XS Financial Inc.

Financial Statements

For the Three and Nine Months ended September 30, 2020 and 2019

(Unaudited)

(Expressed in United States Dollars)

XS Financial Inc.

Table of Contents

NOTICE OF NO AUDITOR REVIEW OF CONDENSED INTERIM CONSOLIDATED FINANCIAL STATEMENTS

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

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

XS Financial Inc.
Condensed consolidated statements of (loss) income and comprehensive (loss) income
For the three and six months ended September 30, 2020 and 2019
(Unaudited)
(Expressed in United States dollars)

	Note	Three months ended September 30, 2020	Three months ended September 30, 2019	Nine months ended September 30, 2020	Nine months ended September 30, 2019
Revenue	7	$ 3,858,329	$ 663,468	$ 5,451,489	$ 1,635,493
Cost of sales	8	3,782,276	718,631	5,297,665	1,903,742
Gross profit (loss)		76,053	(55,163)	153,824	(268,249)
Administrative expenses	8	300,635	543,120	1,313,847	2,928,831
Sales and marketing expenses	8	63,399	82,389	338,822	168,036
Loss from operations		(287,981)	(680,672)	(1,498,845)	(3,365,116)
Financing expense, net	17	128,348	187,110	394,929	630,559
Accretion expense	17	89,656	606,056	241,462	1,518,850
Listing expense	6	-	363,095	-	363,095
Unrealized loss in fair value change of investments	9	320,698	-	2,218,744	-
Change in fair value of derivative liabilities	17	-	(3,706,506)	-	(889,229)
Loss on sale of property, plant and equipment and servicing equipment	14,15	-	81,352	-	101,569
Other (income) expense		(6,757)	(17,723)	(27,267)	(17,723)
(Loss) income before income tax		(819,926)	1,805,944	(4,326,713)	(5,072,237)
Income tax expense	21	-	-	-	975
Net (loss) income		$ (819,926)	$ 1,805,944	$ (4,326,713)	$ (5,073,212)
Other comprehensive (loss) income					
Items that will subsequently be reclassified to operations:					
Unrealized gain (loss) loss on foreign currency translation		2,679	(27,938)	(15,156)	(27,938)
Comprehensive (loss) income		$ (817,247)	$ 1,778,006	$ (4,341,869)	$ (5,101,150)
(Loss) income per share - basic and diluted		$ (0.02)	$ 0.05	$ (0.08)	$ (0.15)
(Loss) income per share - diluted		$ (0.02)	$ 0.04	$ (0.08)	$ (0.15)
Weighted average shares outstanding:					
Basic and diluted		54,589,706	36,295,096	52,563,488	33,974,504
Diluted		54,589,706	49,984,444	52,563,488	33,974,504

Approved on behalf of the Board:

Gary Herman, Director

Stephen Christoffersen, Director

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

XS Financial Inc.
Condensed consolidated statements of financial position
As of September 30, 2020 and December 31, 2019
(Expressed in United States dollars)

	Note	(Unaudited) September 30, 2020	December 31, 2019
Assets			
Current assets			
Cash		$ 717,012	$ 2,487,293
Restricted cash	17	650,000	-
Investments	9	843,071	-
Trade receivables, net	10	195,463	124,715
Financing receivables, short-term	11	765,955	480,466
Inventories	12	-	36,052
Prepaid and other current assets	13	145,747	244,581
Total current assets		3,317,248	3,373,107
Non-current assets			
Servicing equipment	14	300,864	783,195
Property, plant and equipment	15	9,496	7,506
Financing receivables, long-term	11	2,512,124	310,798
Total non-current assets		2,822,484	1,101,499
Total assets		$ 6,139,732	$ 4,474,606
Shareholders' equity and liabilities			
Current liabilities			
Loans and borrowings, short-term	17	$ 600,000	$ 600,000
Trade and other payables	19	698,973	119,752
Accrued expenses	20	964,369	201,317
Unearned revenue	7	17,000	-
Amounts due to related parties	23	38,067	-
Redeemable common stock	17	650,000	650,000
Total current liabilities		2,968,409	1,571,069
Non-current liabilities			
Loans and borrowings, long-term	17	2,257,436	1,978,544
Total liabilities		5,225,845	3,549,613
Shareholders' equity			
Share capital	16	14,359,110	10,342,678
Reserves		3,511,284	3,234,686
Conversion feature - debentures	16	996,668	958,935
Accumulated other comprehensive loss		(39,841)	(24,685)
Accumulated deficit		(17,913,334)	(13,586,621)
Total shareholders' equity		913,887	924,993
Total shareholders' equity and liabilities		$ 6,139,732	$ 4,474,606

Nature of operations and background information (Note 1)
Going concern (Note 3)
Subsequent events (Note 25)

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

XS Financial Inc.
Condensed consolidated statements of changes in equity
For the nine months ended September 30, 2020 and 2019
(Unaudited)
(Expressed in United States dollars)

	Note	Number of Common Shares	Number of Proportionate Common Shares	Share Capital	Reserves	Conversion feature for debentures	Accumulated other comprehensive loss	Accumulated deficit	Total
Balance at January 1, 2019		32,501,238	-	$ 4,737,813	$ 582,670	$ -	$ -	$ (6,214,702)	$ (894,219)
Issuance of Class A common stock	16	757,500	-	-	626,874	-	-	-	626,874
Fair value allocation of loan borrowing proceeds	17	-	-	-	263,587	-	-	-	263,587
Issuance of Proportionate Voting Shares	16	(17,737,588)	17,737	-	-	-	-	-	-
Shares issued to Caracara shareholders	6	3,896,958	-	953,167	-	-	-	-	953,167
Conversion of Series B and Series C debentures to common stock	16	10,050,378	359	4,498,139	1,101,800	-	-	-	5,599,939
Conversion feature of Sub Receipt debentures, net of tax	17	-	-	-	-	1,019,572	-	-	1,019,572
Conversion feature of convertible debentures	17	-	-	-	-	47,265	-	-	47,265
Conversion of Sub Receipt debentures to common stock and warrants	16,18	363,636	-	151,217	79,512	(94,650)	-	-	136,079
Issuance of warrants for services	18	-	-	-	649,341	-	-	-	649,341
Share-based incentive compensation	22	-	-	-	463,983	-	-	-	463,983
Net loss and comprehensive loss		-	-	-	-	-	(27,938)	(5,073,212)	(5,101,150)
Balance at September 30, 2019		29,832,122	18,096	$ 10,340,336	$ 3,767,767	$ 972,187	$ (27,938)	$ (11,287,914)	$ 3,764,438
Balance at January 1, 2020		29,986,764	12,507	$ 10,342,678	$ 3,234,686	$ 958,935	$ (24,685)	$ (13,586,621)	$ 924,993
Conversion of Sub Receipt debentures to common stock and warrants	16	48,181	-	18,332	(37,733)	37,733	-	-	18,332
Redeemable common stock held in escrow	17	-	-	650,000	-	-	-	-	650,000
Issuance of common shares to third party providers	16	1,069,047	-	190,047	-	-	-	-	190,047
Issuance of proportionate voting shares	16	-	10,600	3,061,815	-	-	-	-	3,061,815
Issuance of common shares for the purchase of a lenders license	16	450,671	-	96,238	-	-	-	-	96,238
Share-based incentive compensation	22	-	-	-	314,331	-	-	-	314,331
Net loss and comprehensive loss		-	-		-	-	(15,156)	(4,326,713)	(4,341,869)
Balance at September 30, 2020		31,554,663	23,107	$ 14,359,110	$ 3,511,284	$ 996,668	$ (39,841)	$ (17,913,334)	$ 913,887

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

XS Financial Inc.
Condensed consolidated statements of cash flows
For the nine months ended September 30, 2020 and 2019
(Unaudited)
(Expressed in United States dollars)

	Note	Nine months ended September 30, 2020	2019
Cash flows from operating activities			
Loss for the period		$ (4,326,713)	$ (5,073,212)
Adjustments to reconcile loss to net cash flows:			
Depreciation and amortization	14,15	89,995	418,694
Gain on sale of servicing equipment to a customer	14	-	(348,807)
Loss on sale of inventory, servicing equipment and property, plant and equipment to vendors and third party buyers	12,14,15	149,371	101,568
Noncash transaction costs	15	96,237	-
Noncash finance lease income	11	(366,828)	18,257
Incentive compensation expense	22	314,331	463,983
Common shares, warrants and debentures issued for services	16,17,18	171,000	803,997
Finance and accretion expense	17	241,463	1,518,850
Listing expense	6	-	363,095
Change in fair value of embedded derivative liabilities	17	-	(889,229)
Unrealized loss in fair value change of investments	8	2,218,744	-
Purchases of equipment for finance leases	12	(2,824,431)	-
Proceeds from finance lease receivables	11	2,800,803	37,500
		(1,436,028)	(2,585,304)
Change in working capital items:			
Trade and other receivables	10	49,769	(35,926)
Inventories	12	-	979
Prepaid and other current assets	13	98,834	102,186
Trade and other payables	19	(55,656)	(96,805)
Accrued expenses	20	(121,620)	506,326
Unearned revenue	7	(654,589)	(11,397)
Aamounts due to related parties	23	38,067	547,258
Net cash flows used in operating activities		(2,081,223)	(1,572,683)
Cash flows from investing activities			
Proceeds from the sale of servicing equipment and property, plant and equipment	14,15	522,205	313,380
Purchases of servicing equipment	14	(246,542)	(46,915)
Purchases of property, plant and equipment	15	(5,327)	(1,113)
Cash acquired as part of reverse acquisition	6	-	698,858
Net cash flows provided by investing activities		270,336	964,210
Cash flows from financing activities			
Proceeds from loans and borrowings	17	55,762	1,100,000
Proceeds from issuance of Sub Receipt debentures	16	-	4,472,085
Repayment of debt	17	-	(49,664)
Payment of debt issuance and deferred financing costs	17	-	(477,007)
Net cash flows provided by financing activities		55,762	5,045,414
Effect of exchange rate changes on cash		(15,156)	(27,938)
Net decrease in cash		(1,770,281)	4,409,003
Cash at beginning of the the period		2,487,293	534,148
Cash at end of the period		$ 717,012	$ 4,943,151

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

XS Financial Inc.
Condensed consolidated statements of cash flows
For the nine months ended September 30, 2020 and 2019
(Unaudited)
(Expressed in United States dollars)

Supplemental disclosure of cash flow information:			
Cash paid for interest		$ 361,920	$ 521
Non-cash investing and financing activities			
Purchases of servicing equipment included in trade payables, accrued expenses and amounts due to related parties	19,23	$ 1,390,314	$ 381,913
Issuance of proportionate common shares	16	3,061,815	-
Issuance of common shares to a third party service provider	16	19,047	-
Discount on loan borrowings proceeds	17	-	228,183
Issuance of convertible debt, net of discount of $163,563	17	-	55,306
Prepaid debt issuance costs - warrants issued and common stock issued	16,17,18	-	505,764
Issuance of warrants to service providers, consultants and and Series C debenture holders	18	-	1,199,873
Issuance of embedded derivative liabilities	17	-	135,180
Conversion of Series B and Series C convertible debt to common stock	16	-	5,599,939
Conversion of Sub Receipt convertible debt to common stock	16,17	18,332	154,057
Servicing equipment sold and reduction to deferred revenue	7	-	1,006,542

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

(1) Nature of operations and background information

XS Financial Inc. ("XSF", or "the Company"), which changed its name from Xtraction Services Holdings Corp. on June 26, 2020 and formerly known as Caracara Silver Inc. ("Caracara") was incorporated under the laws of the Province of British Columbia on December 3, 2009, and is listed on the Canadian Securities Exchange ("CSE") under the symbol "XSF".

XSF, inclusive of it's wholly-owned subsidiary Xtraction Services, Inc ("XSI"), is a specialty finance company that provides equipment leasing solutions in the United States to owner/operators of cannabis and hemp companies including cultivators, oil processors, manufacturers, testing laboratories, among others and operates in one business segment in one geographic area. Its registered office is located at 1901 Avenue of The Stars, Suite 120, Los Angeles, California 90067, USA.

Xtraction Services, Inc. ("XSI") was originally established as a Delaware limited liability company on October 9, 2017. In July 2018, XSI filed with the Secretary of State of Delaware to change its corporate status from a Delaware limited liability company to a Delaware corporation and elected to be classified as a corporation. On July 19, 2018, XSI received a Certificate of Conversion and Certificate of Incorporation from the Secretary of State of Delaware.

On March 22, 2019, XSI entered into a definitive merger agreement with Caracara pursuant to which Caracara would acquire all of the issued and outstanding common shares of XSI. The transaction was structured as a “reverse triangular merger” between XSI, Caracara and a wholly-owned subsidiary of Caracara incorporated under the laws of Delaware. On September 11, 2019, the merger became effective whereby Caracara's subsidiary acquired all of the issued and outstanding Class A and Class B common shares, stock options and warrants of XSI and the resulting issuer changed its name from Caracara Silver Inc. to Xtraction Services Holdings Corp. and continued with the business of XSI.

The accompanying condensed consolidated financial statements have been approved by the Company’s board of directors and are authorized for issuance as of November 25, 2020.

(2) Basis of presentation

Statement of compliance

These condensed consolidated financial statements have been prepared in accordance with International Financial Reporting Standards and International Accounting Standards and Interpretations (collectively IFRSs) as issued by the International Accounting Standards Board (IASB).

Basis of consolidation

Subsidiaries are entities over which the Company has control, where control is defined to exist when the Company is exposed to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee. Subsidiaries are consolidated from the date control is transferred to the Company, and are de-consolidated from the date control ceases.

The condensed consolidated financial statements incorporate the financial statements of the Company and its wholly owned subsidiaries, Xtraction Services, Inc. incorporated in Delaware, United States, and CSI Princesa Inc. incorporated in Ontario, Canada. The results of subsidiaries acquired or disposed of during the year are included in the condensed consolidated financial statements of loss and comprehensive loss from the effective date of acquisition up to the effective date of disposal, as appropriate.

All intercompany transactions, balances, income and expenses are eliminated upon consolidation.

Functional and presentation currency

The condensed consolidated financial statements of the Company are presented in U.S. dollars (USD). The functional currency of the Company and CSI Princesa Inc., its Canadian subsidiary, is the Canadian dollar. The functional currency of Xtraction Services, Inc. is the U.S. dollar.

With the closing of the reverse acquisition on September 11, 2019, (note 6) the underlying functional currency of the Company changed resulting in changes to previously reported results in the three and nine months ended September 30, 2019.

Basis of measurement

The condensed consolidated financial statements have been prepared on a historical cost basis, except for certain financial instruments measured at fair value through profit and loss. Historical cost is generally based on the fair value of the consideration given in exchange for goods and services. In addition, these consolidated financial statements have been prepared using the accrual basis of accounting except for cash flow information.

Use of estimates and judgement

The preparation of financial statements in compliance with adopted IFRS requires the use of certain critical accounting estimates. It also requires the management of the Company to exercise judgment in applying the Company's accounting policies. The areas where significant judgments and estimates have been made in preparing the condensed consolidated financial statements and their effect are disclosed in note 5 below.

(3) Going concern

The condensed consolidated financial statements have been prepared on a going concern basis, which assumes that the Company will be able to realize its assets and discharge its liabilities in the normal course of business for the foreseeable future. The Company has incurred losses and negative cash flows from operations since inception and has an accumulated deficit of $17,913,334 and $13,586,621 as of September 30, 2020 and December 31, 2019, respectively. The Company's ability to continue as a going concern is dependent upon achieving a profitable level of operations and obtaining additional financing, neither of which is assured. The Company anticipates incurring additional losses until such time that it can generate sufficient revenue from its operations to cover its expenses. Historically, the Company has been successful in obtaining enough funding for operating and capital requirements. The condensed consolidated financial statements do not give effect to any adjustments which may be necessary should the Company be unable to continue as a going concern and be required to realize its assets and discharge its liabilities in other than the normal course of business and at amounts different from those reflected in the accompanying condensed consolidated financial statements. These adjustments could be material.

(Expressed in United States Dollars)

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

In March 2020, the World Health Organization declared the outbreak of a novel coronavirus (COVID-19) as a pandemic, which continues to spread throughout Canada and the United States. The spread of COVID-19 has caused significant volatility in Canadian, U.S. and international markets. There is significant uncertainty around the breadth and duration of business disruptions related to COVID-19, as well as its impact on the Canadian, U.S. and international economies and, although the Company has not experienced any material impact on its operations to date, the Company is unable to determine if it will have a future material impact to its operations or ability to raise funds.

(4) Significant accounting policies

The Company has applied the same accounting policies and methods of computation in its interim condensed consolidated financial statements as in its 2019 and 2018 annual financial statements except for adoption of *IAS 1 – Presentation of Financial Statements* and *IAS 8 – Accounting Policies, Changes in Accounting Estimates* and Errors and *IFRS 3 Business Combinations* on January 1, 2020.

<u>Fair value of financial instruments</u>

As at September 30, 2020, the Company had the following financial instruments measured at fair value:

	Fair Value Measurement at Reporting Date Using			
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total
As of September 30, 2020:				
Assets:				
Investments (note 9)	843,071	$ -	$ -	$ 843,071

As at December 31, 2019, the Company did not have any financial instruments measured at fair value.

Transfers between levels are considered to occur on the date that the fair valuation methodology changes. There were no transfers between levels during the current or comparative periods. There were no liabilities at fair value as at September 30, 2020 and December 31, 2019.

New standards and interpretations recently adopted

Effective January 1, 2020 the Company has adopted *IAS 1 – Presentation of Financial Statements ("IAS 1") and IAS 8 – Accounting Policies, Changes in Accounting Estimates and Errors ("IAS 8")*, which were amended in October 2018 to refine the definition of materiality and clarify its characteristics. The revised definition focuses on the idea that information is material if omitting, misstating or obscuring it could reasonably be expected to influence decisions that the primary users of general purpose financial statements make on the basis of those financial statements. The Company has concluded there was no impact on its financial statements and related disclosures upon the adoption of the amended standards for *IAS 1* and *IAS 8*.

Effective January 1, 2020 the Company has adopted *IFRS 3 – Business Combinations ("IFRS 3")*, which was amended in October 2018 to clarify the definition of a business. This amended definition states that a business must include inputs and a process and clarified that the process must be substantive and the inputs and process must together significantly contribute to operating outputs. In addition it narrows the definitions of a business by focusing the definition of outputs on goods and services provided to customers and other income from ordinary activities, rather than on providing dividends or other economic benefits directly to investors or lowering costs and added a test that makes it easier to conclude that a company has acquired a group of assets, rather than a business, if the value of the assets acquired is substantially all concentrated in a single asset or group of similar assets. The Company has concluded there was no impact on its financial statements and related disclosures upon the adoption of the amended standard for *IFRS 3*.

The Company had no additional new standards adopted that resulted in changes to the Company's accounting policies for the nine months ended September 30, 2020.

(5) Critical accounting estimates and judgements

In the application of the Company's accounting policies, which are described in note 4 above, the Company's management are required to make judgments, estimates and assumptions about the carrying amounts of assets and liabilities that are not readily apparent from other sources. The estimates and associated assumptions are based on historical experience and other factors that are considered to be relevant. Actual results may differ from these assumptions.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimate is revised if the revision affects only that period, or in the period of the revision and future periods if the revision affects both current and future periods. Significant judgments, estimates and assumptions that have the most significant effect on the amounts recognized in the condensed consolidated financial statements are described below.

Depreciation and Amortization of Servicing Equipment, Property, Plant and Equipment, and Intangible Assets and Estimate of Useful Lives

Depreciation and amortization of servicing equipment, property, plant and equipment and intangible asset is dependent upon estimates of useful lives. The Company estimates the useful lives of these assets based on the period over which the assets are expected to be available for use. The estimated useful lives are reviewed periodically and are updated if expectations differ from previous estimates due to physical wear and tear, technical or commercial obsolescence and legal or other limits on the use of the relevant assets.

Long-Lived Assets and Impairment

Long-lived assets, such as servicing equipment, property, plant and equipment and finite intangible assets, are reviewed for impairment whenever events or changes in circumstances indicate the carrying amount of an asset may not be recoverable. If circumstances require a long-lived asset or asset group be tested for possible impairment, the Company estimates its recoverable amount. An impairment loss is recognized to the extent the carrying value exceeds its recoverable amount. Fair value is determined using various valuation techniques, including discounted cash flow models, quoted market values, and third-party independent appraisals, as considered necessary.

Share-based Incentive Compensation

The Company uses the Black-Scholes option pricing model to determine the fair value of share-based awards granted. In estimating fair value, management is required to make certain assumptions and estimates such as the expected term, volatility of the Company’s future share price, risk free interest rates, future dividend yields and estimated forfeitures at the initial grant date. Changes in assumptions used to estimate fair value could result in materially different results.

Derivative Liabilities

Derivative liabilities are initially recognized at fair value on the date entered into and are subsequently remeasured to their fair value at the end of each reporting period. Changes in the fair value of any derivative instrument are recognized immediately as a component of other expense (income) in the consolidated statements of loss and comprehensive loss. The fair value of the derivative liabilities are subject to measurement uncertainty due to the assumptions made for the inputs in the Black-Scholes option valuation. See note 17.

Compound Financial Instruments

The initial recognition of the compound financial instruments requires that the liability component and the conversion feature are recognized separately. Judgement is required to determine whether the conversion feature meets the definition of equity or a derivative liability. The fair values at initial recognition is subject to measurement uncertainty. See note 17.

Functional Currency Determination

The functional currency for the Company and its subsidiaries is the currency of the primary economic environment in which the entity operates.

Determination of functional currency is conducted through an analysis of the consideration factors identified in IAS 21. The Effects of Changes in Foreign Exchange Rates and may involve certain judgments to determine the primary economic environment. The Company reconsiders the functional currency of its entities if there is a change in events and conditions which determine the primary economic environment. Significant changes to those underlying factors could cause a change to the functional currency.

Determination of Discount Rates

Determination of the discount rate for term loans and convertible debentures is based on comparison to similar interest bearing debt instruments of a group of comparative companies.

Determination of Financing Lease or Operating Lease

In making the determination of whether an arrangement should be accounted for as a financing lease or an operating lease, the Company makes certain assumptions including the fair value of the equipment under lease, the interest implicit in the lease and the residual value of the equipment at the end of the lease.

Expected Credit Losses

See notes 10 and 11.

Definition of a Business

Determination of whether a set of assets acquired, and liabilities assumed constitute a business under IFRS 3 requires the Company to make certain judgments, taking into account all facts and circumstances. See note 6.

Contingencies

See note 23.

(Expressed in United States Dollars)

(6) Reverse acquisition

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

Cash	$	698,858
Other receivable		6,048
Accounts payable and accrued expenses		(114,834)
Net assets acquired		590,072
Purchase price paid:		
3,896,958 common shares	$	953,167
Excess of purchase price paid over net assets acquired allocated to listing expense	$	363,095

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

On September 11, 2019, the merger became effective via a "reverse triangular merger", pursuant to which Caracara acquired all of the issued and outstanding class A and class B common shares, stock options and warrants of XSI by way of a merger between XSI and Caracara's wholly-owned subsidiary. As a result of the transaction, the former shareholders of XSI held greater than 50% of the issued and outstanding shares of the resulting issuer. The substance of the transaction is a reverse acquisition of a non-operating company, as Caracara did not meet the definition of a business under IFRS 3. As a result, the transactions has been accounted for as a capital transaction with XSI being identified as the accounting acquirer and the equity consideration being measured at fair value under IFRS 2, using the acquisition method of accounting. The resulting issuer changed its name from Caracara to Xtraction Services Holdings Corp. and continued with the business of XSI.

The issued and outstanding common shares of Caracara were consolidated on the basis of 1 post-consolidation Caracara common share for every 6.262 outstanding Caracara common shares existing immediately before the consolidation. The fair value of the acquisition of 3,896,958 post-consolidation shares of Caracara at a fair value per share of $0.24, based on the quoted price of the shares on the date of the transaction, was $953,167. The purchase price allocation of the merger includes net assets acquired of $590,072, resulting in a listing expense of $363,095 reflected in the condensed consolidated statements of (loss) income and comprehensive (loss) income for the three and nine month ended September 30, 2019.

(Expressed in United States Dollars)

(7) Revenue

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

	Three months ended September 30,		Nine months ended September 30,	
	2020	2019	2020	2019
Revenue source:				
Financing leases (note 11)	$ 3,447,289	$ 385,573	$ 4,754,234	$ 406,945
Equipment sales	388,535	165,931	521,935	1,015,529
Royalty sales	-	72,247	-	173,302
Operating leases	-	39,122	143,250	39,122
Other revenue	22,505	595	32,070	595
	$ 3,858,329	$ 663,468	$ 5,451,489	$ 1,635,493
Timing of revenue recognition under IFRS 15 from contracts with customers:				
Products and services transferred at a point in time	$ 388,535	$ 165,931	$ 521,935	$ 1,015,529
Services transferred over time	$ 3,469,794	$ 497,537	$ 4,929,554	$ 619,964

At September 30, 2020 the Company had unsatisfied performance obligations of $17,000, related to proposal fees received for financing lease transactions under evaluation, which is reflected as unearned revenue in the condensed consolidated statements of financial position.

The Company's largest revenue transaction in the three and nine months ended September 30, 2019 resulted from the sale of equipment to a single customer that was fully paid in October 2018 with delivery and installation completed in November 2019.

The Company had $nil and $426,316 of servicing equipment (note 14) subject to revenue generated from operating lease arrangements as of September 30, 2020 and December 31, 2019, respectively.

Revenue concentration

All of the Company's revenue is derived from customers in the United States with one customer representing 67% and 66% of the Company's recognized revenue in the three and nine months ended September 30, 2020, respectively, and another two customers representing 64% and 24% of the Company's recognized revenue in the three months ended September 30, 2019 and 62% and 27% of the Company's recognized revenue in the nine months ended September 30, 2019.

(Expressed in United States Dollars)

(8) Expenses by nature

The following tables presents an analysis of expense by nature:

	Three months ended September 30,		Nine months ended September 30,	
	2020	**2019**	**2020**	**2019**
Cost of sales:				
Compensation and benefits	$ 36,801	$ 64,894	$ 126,286	$ 210,822
Depreciation expense	18,988	87,241	89,995	303,820
Amortization of intangible	-	38,291	-	114,874
Equipment inventory purchases	-	67,209	-	684,128
Equipment inventory costs	3,246,060	432,401	4,396,269	432,401
Supplies and materials	-	24,050	551	81,622
Maintenance and repair costs	-	4,500	-	25,836
Other expenses	480,427	45	684,564	50,239
	$ 3,782,276	$ 718,631	$ 5,297,665	$ 1,903,742
Administrative expenses:				
Compensation and benefits	$ -	$ 8,870	$ 2,351	$ 53,256
Incentive compensation	28,829	64,553	314,331	463,983
Contractors and outside services	51,171	91,151	113,158	229,553
Management fee	-	86,000	146,200	260,400
Professional fees	160,272	234,185	440,817	1,651,695
Office rent, utilities and expenses	(1,857)	9,068	23,834	46,057
Travel, meals and entertainment	1,120	3,172	9,616	30,998
Insurance	45,131	(120,647)	152,451	-
Other expenses	15,969	166,768	111,089	192,889
	300,635	$ 543,120	1,313,847	$ 2,928,831
Sales and marketing expenses:				
Compensation and benefits	$ 647	$ 47,122	$ 50,392	$ 67,287
Contractors and outside services	-	-	10,000	-
Commissions	13,535	-	126,295	-
Professional fees	43,209	3,250	71,076	49,083
Advertising and marketing	5,591	31,704	79,093	42,857
Trade shows	-	-	-	7,209
Other expenses	417	313	1,966	1,600
	$ 63,399	$ 82,389	$ 338,822	$ 168,036

(Expressed in United States Dollars)

(9) Investments

In January 2020, the Company entered into a strategic partnership and cooperation agreement with KushCo Holdings Co. Inc. ("KushCo") whereby the Company issued 10,600.3 proportionate voting shares at a share price of $0.38CAD ($0.29) (note 16) for total consideration of $3,061,815 in exchange for 1,653,081 shares of KushCo valued at an amount equal to the consideration given up by the Company.

The Company recorded the shares received from KushCo as investments on the condensed consolidated statement of financial position. Investments are classified at fair value through profit or loss (FVPL). At September 30, 2020, the investment in KushCo was re-valued at $843,071, with the change in fair value of $320,698 and $2,218,744 reflected at FVPL in the condensed consolidated statements of comprehensive loss for the three and nine months ended September 30, 2020, respectively.

(10) Trade receivables

The carrying value of trade receivables as of September 30, 2020 and December 31, 2019 was $195,463 and $124,715, respectively.

Trade receivables are measured at amortized cost net of allowance for uncollectible amounts. The Company determines its expected credit loss based on a number of factors, including length of time an account is past due, the customer's previous loss history, and the ability of the customer to pay its obligation to the Company. The Company writes off receivables when they become uncollectible. Allowance for uncollectible accounts is included in general and administration expenses within the condensed consolidated statements of (loss) income and comprehensive (loss) income.

The following table presents the movement in the allowance on trade receivables from January 1, 2020 through September 30, 2020:

Balance at January 1, 2020	$	-
Bad debt provision		40,000
Receivables written-off as uncollectible		(40,000)
Balance at September 30, 2020	$	-

(Expressed in United States Dollars)

(11) Financing receivables

The following table presents financing receivables:

	September 30, 2020	December 31, 2019
Financing receivables, short-term	$ 765,955	$ 480,466
Financing receivables, long-term	2,512,124	310,798
	$ 3,278,079	$ 791,264

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

The following table presents a maturity analysis of lease receivables, including the undiscounted lease payments to be received as at September 30, 2020:

2020	$ 369,149
2021	1,291,080
2022	1,239,099
2023	1,021,096
2024	666,846
Total undiscounted lease payments receivable	4,587,270
Unearned finance income	(1,309,192)
Net investment in lease	$ 3,278,079

Allowance for credit losses

The Company measures loss allowances based on an expected credit loss ("ECL") impairment model for all financial instruments except those measured at fair value through profit and loss. Application of the model depends on the following credit stages of the financial assets:

(i) Stage 1 - for new leases recognized and for existing leases that have not experienced a significant increase in credit risk since initial recognition, a loss allowance is recognized equal to the credit losses expected to result from defaults occurring in the next 12 months;
(ii) Stage 2 - for those leases that have experienced a significant increase in credit risk since initial recognition, a loss allowance is recognized equal to the credit losses expected over the remaining life of the lease; and
(iii) Stage 3 - for leases that are considered to be credit-impaired, a loss allowance equal to full life time ECLs is recognized.

Thus, the evaluation of the allowance for credit losses is performed on a lease by lease basis. Definitions of default have been selected to eliminate the judgement that may otherwise be necessary, given the diversity within the finance receivable portfolio, the lack of individual drivers of changes in credit risk across assets and over time, and the resulting inability to assess which specific assets will be rectified. For the purposes of measuring ECL, a default is defined as leases and loans that have missed one payment and are not subsequently rectified within 30 days.

(Expressed in United States Dollars)

The Company is entitled to repossess financed equipment if the borrower defaults on their lease obligations. Any amounts recovered from the sale of repossessed equipment are credited to the allowance for credit losses when received.

The process of estimating ECLs uses the following inputs and assumptions to reflect information about past events, current conditions and forecasts of future conditions that are not already captured in the inputs:

- Security deposits held;
- Recoveries of amounts previously written off in the last 12 months, as an estimate of recoveries for the next 12 months;
- An estimate of the effects of natural disasters and economic shocks that have occurred on credit losses in the next 12 months;
- The stage of the business cycle for the industry, which considers: the competitive environment, GDP growth, prevailing interest rates and expectations of future rates, fiscal policy and inflation rates; and
- Current delinquency trends of non-accrual and greater than 30 days delinquency rates.

Determining the inputs listed and ECLs requires significant estimation uncertainty. The estimation and application of forward-looking information requires significant judgement.

As of September 30, 2020, there are no finance receivables past due or impaired and all leases are considered to be Stage 1.

(12) Inventories

Inventories primarily consist of equipment and spare parts that the Company intends to either sell to customers as part of the installation of servicing equipment for customers or for repair orders.

The carrying value of spare parts inventory as of September 30, 2020 and December 31, 2019 was $nil and $36,052, respectively. The spare parts inventory is being carried at cost, as it is the lower of cost or net realizable value.

The following table presents a continuity of inventory from January 1, 2020 through September 30, 2020:

Balance at January 1, 2020	$ 36,052
Purchases of servicing equipment for finance leases	4,361,305
Cost of goods sold - finance leases	(4,361,305)
Sale of spare parts inventory	(36,052)
Balance at September 30, 2020	$ -

(Expressed in United States Dollars)

In the third quarter of 2020, the Company sold spare parts inventory to a third party buyer resulting in the Company receiving gross proceeds of $3,000 with a recognized loss of $33,052 included in cost of sales within the consolidated statements of (loss) income and comprehensive (loss) income for the three and nine months ended September 30, 2020.

(13) Prepaid and other current assets

The following table presents prepaid and other current assets:

	September 30, 2020	December 31, 2019
Prepaid insurance	$ 44,275	$ 197,313
Prepaid consulting services	-	6,250
Other	101,472	41,018
	$ 145,747	$ 244,581

(14) Servicing equipment

The following table below presents the change in carrying value of the Company's servicing equipment from January 1, 2020 through September 30, 2020:

	Extraction and ancillary extraction equipment	Pre-Processing equipment	Post-Processing equipment	Anlytical and other equipment	Total
Cost:					
Balance at January 1, 2020	$ 638,637	$ 14,453	$ 239,246	$ 39,381	$ 931,717
Additions	-	-	246,542	-	246,542
Equipment sales	(285,079)	(12,203)	(383,631)	(39,381)	(720,294)
Finance lease sales (note 10)	-	-	(8,195)	-	(8,195)
Balance at September 30, 2020	$ 353,558	$ 2,250	$ 93,962	$ 0	$ 449,770
Accumulated Depreciation:					
Balance at January 1, 2020	$ (108,282)	$ (1,754)	$ (30,602)	$ (7,884)	$ (148,522)
Depreciation	(37,949)	(1,431)	(40,914)	(6,364)	(86,658)
Equipment sales	32,588	2,547	35,389	14,248	84,772
Finance lease sales (note 10)	-	-	1,502	-	1,502
Balance at September 30, 2020	$ (113,643)	$ (638)	$ (34,625)	$ -	$ (148,906)
Net book value:					
Balance at December 31, 2019	$ 530,355	$ 12,699	$ 208,644	$ 31,497	$ 783,195
Balance at September 30, 2020	239,915	1,612	59,337	0	300,864

All of the servicing equipment is located in the United States.

Equipment sales

In January 2020, the Company sold extraction and ancillary extraction equipment back to the original supplier of the equipment, Khrysos Global Inc. ("Khrysos"), and throughout the second and third quarter of 2020, the Company sold other servicing equipment to third party buyers. The total of these transactions resulted in the Company receiving gross proceeds of $519,205 with recognized losses of $84,517 and $116,319 included in cost of sales within the consolidated statements of (loss) income and comprehensive (loss) income for three and nine months ended September 30, 2020, respectively.

In February 2020, the Company received a refund on sales taxes on previously purchased servicing equipment resulting in a net gain of $(10,999), included in other (income) expense in the condensed consolidated statements of (loss) income and comprehensive (loss) income for the nine months ended September 30, 2020.

Customer equipment sale

Throughout 2019, the Company delivered servicing equipment associated with a customer equipment sale (note 7). During the nine months ended September 30, 2019 the Company sold equipment with a net book value of $657,735 of which $97,597 was servicing equipment and $560,138 was transferred from prepaid servicing equipment. The Company recorded the proceeds in revenues and recognized a gross margin on the sale of the servicing equipment of $102,104 and $351,558 in the condensed consolidated statements of (loss) income and comprehensive (loss) income for the three and nine months ended September 30, 2019, respectively.

Finance lease sales

The Company is a lessor for lease arrangements considered to be finance leases (note 11). As a result of substantially all of the risks and rewards of ownership of the servicing equipment transferring to the lessee, the Company transfers the net book value of the servicing equipment to inventories.

Prepaid servicing equipment

Prepaid servicing equipment represents servicing equipment purchased but not yet installed or delivered at a customer site, and servicing equipment that has yet to be allocated to a specific customer site. The carrying value of prepaid service equipment at September 30, 2020 and December 31, 2019 was $Nil. This reflects the Company's recent leasing protocols which require a signed lease agreement in order to initiate a new equipment purchase. All equipment purchases are delivered directly to customer sites.

Depreciation expense related to servicing equipment is included in cost of sales within the condensed consolidated statements of (loss) income and comprehensive (loss) income.

(Expressed in United States Dollars)

(15) Property, plant and equipment

The following table below presents the change in carrying value of the Company's property plant and equipment from January 1, 2020 through September 30, 2020:

		Computers		Machinery and equipment		Total
Cost:						
Balance at January 1, 2020	$	8,294	$	3,490	$	11,784
Additions		5,327		-		5,327
Balance at September 30, 2020	$	13,621	$	3,490	$	17,111
Accumulated Depreciation:						
Balance at January 1, 2020	$	(3,289)	$	(989)	$	(4,278)
Depreciation		(2,813)		(524)		(3,337)
Balance at September 30, 2020	$	(6,102)	$	(1,513)	$	(7,615)
Net book value:						
Balance at December 31, 2019	$	5,005	$	2,501	$	7,506
Balance at September 30, 2020		7,519		1,977		9,496

All of the property, plant and equipment is located in the United States.

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

(16) Share capital

As at September 30, 2020 and December 31, 2019, the Company has an unlimited number of authorized common and proportionate voting shares with no par value. Proportionate voting shares can be converted into common shares at the option of the holders at a ratio of 1,000 to 1 upon approval of the Company's Resulting Issuer Board and satisfaction of the condition that greater than 40% of common and proportionate shareholders are US residents. On all voting matters, common shareholders are entitled to one vote and proportionate voting shareholders are entitled to 1,000 votes per proportionate voting share. Generally, in all other matters the proportionate voting shareholders have the same rights as the common shareholders and will be treated as if they were one class of shares. At September 30, 2020 and December 31, 2019, the Company had 31,554,663 and 29,986,764 issued and outstanding common shares and 23,107 and 12,207 issued and outstanding proportionate voting shares, respectively.

Share and member unit issuances

In January 2020, the Company issued 10,600.3 proportionate voting shares at a share price of $0.38CAD ($0.29) to KushCo for total consideration of $3,061,815 in exchange for 1,653,081 shares of KushCo valued at an amount equal to the consideration given up by the Company (note 9). On completion of the share swap, KushCo became a 19.9% shareholder of the Company.

(Expressed in United States Dollars)

In January and March 2020, the Company issued 22,727 and 25,454 shares of common shares, respectively, on the conversion of Sub Receipt debentures (note 17). Total shareholders' equity increased $18,332 as a result of this conversion.

In May 2020, the Company issued a combined 950,000 common shares at a share prices ranging between $0.26CAD ($0.18) and $0.30CAD ($0.18) to two separate service providers as consideration for a finder's fee earned on a new customer lease transaction and marketing services provided. The Company recorded $171,000 as sales and marketing expense within the condensed consolidated statements of (loss) income and comprehensive (loss) income for the nine months ended September 30, 2020.

In July 2020, the Company issued 450,761 common shares at a share price of $0.29CAD ($0.21) as consideration for the purchase of a California lenders license from CA Licensed Lenders LLC. The Company recorded $96,237 as professional fee transaction expense within the condensed consolidated statements of (loss) income and comprehensive (loss) income for the three and nine months ended September 30, 2020. Additionally, in July 2020, the Company issued 119,047 common shares at a share price of $0.21CAD ($0.16) to a third party service provider for settlement of an obligation for services provided. The Company recorded $19,047 against accounts payable within the condensed consolidated statements of financial position.

(17) Loans and borrowings

The following table presents loans and borrowings outstanding:

Description	Maturity date	Interest rate	September 30, 2020	December 31, 2019
Term loans:				
Archytas	November 7, 2020	12% - 18% (1)	$ 600,000	$ 600,000
Customers Bank	April 29, 2022	1.0%	55,762	-
Convertible debentures	March 22, 2024	10.0%	218,869	218,869
Sub Receipt convertible debentures	September 11, 2024	10.0%	4,107,816	4,126,148
			4,982,447	4,945,017
Less:				
Unamortized discounts, debt issuance costs and prepaid offering costs (2)			(2,125,011)	(2,366,473)
			$ 2,857,436	$ 2,578,544
Non-current			$ 2,257,436	$ 1,978,544
Current			$ 600,000	$ 600,000

Notes to the table:

(1) In May 2020, the Company amended the term loan agreement to lower the per annum interest rate from 18% to 12% starting on May 1, 2020 through maturity.

(2) The carrying value of the $600,000 term loan was adjusted using a discount rate of 50% to reflect the prevailing borrowing rates associated with debt acquired by companies with a similar credit risk profile

(Expressed in United States Dollars)

as the Company. The carrying value of the convertible debentures and Sub Receipt convertible debentures issued in 2019 were adjusted using a discount rate of 25% to reflect the prevailing borrowing rates associated with debt acquired by companies with a similar credit risk profile as the Company. The debt discount is accreted over the life of the respective debt instruments using the effective interest method.

The following table below shows the change in carrying value of the Company's loans and borrowings from January 1, 2020 through September 30, 2020:

	Term Loans	Convertible debentures	Debt discounts and and prepaid costs	Total
Balance at January 1, 2020	$ 600,000	$ 4,345,017	$ (2,366,473) [1]	$ 2,578,544
Borrowings	55,762	-	-	55,762
Conversion of Sub Receipt convertible debenture	-	(18,332)	-	(18,332)
Amortization and accretion of debt discounts and debt issuance costs	-	-	241,462	241,462
Balance at September 30, 2020	$ 655,762	$ 4,326,685	$ (2,125,011)	$ 2,857,436

Notes to the table:

(1) Represents debt discounts for the discount on loan borrowing proceeds and convertible debt issuances, and debt issuance costs netted against the gross proceeds of the Sub Receipt debenture issuance**.**

Term loans

The $600,000 term loan is due on or before the maturity date of November 2020 and bears interest at a rate of 12% per annum, payable monthly. Prior to May 2020 the term loan bore an interest rate of 18% per annum. The Company incurred interest expense of $18,000 and $66,000 in the three and nine months ended September 30, 2020, respectively, and $27,000 and $81,000 in the three and nine months ended September 30, 2019, respectively, related to this loan.

In January, February March and April 2019, the Company received additional funding of $1,100,000 in the form of term loans ("2019 term loans") from Archytas with maturity dates ranging from September 2019 to February 2020. The 2019 term loans bore interest at a rate of 18% per annum, payable monthly. In November 2019, the Company repaid Archytas the 2019 term loans in full. The Company incurred interest expense of $49,500 and $126,244 in the three and nine months ended September 30, 2019, respectively, in relation to these term loans.

In April 2020, the Company entered into a promissory note with a third-party lender to borrow $55,762 under the U.S. government's Paycheck Protection Program ("PPP") via the Coronavirus Aid, Relief, and Economic Security ("CARES") Act. Under the provisions of the PPP, loan proceeds are expected to be used for payroll costs, rent and utilities. The promissory note is unsecured, with a maturity date of April 29, 2022, accrues interest at 1.00% and requires eighteen fixed scheduled monthly amortization payments commencing in November 2020. PPP borrowers may apply for loan forgiveness in an amount equal to the sum of payroll costs, rent and utilities incurred during the 24 week period following the receipt of loan proceeds, whereby not more 40% of the amount forgiven can be attributable to non-payroll costs.

Convertible debentures

In March and April 2019, the Company issued $294,000CAD ($218,869) of convertible debentures to investment advisors and brokers for services rendered in raising debt subscriptions. The convertible debentures mature after 5 years and bear interest at a rate of 10% per annum payable in cash in equal quarterly installments. The convertible debentures convert into common shares and warrants at a conversion price of $1.10CAD ($0.82) at the holders' option prior to maturity or upon a change of control. The warrants to be received have an exercise price of a $1.50CAD ($1.12) and have a five-year term. Upon a change in control, the Company is required to purchase the convertible debentures at a price of 105% of the principal balance plus accrued, unpaid interest. The Company has accounted for the fair value of the convertible debt at issuance of $218,869 as debt issuance costs, within the condensed consolidated statements of financial position and is being amortized to interest expense over the term of the Sub Receipt debentures under the effective interest rate method within the condensed consolidated statements of (loss) income and comprehensive (loss) income. The debt discount of $160,499 is being amortized to interest expense over the term of the convertible debentures under the effective interest rate method within the condensed consolidated statements of (loss) income and comprehensive (loss) income. As of September 11, 2019, with the completion of the reverse acquisition, the debentures were re-issued through the legal parent entity and the underlying functional currency change triggered a reclassification of the debenture liability to equity. The fair value of the debenture liability as at September 11, 2019 immediately prior to the reclassification was $145,989.

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

The principal amount of the debenture was estimated at its fair value of $2,630,804 based on a discount rate of 25%. The Company incurred debt issuance costs, netted against the gross proceeds of the issuance, of $1,398,268CAD ($1,060,821) in connection with the issuance of the Sub Receipt debentures, of which $821,332CAD ($623,112) was allocated to the debenture liability. The debt issuance costs were recorded as a discount on the Sub Receipt debentures carrying value, and are being amortized to interest expense over the life of the sub receipts convertible debentures under the effective interest rate method. The residual value of the debenture of $1,841,281 was allocated to the conversion feature and recorded as a component of equity, net of issuance costs of $437,709 and deferred tax impact of $384,000.

In January and March 2020, investors exercised their conversion feature on $25,000CAD ($8,941) and $28,000CAD ($9,391) of the Sub Receipt debentures and received 22,727 and 25,454 common shares, respectively.

Embedded derivative liabilities

The conversion feature of the Series C debentures issued in September, October and December of 2018 and subsequently converted to equity upon the merger of XSI and Caracara was considered an embedded derivative liability as the conversion price was not fixed. The Company performed a Black-Scholes model while probability weighting various expected conversion prices, resulting in a fair value of $1,341,557 determined at issuance, and accounted for the embedded derivative liabilities as a long-term liability within the condensed consolidated statements of financial position. In March 2019, the Company amended the conversion feature of the Series C debentures pursuant to which each holder of such debentures will receive upon conversion at price of $0.94CAD, thereof one share of common shares and a warrant, which has a $1.50CAD ($1.12) exercise price and a five year term, upon conversion. On date of modification, the embedded derivative relating to the Series C debentures was revalued using Black-Scholes valuation model with the following assumptions: risk free rate – 1.77%, expected volatility – 90% and exercise price of $0.94CAD ($0.71).

The conversion feature of the $294,000CAD ($218,869) issued to investment advisors and brokers in March and April 2019 was considered an embedded derivative liability as the conversion price was denominated in a currency that was different from the functional currency at the time of issuance. On issuance date, the fair value of the embedded derivative liability was determined using the Black-Scholes option valuation model as $135,180 with the following assumptions: risk free rate – 1.48%, expected volatility – 90% and exercise price of $1.10CAD ($0.82). On September 11, 2019, with the completion of the reverse acquisition the debentures were transferred to the legal parent entity and the underlying functional currency change triggered a re-valuation of the embedded derivative liability. The fair value of the embedded derivative liability as at September 11, 2019 of $47,265 was reclassified as a component of equity. Prior to the re-valuation of the embedded derivative liability the Company had reflected changes in the fair market value of the embedded derivative liabilities of $87,915 in the condensed consolidated statements of (loss) income and comprehensive (loss) income for the nine months ended September 30, 2019.

In September 2019, the embedded derivative liabilities associated with the Series C conversion feature were reclassified to shareholders' equity within the consolidated statements of financial position in conjunction with the conversion of the Series C debentures. Prior to the Series C debenture conversion, the Company had reflected changes in the fair market value of the embedded derivative liabilities of $801,314 in the condensed consolidated statements of (loss) income and comprehensive (loss) income for the nine months ended September 30, 2019.

(Expressed in United States Dollars)

Redeemable common stock

In July 2018, Archytas and another member exercised the conversion feature of term loans held with the Company and received a combined 6,737,588 shares of Class A common shares. The Company classified $650,000 of the amount converted as redeemable common shares and a liability within the condensed consolidated statements of financial position as this represents amounts subject to rescission due to an ongoing governmental investigation of the Member's finances. An escrow balance of $650,000 was maintained by Archytas on behalf of the Company to satisfy the obligation. In third quarter of 2020, the terms of the escrow agreement were amended such that the escrowed funds would require the approval of the Company's audit committee to be transferred or utilized. As these funds are held in escrow for the Company and are now under the control and oversight of the Company's audit committee, the Company has reflected these funds as restricted cash on the condensed consolidated statements of financial position at September 30, 2020.

(18) Warrants

The following table summarizes warrant activity from January 1, 2020 through September 30, 2020:

	Number of warrants		Weighted average exercise price per share
Outstanding at January 1, 2020	8,466,908		$ 1.13
Granted	48,181	(1)	$ 1.10
Expired	(840,250)		$ 0.80
Outstanding at September 30, 2020	7,674,839		$ 1.05

Note to the table:

(1) All of the warrants granted in the nine months ended September 30, 2020 were accounted for as a component of shareholders' equity.

Warrant issuances

In January and March 2020, the Company issued 48,181 of warrants related to the conversion of Sub Receipt debentures (note 17). The warrants have a term of five years and exercise price of $1.50CAD ($1.13 - $1.14) per share. The warrants had a value of $18,332 on the date of issue based on the allocation of the total carrying value of the debenture liability and conversion feature using the Black-Scholes option pricing model.

The fair value of the warrants was determined using the Black-Scholes option pricing model with the following assumptions:

(Expressed in United States Dollars)

	2020 issuances
Expected dividend yield	-
Expected volatility	90.0%
Risk-free interest rate	0.8 - 1.6%
Expected term	4.5 - 4.7 years
Conversion price	$ 1.05 - 1.16

The following table presents warrants outstanding at September 30, 2020:

Expiration date	Term (years)	Number of warrants outstanding	Number of warrants exercisable	Exercise price US $	Exercise price CAD $
17-Oct-20	2	17,647	17,647	$ 0.85	$ 1.11
17-Oct-20	2	17,647	17,647	$ 0.85	$ 1.11
30-Oct-20	2	30,000	30,000	$ 0.85	$ 1.11
30-Oct-20	2	2,118	2,118	$ 0.85	$ 1.11
28-Nov-20	2	31,765	31,765	$ 0.85	$ 1.11
5-Dec-20	2	26,470	26,470	$ 0.85	$ 1.11
31-Dec-20	2	174,115	174,115	$ 0.85	$ 1.11
22-Mar-21	2	400,000	400,000	$ 0.82	$ 1.10
12-Apr-24	5	500,000	500,000	$ 0.82	$ 1.10
15-May-21	2	36,818	36,818	$ 0.82	$ 1.10
17-Jul-21	2	150,000	150,000	$ 0.84	$ 1.10
11-Sep-24	5	374,308	374,308	$ 0.82	$ 1.10
11-Sep-24	5	5,452,134	5,452,134	$ 1.12	$ 1.50
11-Sep-24	5	363,636	363,636	$ 1.13	$ 1.50
11-Sep-24	5	50,000	50,000	$ 1.14	$ 1.50
11-Sep-24	5	22,727	22,727	$ 1.16	$ 1.50
11-Sep-24	5	25,454	25,454	$ 1.05	$ 1.50
Total	2 - 5 years	7,674,839	7,674,839	$ 1.05	$ 1.41

The weighted average remaining time to expiry for the outstanding warrants is 3.52 years.

(19) Trade and other payables

The following table presents trade and other payables:

	September 30, 2020	December 31, 2019
Trade payables	$ 691,725	$ 119,452
Credit card payable	7,248	300
	$ 698,973	$ 119,752

(Expressed in United States Dollars)

(20) Other current liabilities

The following table presents accrued expenses:

	September 30, 2020	December 31, 2019
Accrued insurance	$ 20,176	$ 152,295
Accrued professional fees	-	30,756
Accrued compensation, commissions, benefits and related taxes	9,346	9,212
Accrued servicing equipment purchases	903,719	-
Accrued other	31,128	9,054
	$ 964,369	$ 201,317

(21) Income taxes

The Company recognized a deferred income tax provision of $Nil and $975 for the three and nine months ended September 30, 2020 and 2019, respectively.

Income tax expense is recognized based on management's estimate of the weighted average effective annual income tax rate expected for the full financial year. The estimated average annual tax rate was 26.5%, for the three and nine months ended September 30, 2020 and 2019.

(22) Share-based compensation

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

The following table summarizes stock option activity under the Option Plan from January 1, 2020 through September 30, 2020:

	Number of shares	Weighted average exercise price per share	Weighted average remaining contractual term (years)
Outstanding at January 1, 2020	3,010,129	$ 0.38	6.2
Granted	1,808,889	$ 0.16	
Cancelled / forfeited	(150,000)	$ 0.26	
Outstanding at September 30, 2020	4,669,018	$ 0.30	5.1
Exercisable and vested at September 30. 2020	3,478,489	$ 0.30	5.1

(Expressed in United States Dollars)

As of September 30, 2020 there was approximately $73,000 of unrecognized compensation expense related to unvested stock options, which is expected to be recognized over a weighted average period of 0.6 years.

The Company recorded compensation expense for stock options of $28,829 and $64,553 for the three months ended September 30, 2020 and 2019, respectively, and $314,331 and $463,983 for the nine months ended September 30, 2020 and 2019, respectively.

The following table summarizes the stock options outstanding as at September 30, 2020:

Expiry Date	Exercise Price US $	Exercise Price CAD $	Weighted Average Remaining Contractual Life (years)	Number of Options Outstanding	Number of Options Vested
July 2028	$ 0.60	$ 0.78	7.80	1,055,129	615,931
November 2024	$ 0.26	$ 0.34	4.15	1,805,000	1,053,669
April 2025	$ 0.16	$ 0.22	4.55	1,808,889	1,808,889
	$ 0.30	$ 0.39	5.10	4,669,018	3,478,489

(23) Related party transactions

The following presents balances and transactions between the Company and other related parties as of September 30, 2020 and December 31, 2019, and for the three and nine months ended September 30, 2020 and 2019, respectively.

Key management personnel

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

	Three months ended September 30,		Nine months ended September 30,	
	2020	2019	2020	2019
Salaries, contractor costs, management fees and benefits	$ 51,171	$ 138,435	$ 270,897	$ 378,199
Incentive compensation (non-cash)	18,889	9,751	56,897	324,969
	$ 70,060	$ 148,186	$ 327,794	$ 703,168

See also notes 16, 18 and 22.

Related party transactions and amounts due to related parties

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

(Expressed in United States Dollars)

	Archytas		Khrysos		Total	
Amounts due to related parties at January 1, 2019	$	13,000	$	105,654	$	118,654
Interest expense		218,957		-		218,957
Management fee		260,400		-		260,400
Operating expenses		-		86,614		86,614
Prepaid equipment purchases		-		286,083		286,083
Conversion of accrued interest to comon stock		(15,713)		-		(15,713)
Less payments to related parties		-		(3,000)		(3,000)
Amounts due to related parties at September 30, 2019		476,644	$	475,351	$	951,995
Amounts due to related parties at January 1, 2020	$	-	$	-	$	-
Interest expense		66,000		-		66,000
Management fee		146,200		-		146,200
Less payments to related parties		(174,133)		-		(174,133)
Amounts due to related parties at September 30, 2020		38,067	$	-	$	38,067

Effective January 2019, the Company entered into a management services agreement with Archytas at a monthly rate of $28,667 and a term of five years, with one year automatic renewals, whereby Archytas will provide day-to-day executive management and support to the Company. Archytas is a shareholder of the Company, having been involved in the initial formation of XSI. In May and June 2020, the Company lowered the monthly rate to $20,067 as part of a 30% cost reduction to the Company’s management team, employees and external consultants. In June 2020 the management services agreement was amended to reduce the monthly rate to $nil for July, August, and September 2020. In addition, two officers and directors of the Company are partners of Archytas. The agreement cannot be terminated until Archytas holds less than 5% of the fully diluted capital stock of the Company. As at September 30, 2020, Archytas held 19.8% of outstanding voting shares of the Company.

Related party loans and borrowings

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

	September 30, 2020		December 31, 2019	
Archytas:				
Term loan (note 17)	$	600,000	$	600,000
Accrued interest		18,000		-
	$	618,000	$	600,000

The carrying value of the above loans and borrowings were reduced by discounts as of September 30, 2020 and December 31, 2019, respectively (note 17). In January, February, March and April 2019, the Company received additional funding of $1,100,000 in the form of the 2019 term loans from Archytas with maturity dates ranging from September 2019 to February 2020 (note 17). In November 2019, the Company repaid Archytas the 2019 term loans in full.

Related party sales

In March and April 2019, the Company entered into rental lease agreements to lease extraction machines and other ancillary processing equipment to Carolina Botanical Development, LLC ("CBD LLC"). CBD LLC is a related party to the Company as a result of a shareholder of the Company also being an owner of CBD LLC. As part of the March 2019 lease agreement, CBD LLC paid $100,000 owed to a related party of the Company, on behalf of the Company.

(24) Financial instrument risk exposures

Financial risk management

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

Credit risk

Credit risk is the risk of a potential loss to the Company if a customer or third party to a financial instrument fails to meet its contractual obligations. The maximum credit exposure is the carrying amount of cash, trade and other receivables and financing receivables. The Company does not have significant credit risk with respect to customers. All cash is placed with recognized U.S. financial institutions. The Company provides credit to its customers in the normal course of business and has established credit evaluation and monitoring processes to mitigate credit risk. The Company has not recognized any loss allowance for expected credit losses on the trade and other receivables and financing receivables as of September 30, 2020. See also notes 10 and 11.

The Company's financing receivables are originated with various customers, some are smaller, often owner-operated businesses, some of whom have limited access to traditional financing. A portion of the Company's lessees are either start-up businesses that have not established business credit or more tenured businesses that have experienced some business credit difficulty at some time in their history ("non-prime"). As a result, such leases entail higher credit risk, (reflected in higher than expected levels of delinquencies and loss) relative to the prime commercial equipment finance market.

The Company is entitled to repossess financed equipment if the lessee defaults on their contract in order to minimize any credit losses.

Liquidity risk

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

At September 30, 2020, the Company had current assets of $3,317,248 and current liabilities of $2,968,409. All current liabilities are due within one year.

At September 30, 2020, the Company also has undiscounted loans and borrowings of $4,982,447 of which $600,000 are due in 2020, $55,762 are due in 2022 if not forgiven (note 17) and $4,326,685 are due in 2024, as follows:

	Less than 6 months	6 months to 1 years	1 to 3 years	Over 3 years
Trade and other payables	$ 698,973	$ -	$ -	$ -
Accrued expenses	964,369	-	-	-
Loans and borrowings	600,000	-	55,762	4,326,685
Balance at September 30, 2020	$ 2,263,342	$ -	$ 55,762	$ 4,326,685

<u>Market risk</u>

Currency risk

The Company has determined its functional currency to be the Canadian dollar and U.S. dollar. The operating results and financial position of the Company are reported in U.S. dollars. The Company has minimal financial transactions denominated in currencies other than the Canadian and U.S. dollar. The Company has no hedging agreements in place with respect to foreign exchange rates. The Company believes its exposure to currency risk is not significant.

Interest rate risk

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

(25) Events after the reporting date

<u>Line of credit</u>

In November 2020, the Company closed a $2,000,000 senior secured revolving credit facility, with an FDIC insured bank, which has a term of two years, expiring in November 2022. Loans made under the revolving facility will bear interest at an annual rate equal to the greater of (i) 8.0% per annum or (ii) the Wall Street Journal Prime plus 4.0% and may be prepaid with no penalty at any time. The Company intends to use such loan proceeds, together with cash on hand, to fund additional equipment leases with new and existing customers.

<u>New leases</u>

In October 2020, the Company announced it had entered into lease agreement with Skymint Brands (formerly known as Green Peak Innovations), Michigan's leading vertically integrated cannabis operator. Skymint Brands was approved for an equipment lease facility of up to

$5,000,000 for new equipment, to be deployed in multiple tranches on a pro-rata basis and based on 48-month terms.

In November 2020, the Company announced that it had entered into a lease agreement with a large scale, vertically integrated publicly traded company with operations in Nevada and Massachusetts. The customer was approved for an equipment lease facility of up to $5,000,000, which can be drawn upon in multiple tranches as needed, with 48-month terms.