated ground, grade or water conditions;
- inability to acquire or maintain necessary permits or mining or water rights;

- late delivery of supplies;
- changes in the price and availability of natural gas or electricity that Source uses as fuel sources for its frac sand plants and equipment;
- technical difficulties or failures;
- cave-ins or similar pit wall failures;
- environmental hazards, such as unauthorized spills, releases and discharges of wastes, tank ruptures and emissions of unpermitted levels of pollutants;
- industrial accidents;
- changes in laws and regulations (or the interpretation thereof) related to the mining and oil and natural gas industries, silica dust exposure or the environment;
- inability of Source's customers or distribution partners to take delivery;
- reduction in the amount of water available for processing;
- fires, explosions or other accidents; and
- facility shutdowns in response to environmental regulatory actions.

The occurrence of any of these events could have a material adverse effect on Source's business, financial position, results of operations and cash flows.

Source faces significant competition that may cause it to lose market share

The proppant industry is highly competitive. The proppant market is characterized by a small number of large, national producers and a large number of small, regional or local producers. Competition in this industry is based on price, consistency and quality of product, site location, distribution capability, customer service, reliability of supply, breadth of product offering and technical support. Some of Source's competitors have greater financial and other resources than Source does. In addition, Source's larger competitors may develop technology superior to Source's or may have production facilities that offer lower cost transportation to certain customer locations than Source does. When the demand for hydraulic fracturing services decreases or the supply of proppant available in the market increases, prices in the frac sand market can materially decrease. Furthermore, oil and natural gas exploration and production companies and other providers of hydraulic fracturing services have acquired and, in the future, may acquire their own frac sand reserves to fulfill their proppant requirements, and these other market participants may expand their existing frac sand production capacity, all of which would negatively impact demand for Source's frac sand. In addition, increased competition in the proppant industry could have an adverse impact on Source's ability to enter into long term contracts or to enter into contracts on favourable terms.

Source's proppant sales are subject to fluctuations in market pricing

A majority of Source's supply agreements involving the sale of frac sand contain market-based pricing mechanisms. Accordingly, in periods with decreasing prices, Source's results of operations may be lower than if Source's agreements had fixed prices. During these periods Source's customers may also elect to reduce their purchases from Source and seek to find alternative, cheaper sources of supply. In periods with increasing prices, these agreements permit Source to increase prices; however, these increases are generally calculated on a quarterly basis and do not increase on a dollar-for-dollar basis with increases in spot market pricing. Furthermore, certain volume-based supply agreements may restrict the ability to fully capture current market pricing. These pricing provisions may result in significant variability in Source's results of operations and cash flows from period to period. Changes in supply and demand dynamics could also impact market pricing for proppants. A number of existing proppant providers and new market entrants have announced reserve acquisitions, processing capacity expansions and greenfield projects. In periods where sources of supply of frac sand exceed market demand, market prices for frac sand may decline and Source's results of operations and cash flows may correspondingly decline, be volatile, or otherwise be adversely affected.

Restrictions in the Amended Credit Agreement and the Secured Note Indenture may limit Source's ability to capitalize on potential acquisition and other business opportunities

The operating and financial restrictions and covenants in the Amended Credit Agreement and the Secured Note Indenture and any future financing agreements could restrict Source's ability to finance future operations or capital needs or to expand or pursue its business activities. For example, the Amended Credit Agreement and the Secured Note Indenture restrict or limit Source's ability to:

- grant liens;
- incur additional indebtedness;
- engage in a merger, consolidation or dissolution;
- enter into transactions with affiliates;
- sell or otherwise dispose of assets, businesses and operations;
- materially alter the character of Source's business; and
- make acquisitions, investments and capital expenditures.

Furthermore, the Amended Credit Agreement and the Secured Note Indenture contain certain operating and financial covenants. Source's ability to comply with such covenants and restrictions may be affected by events beyond its control, including prevailing economic, financial and industry conditions. If market or other economic conditions deteriorate, Source's ability to comply with these covenants may be impaired. Further, if Source violates any of the restrictions, covenants, ratios or tests in the Amended Credit Agreement, a significant portion of Source's indebtedness may become immediately due and payable, and any lenders' commitment to make further loans to Source may terminate. Source might not have, or be able to obtain, sufficient funds to make these accelerated payments. Any subsequent replacement of the Amended Credit Agreement or any new indebtedness could have similar or greater restrictions.

Climate-related risks have the potential to impact Source's operations

Climate-related risks have the potential to impact Source's operations, the delivery of its services and future financial condition. Significant changes, such as more frequent, severe weather in the markets Source serves or the areas where our assets are located, could cause increased expenses and impact to its operations and the operations of its customers. As a service provider to its customers in the oil and gas industry, Source is unable to predict how a change in the environmental or regulatory regime might affect our customers and consequently our business model. The costs associated with interrupted operations will depend on the duration and severity of any physical event, the impact on its customers and the damage to be repaired and remedial work to be carried out. Financial implications could include business interruption, damage or loss of production and uptime. While Source does not currently have a formal risk management process in place to identify and assess the potential size, scope and prioritization of climate-related risks, Source's business operations are, located, designed and operated to accommodate a range of climate conditions. Given the evolving nature of the environmental and regulatory regime surrounding climate change, it is not currently possible to predict the impact it may have on its future financial conditions, operations and customers.

COVID-19 and other global or national health concerns, including the outbreak of pandemic or contagious diseases, may adversely affect Source

The Company's business, operations and financial condition could be materially adversely affected by the outbreak of epidemics or pandemics or other health crises. On March 11, 2020, the World Health Organization declared COVID-19 a pandemic. Reactions to and outbreaks of COVID-19 across the globe have caused cities, provinces, states, countries and companies to impose unprecedented restrictions such as quarantines, closures, shelter in place declarations and travel restrictions, among other measures, in an attempt to slow the spread of COVID-19. The duration of the business disruptions domestically and internationally and related financial impacts cannot be reasonably estimated at this time and may last for an extended period of time. Such public health crises can result in volatility and disruptions in the supply and demand for oil and natural gas, global supply chains and financial markets, as well as declining trade and market sentiment and reduced mobility of people, all of which could affect commodity prices, interest rates, credit ratings, credit risk and inflation. In particular, oil prices significantly weakened in response to COVID-19. The risks to the Company of such public health crises also include risks to employee health and safety and a slowdown or temporary suspension of operations in geographic locations impacted by an outbreak. At this point, the extent to which COVID-19 may impact the Company is uncertain; however, it is possible that COVID-19 may have a material adverse effect on the Company's business, results of operations and financial condition. Global or national health concerns, including the outbreak of pandemic or contagious diseases, such as COVID-19, may adversely affect the Company by: (i) reducing global economic activity thereby resulting in lower demand for crude oil, NGLs and natural gas, which in turn could also reduce the demand for Source's frac sand; (ii) interrupting the Company's operations (for example, as a result of government mandated shut-down or other preventative measures, or illness among our workforce); and (iii) affecting the health of the Company's workforce, rendering employees unable to work or travel. Should an employee or visitor at any of the Company's facilities, offices or work sites become infected with a serious illness that has the potential to spread rapidly, this could place our workforce at risk. COVID-19 is one example of such an illness. The Company takes precautions to strictly meet or exceed industrial hygiene and occupational health and safety guidelines. Additionally, the Company follows posted health guidelines to protect the health of its employees and decrease the potential impact of serious illness on the Company's operations. There can be no assurance that COVID-19 or another infectious illness will not impact the Company's personnel and ultimately its operations.

Financial Instruments and Other Instruments

Risk Management Overview

Source's activities expose it to a variety of financial risks including credit risk, liquidity risk and market risk. Further quantitative disclosures are included in the Company's financial statements. Source employs risk management strategies and policies to ensure that any exposures to risk are in compliance with Source's business objectives and risk tolerance levels. While the Board has the overall responsibility for Source's risk management framework, Source's management has the responsibility to administer and monitor these risks.

For additional information regarding the risks that Source is exposed to, see the disclosure provided under the heading ‘Risk Factors’ in the AIF.

Fair Value of Financial Instruments

The fair values of cash, accounts receivable, accounts payable and accrued liabilities approximate their carrying values due to the short-term maturity of those instruments. The fair value of the Credit Facility approximates the carrying value as it bears interest at floating market rates consistent with market rates for similar debt. Based on the closing market price as of December 31, 2021, the fair value of the Notes was $90.3 million. In October 2021, Source entered into currency hedging arrangements. At December 31, 2021, the fair value of these derivative assets were $1.7 million.

Critical Accounting Estimates

The following discussion sets forth management’s most critical estimates and assumptions in determining the value of assets, liabilities and equity.

Allowance for doubtful accounts

The Company performs ongoing credit evaluations of its customers and grants credit based on a review of historical collection experience, current aging status, the customer’s financial condition and anticipated industry conditions. Customer payments are regularly monitored. A provision for doubtful accounts is established based on the expected credit loss model under IFRS 9.

Inventories

The Company evaluates its inventory to ensure it is carried at the lower of average cost and net realizable value. Allowances are made against obsolete or damaged inventories and charged to cost of sales. The reversal of any write-down of inventory arising from an increase in net realizable value would be recognized as a reduction in cost of sales in the period in which the reversal occurred.

Depreciation

The amounts recorded for depreciation of property and equipment are based on estimates of the useful lives of the assets and residual values. The estimated residual value and useful lives of property and equipment are reviewed at the end of each reporting period and adjusted if required.

Decommissioning liabilities

The amounts recorded for decommissioning liabilities are based on the Company’s mining activities and the estimated costs to abandon and reclaim the land and facilities, the estimated time period in which these costs will be incurred in the future and the discount and inflation rates. Any changes to these estimates could change the amount of decommissioning liability and may materially impact the consolidated financial statements in future periods.

Income taxes

The amounts recorded for deferred income taxes are based on estimates regarding the timing of the reversal of temporary differences and tax rates currently substantively enacted. Legislation and regulations in the various jurisdictions that the Company operates in are subject to change and differing interpretations require management judgment. Income tax filings are subject to audits, re-assessments and changes in facts, circumstances and interpretations of the standards could result in a material change in the Company’s provision for income taxes. As such, income taxes are subject to measurement uncertainty including judgment regarding the recognition or derecognition of deferred tax assets.

Share-based compensation

The Company’s compensation plans include the following award types: stock option, RSUs, PSUs, DSUs and SARs. DSUs and SARs are cash-settled awards and RSUs and PSUs may be settled in common shares but are expected to be settled for cash. As such, these awards are considered liability-settled awards for accounting purposes. The fair value of stock options and SARs are estimated using the Black-Scholes option pricing model, which includes underlying assumptions related to the risk-free interest rate, average expected unit life, estimated forfeitures and estimated volatility of Source.

Cash-generating units

The determination of a cash-generating unit (“CGU”) is based on management’s judgment regarding geographical proximity, shared equipment and mobility of equipment. Management has determined that the Company’s operations represent one CGU.

Impairment of non-financial assets

Assets that are subject to depreciation are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognized for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs of disposal and value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are largely independent cash inflows (CGUs). The recoverable amount of a CGU is determined using an approach which considers a discounted cash flow model and an earnings multiple approach. The discounted cash flow model incorporates significant assumptions including a revenue growth rate and discount rate. The earnings multiple approach uses earnings before interest, taxes, depreciation and amortization less corporate expenses and comparable market multiples to determine the recoverable amount of the CGU. Prior impairments of non-financial assets are reviewed for possible reversal at each reporting date.

Embedded derivatives

An embedded derivative is a component of a contract that modifies the cash flows of the contract. Embedded derivatives are separated from the contract and accounted for as derivative liabilities or assets. Embedded derivatives are measured at fair value through profit or loss. The fair value of the derivatives may be based on prices or valuation techniques that require inputs that are not based on observable market data.

Revenue recognition

Contractual arrangements for revenue may have multiple contractual elements within them, resulting in complex recognition in the financial statements. The contractual elements which require significant consideration may include embedded derivatives, contract liabilities, take-or-pay commitments and leasing arrangements. Significant judgement is required in identifying and assessing the appropriate accounting recognition for each contractual element identified within these contractual arrangements.

Newly Adopted Accounting Policies

The following amendments have been issued by the IASB and were adopted by the Company effective for the fiscal year beginning January 1, 2021:

Standard	Description of change
Interest rate benchmark reform - Phase 2 (Amendments to IFRS 9, IAS 39, IFRS 7, IFRS 4 and IFRS 16)	The amendments introduce a practical expedient to account for a change in the basis for determining the contractual cash flows of financial instruments that are affected by IBOR reform.
COVID-19 related rent concessions (Amendment to IFRS 16)	The amendment provides a practical expedient that relieves a lessee from determining whether a COVID-19 rent-related concession is a lease modification.

The Company completed its assessment of the impact of the amendments and concluded that they do not have a material impact on the consolidated financial statements.

Future Accounting Policy Changes

The following amendments to accounting standards, issued by the IASB, are effective for fiscal years beginning on or after January 1, 2022:

Standard	Description of change
Classification of Liabilities as Current or Non-current (Amendment to IAS 1)	This amendment clarifies the classification requirements for non-current liabilities.
Deferred Tax related to Assets and Liabilities arising from a Single Transaction (Amendment to IAS 12)	This amendment changes the deferred tax initial recognition exemption, which does not apply to transactions in which both deductible and taxable temporary differences arise on initial recognition that result in the recognition of deferred tax assets and liabilities in the same amount.
Property, Plant and Equipment - Proceeds before intended use (Amendment to IAS 16)	This amendment states that deducting proceeds from selling items produced while bringing an asset to its intended use from the cost of the asset is prohibited and shall be recognized in profit or loss.
Provisions, Contingent Liabilities and Contingent Assets - Onerous Contracts (Amendment to IAS 37)	This amendment clarifies the costs that shall be included in determining the cost of fulfilling a contract when assessing whether a contract is onerous.
Disclosure of Accounting Policies (Amendment to IAS 1)	This amendment states that a complete set of financial statements shall disclose material, rather than significant, accounting policy information.
Definition of Accounting Estimates (Amendment to IAS 8)	This amendment introduces a new definition for accounting estimates.

The Company intends to adopt the amendments on their respective effective dates and the revisions are not expected to have a material impact on the consolidated financial statements.

NON-IFRS MEASURES

This MD&A refers to certain financial measures that are not determined in accordance with IFRS. These financial measures do not have standardized meanings prescribed by IFRS and Source's method of calculating these measures may differ from the method used by other entities and, accordingly, they may not be comparable to similar measures presented by other companies. These financial measures should not be considered as an alternative to, or more meaningful than, net income (loss), cash flows from operating activities, gross margin and other measures of financial performance as determined in accordance with IFRS.

Source believes that the non-IFRS measure of Adjusted EBITDA is a useful measure to management and investors to provide relative performance and measure changes in respect of Source's financial performance in the context of earnings generated to fund capital investments and meet financial obligations. Adjusted Gross Margin is useful to management and investors in measuring pricing and operating cost performance relative to other publicly listed competitors throughout North America. Free Cash Flow is a useful measure to management and investors as it reflects the Company's ability to generate cash flows that can be used to pay down long-term debt or provide other forms of returns to investors. Adjusted EBITDA per MT and Adjusted Gross Margin per MT are calculated by taking the non-IFRS measures and dividing by sand volumes for the periods stated.

Adjusted EBITDA represents earnings generated to fund capital investments and meet financial obligations. It represents, for the period presented, net income (loss) plus income taxes, interest expense, cost of sales - depreciation, depreciation, amortization, impairment and gain on debt extinguishment; and is adjusted to add back or deduct, as applicable, the following expense charges or benefits incurred in such period which, in management's view, are not indicative of the underlying business performance: finance expense excluding interest expense, loss (gain) on asset disposal, transaction and related professional fees, unrealized loss (gain) on derivative instruments, gain on settlement of deferred revenue, share-based compensation, loss (gain) on sublease and other expense as it relates to the incident at the Fox Creek terminal facility.

Adjusted Gross Margin represents a margin more comparable to other publicly listed competitors throughout North America. It represents, for the period presented, gross margin plus cost of sales - depreciation.

Free Cash Flow represents, for the period presented, cash flows provided by (used in) operating activities adjusted for financing expense paid, maintenance and sustaining capital spend needed to maintain operations, mandatory debt repayments and various non-cash operating activities. Free Cash Flow is considered a key non-IFRS measure as it reflects Source's ability to generate cash flows that can be used to pay down long-term debt or provide other forms of returns to investors. The reconciliation to the comparable IFRS measure, cash flows provided by (used in) operating activities, can be found on page 10.

This MD&A makes reference to these non-IFRS measures. These non-IFRS measures and other financial estimates of management are based upon variable components. There can be no assurance that these components and future calculations of non-IFRS measures will not vary. Investors are cautioned not to consider these non-IFRS measures in isolation or place undue reliance on ratios or percentages calculated using these non-IFRS measures.

Reconciliation of Adjusted EBITDA to Net Income

	Three months ended December 31,		Year ended December 31,	
($000's)	**2021**	2020	**2021**	2020
Net loss	**(14,566)**	24,015	**(24,403)**	(185,466)
Add:				
Income taxes	**—**	—	**—**	31,350
Interest expense	**6,594**	6,615	**25,677**	25,052
Cost of sales – depreciation	**4,071**	5,253	**21,102**	32,188
Depreciation	**2,426**	2,647	**9,873**	13,860
Impairment expense	**—**	—	**—**	143,656
Gain on debt extinguishment	**—**	(27,690)	**—**	(27,690)
Finance expense excluding interest expense	**1,215**	1,132	**4,643**	4,637
Share-based compensation expense (recovery)	**476**	77	**643**	(14)
Gain on asset disposal	**—**	—	**(63)**	(150)
Unrealized gain on derivative assets	**173**	—	**(247)**	—
Loss on sublease	**1,159**	—	**1,159**	—
Other expense(1)	**108**	112	**203**	298
Adjusted EBITDA	**1,656**	12,161	**38,587**	37,721

Note:
(1) Expenses related to the incident at the Fox Creek terminal facility, refer to 'Contractual Obligations' above.

Reconciliation of Gross Margin to Adjusted Gross Margin

	Three months ended December 31,		Year ended December 31,	
($000's)	**2021**	2020	**2021**	2020
Gross margin	**4,189**	11,066	**39,330**	24,657
Cost of sales – depreciation	**4,071**	5,253	**21,102**	32,188
Adjusted Gross Margin	**8,260**	16,319	**60,432**	56,845

FORWARD-LOOKING STATEMENTS

Certain statements contained in this MD&A constitute forward-looking statements relating to, without limitation, expectations, intentions, plans and beliefs, including information as to the future events, results of operations and Source's future performance (both operational and financial) and business prospects. In certain cases, forward-looking statements can be identified by the use of words such as "expects", "estimates", "intends", "anticipates", "believes", "continues", "plans", "predicts", "projects", "focus" or variations of such words and phrases, or state that certain actions, events or results "may" or "will" be taken, occur or be achieved. Such forward-looking statements reflect Source's beliefs, estimates and opinions regarding its future growth, results of operations, future performance (both operational and financial), and business prospects and opportunities at the time such statements are made, and Source undertakes no obligation to update forward-looking statements if these beliefs, estimates and opinions or circumstances should change unless required by applicable law. Forward-looking statements are necessarily based upon a number of estimates and assumptions made by Source that are inherently subject to significant business, economic, competitive, political and social uncertainties and contingencies. Forward-looking statements are not guarantees of future performance. In particular, this MD&A contains forward-looking statements pertaining, but not limited, to: Source's search for efficiencies to implement in order to lessen the impact of Source's activities on the environment; expectations regarding our 2022 annual ESG performance report; our expectation that strong cash flows among Source's customers in 2021 will result in expanded drilling and completion programs in 2022; our expectation that frac sand supply and demand will remain tight for 2022; increased demand for natural gas, increased natural gas pipeline export capabilities and LNG exports will drive incremental demand for Source's services in the WCSB; industry activity levels, including the continued increase in demand from customers primarily focused on the development of natural gas properties in Montney, Duvernay and Deep Basin; the Company's view that natural gas is an important transitional fuel for the successful movement to a less carbon intensive world; our focus on exploring and developing, and advancement of economic growth opportunities related to the transition to less carbon intense energy solutions; our focus on and expectations regarding increasing Source's involvement in the provision of logistics services for other wellsite items; outlook for commodity prices and sales volumes; expectations respecting future conditions; revenue and profitability; the benefits that Source's "last mile" services provide to customers; expectations regarding funding for future working capital and capital expenditures; Source's planned cash outflows relating to lease commitments and financial liabilities; the availability of any additional future funding; expectations on Source's ability to meet their capital needs; expectations regarding fluctuations in foreign currency; and expectations regarding the outcome of legal claims and proceedings, including but not limited to the outcome of Source's anticipated claim for damages related to the structural failure of its Fox Creek terminal facility.

By their nature, forward-looking statements involve numerous current assumptions, known and unknown risks, uncertainties and other factors which may cause the actual results, performance or achievements of Source to differ materially from those anticipated by Source and described in the forward-looking statements.

With respect to the forward-looking statements contained in this MD&A, assumptions have been made regarding, among other things: proppant market prices; future oil, natural gas and LNG prices; future global economic and financial conditions; future commodity prices, demand for oil and gas and the product mix of such demand; levels of activity in the oil and gas industry in the areas in which Source operates; the continued availability of timely and safe transportation for Source's products, including without limitation, Source's rail car fleet and the accessibility of additional transportation by rail and truck; the maintenance of Source's key customers and the financial strength of its key customers; the maintenance of Source's significant contracts or their replacement with new contracts on substantially similar terms and that contractual counterparties will comply with current contractual terms; operating costs; that the regulatory environment in which Source operates will be maintained in the manner currently anticipated by Source; future exchange and interest rates; geological and engineering estimates in respect of Source's resources; the recoverability of Source's resources; the accuracy and veracity of information and projections sourced from third parties respecting, among other things, future industry conditions and product demand; demand for horizontal drilling and hydraulic fracturing and the maintenance of current techniques and procedures, particularly with respect to the use of proppants; Source's ability to obtain qualified staff and equipment in a timely and cost-efficient manner; the regulatory framework governing royalties, taxes and environmental matters in the jurisdictions in which Source conducts its business and any other jurisdictions in which Source may conduct its business in the future; future capital expenditures to be made by Source; future sources of funding for Source's capital program; Source's future debt levels; the impact of competition on Source; and Source's ability to obtain financing on acceptable terms.

A number of factors, risks and uncertainties could cause results to differ materially from those anticipated and described herein including, among others: the effects of competition and pricing pressures; risks inherent in key customer dependence; effects of fluctuations in the price of proppants; risks related to indebtedness and liquidity, including Source's leverage, restrictive covenants in Source's debt instruments and Source's capital requirements; risks related to interest rate fluctuations and foreign exchange rate fluctuations; changes in general economic, financial, market and business conditions in the markets in which Source operates; changes in the technologies used to drill for and produce oil and natural gas; Source's ability to obtain, maintain and renew required permits, licenses and approvals from regulatory authorities; the stringent requirements of and potential changes to applicable legislation, regulations and standards; the ability of Source to comply with unexpected costs of government regulations; liabilities resulting from Source's operations; the results of litigation or regulatory proceedings that may be brought against Source; the ability of Source to successfully bid on new contracts and the loss of significant contracts; uninsured and underinsured losses; risks related to the transportation of Source's products, including potential rail line interruptions or a reduction in rail car availability; the geographic and customer concentration of Source; the impact of climate change risk; the ability of Source to retain and attract qualified management and staff in the markets in which Source operates; labor disputes and work stoppages and risks related to employee health and safety; general risks associated with the oil and natural gas industry, loss of markets, consumer and business spending and borrowing trends; limited, unfavorable, or a lack of access to capital markets; uncertainties inherent in estimating quantities of mineral resources; sand processing problems; implementation of recently issued accounting standards; the use and suitability of Source's accounting estimates and judgments; the impact of information systems and cyber security breaches; and risks and uncertainties related to COVID-19 or its variants, including changes in energy demand.

Although Source has attempted to identify important factors that could cause actual actions, events or results to differ materially from those described in the forward-looking statements, there may be other factors that cause actions, events or results not to be as anticipated, estimated or intended. There can be no assurance that forward-looking statements will materialize or prove to be accurate, as actual results and future events could differ materially from those anticipated in such statements. The forward-looking statements contained in this MD&A are expressly qualified by this cautionary statement. Readers should not place undue reliance on forward-looking statements. These statements speak only as of the date of this MD&A. Except as may be required by law, Source expressly disclaims any intention or obligation to revise or update any forward-looking statements or information whether as a result of new information, future events or otherwise.

Any financial outlook and future-oriented financial information contained in this MD&A regarding prospective financial performance, financial position or cash flows is based on assumptions about future events, including economic conditions and proposed courses of action based on management's assessment of the relevant information that is currently available. Projected operational information contains forward-looking information and is based on a number of material assumptions and factors, as are set out above. These projections may also be considered to contain future oriented financial information or a financial outlook. The actual results of Source's operations for any period will likely vary from the amounts set forth in these projections and such variations may be material. Actual results will vary from projected results. Readers are cautioned that any such financial outlook and future-oriented financial information contained herein should not be used for purposes other than those for which it is disclosed herein. The forward-looking information and statements contained in this document speak only as of the date hereof and have been approved by the Company's management as at the date hereof. The Company does not assume any obligation to publicly update or revise them to reflect new events or circumstances, except as may be required pursuant to applicable laws.