

Source Rock Royalties Ltd.
Financial Statements
For the years ended December 31, 2022 and 2021

To the Shareholders of Source Rock Royalties Ltd.:

Opinion

We have audited the financial statements of Source Rock Royalties Ltd. (the "Company"), which comprise the statements of financial position as at December 31, 2022 and December 31, 2021, and the statements of income and comprehensive income, changes in shareholders' equity and cash flows for the years then ended, and notes to the financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2022 and December 31, 2021, and its financial performance and its cash flows for the years then ended in accordance with International Financial Reporting Standards.

Basis for Opinion

We conducted our audits 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 Financial Statements section of our report. We are independent of the Company in accordance with the ethical requirements that are relevant to our audits of the 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 our audit of the financial statements of the current period. These matters were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

Key Audit Matter Description

Petroleum and natural gas interests: Assessment of impairment indicators

The Company groups its gross overriding royalties ("GORR's") into cash generating units ("CGU's") for the purpose of evaluating the carrying value of its petroleum and natural gas interests.

At each reporting period, the Company assesses whether there are any indications of possible impairment of their CGU's, which requires management judgment. This management judgment required significant auditor attention and accordingly was considered a key audit matter. Refer to note 5 for details.

Audit Response

We responded to this matter by performing procedures in relation to impairment indicators for petroleum and natural gas assets. Our audit work in relation to this included, but was not restricted to, the following:

- We obtained an understanding of management's process related to assessing whether indicators of impairment may exist.
- We obtained management's assessment of indicators of impairment and evaluated this assessment against the criteria of IAS 36 - Impairment of assets.

Other Information

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

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

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

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

Responsibilities of Management and Those Charged with Governance for the Financial Statements

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

In preparing the 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 Financial Statements

Our objectives are to obtain reasonable assurance about whether the 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 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 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 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 financial statements, including the disclosures, and whether the 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 audits and significant audit findings, including any significant deficiencies in internal control that we identify during our audits.

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 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 Scott Laluk.

Calgary, Alberta

April 14, 2023

MNP LLP

Chartered Professional Accountants

Source Rock Royalties Ltd.
Statements of Financial Position
(Expressed in Canadian dollars)

	December 31, 2022	December 31, 2021
Assets		
Current assets		
Cash and cash equivalents	\$ 13,152,502	\$ 1,492,322
Trade and other receivables (note 4)	1,094,826	822,553
Deferred financing costs (note 8d)	-	164,280
Prepaid expense	44,947	5,777
Total current assets	14,292,275	2,484,932
Petroleum and natural gas interests (note 5)	14,057,591	12,622,096
Intangible (note 6)	250,000	250,000
Deferred tax (note 10)	218,330	-
Total assets	\$ 28,818,196	\$ 15,357,028
Liabilities		
Current liabilities		
Trade and other payables	\$ 26,853	\$ 124,382
Corporate taxes payable	678,498	82,308
Dividend payable (note 13)	673,450	443,438
Total current liabilities	1,378,801	650,128
Deferred tax (note 10)	-	145,802
Total liabilities	1,378,801	795,930
Shareholders' equity		
Share capital (note 8a)	26,292,227	13,984,321
Warrants (note 8a)	306,682	-
Contributed surplus (note 8b)	16,130,994	15,731,541
Deficit	(15,290,508)	(15,154,764)
Total shareholders' equity	27,439,395	14,561,098
Total liabilities and shareholders' equity	\$ 28,818,196	\$ 15,357,028

Approved on behalf of the Board of Directors by:

"Signed" Brad Docherty

Director

"Signed" John Bell

Director

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

Source Rock Royalties Ltd.
Statements of Income and Comprehensive Income

For the years ended December 31,
(Expressed in Canadian dollars)

		2022		2021
Royalty revenues (note 9)	\$	6,490,519	\$	4,261,974
Expenses				
Administrative expenses		753,897		475,859
Bad debt (recovery) expense		-		(9,908)
Share-based compensation (notes 8c and 8d)		399,453		313,704
Depletion (note 5)		2,181,041		2,235,533
Impairment (note 5)		-		1,381,559
Total expenses		3,334,391		4,396,747
Income (loss) for the year		3,156,128		(134,773)
Other income				
Interest		286,583		956
Income (loss) before taxes		3,442,711		(133,817)
Provision for income taxes				
Current tax expense		894,499		82,308
Deferred tax recovery		(9,842)		(392,666)
Income tax recovery (note 10)		884,657		(310,358)
Total comprehensive income	\$	2,558,054	\$	176,541
Income per share, basic	\$	0.060	\$	0.006
Income per share, diluted	\$	0.059	\$	0.006
Weighted average number of shares:				
Basic		42,344,911		29,422,055
Diluted		43,218,505		31,210,964

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

Source Rock Royalties Ltd.
Statements of Changes in Shareholders' Equity

*For the years ended December 31,
(Expressed in Canadian dollars)*

	Share capital	Warrants	Contributed surplus	Deficit	Total shareholders' equity
As at December 31, 2020	\$ 28,679,325	\$ -	\$ 1,081,271	\$ (14,008,527)	\$ 15,752,069
Shares issued on acquisition of royalty interests (note 4)	85,000	-	-	-	85,000
Return of capital	(443,438)	-	-	-	(443,438)
Reduction of stated capital	(14,556,562)	-	14,556,562	-	-
Shares issued for compensation (note 8c and 8d)	186,000	-	127,704	-	313,704
Shares issued on exercise of stock options (note 8c)	33,996	-	(33,996)	-	-
Dividends (note 8f)	-	-	-	(1,322,778)	(1,322,778)
Total comprehensive loss for the year	-	-	-	176,541	176,541
As at December 31, 2021	\$ 13,984,321	\$ -	\$ 15,731,541	\$ (15,154,764)	\$ 14,561,098
Shares issued for cash (note 8a)	13,494,008	-	-	-	13,494,008
Warrants (note 8a)	-	306,682	-	-	306,682
Share issuance costs, net of deferred tax benefit of \$354,290	(1,186,102)	-	-	-	(1,186,102)
Share-based compensation (note 8c and 8d)	-	-	399,453	-	399,453
Dividends (note 8f)	-	-	-	(2,693,798)	(2,693,798)
Total comprehensive income for the year	-	-	-	2,558,054	2,558,054
As at December 31, 2022	\$ 26,292,227	\$ 306,682	\$ 16,130,994	\$ (15,290,508)	\$ 27,439,395

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

Source Rock Royalties Ltd.

Statements of Cash Flows

For the years ended December 31,
(Expressed in Canadian dollars)

	2022	2021
Operating activities		
Net income	\$ 2,558,054	\$ 176,541
Adjustments for:		
Share-based compensation (notes 8c and 8d)	399,453	313,704
Depletion (note 5)	2,181,041	2,235,533
Impairment (note 5)	-	1,381,559
Bad debt (recovery)	-	(9,908)
Deferred income taxes (recovery) (note 10)	(9,842)	(392,666)
Change in non-cash working capital balances		
Trade and other receivables	(272,273)	(447,907)
Prepaid expense	(39,170)	21,047
Trade and other payables	(97,529)	45,400
Corporate taxes payable	596,190	82,308
Cash flows from operating activities	5,315,924	3,405,611
Financing activities		
Dividends paid to shareholders (note 8e)	(2,020,348)	(1,469,014)
Return of capital (note 8a)	(443,438)	-
Proceeds from shares issued (note 8a)	13,494,008	-
Proceeds from warrants issued (note 8a)	306,682	-
Share issuance costs	(1,376,112)	-
Deferred Financing Costs (note 8d)	-	(164,280)
Cash flows from (used in) financing activities	9,960,792	(1,633,294)
Investing activities		
Purchase of petroleum and natural gas interests (note 5)	(3,616,536)	(1,193,555)
Cash flows used in investing activities	(3,616,536)	(1,193,555)
Increase in cash and cash equivalents	11,660,180	578,762
Cash and cash equivalents, beginning of year	1,492,322	913,560
Cash and cash equivalents, end of year	\$ 13,152,502	\$ 1,492,322

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

Source Rock Royalties Ltd.

Notes to the Financial Statements

For the years ended December 31, 2022 and December 31, 2021

1. REPORTING ENTITY

Source Rock Royalties Ltd. ("Source Rock" or the "Company") was incorporated under the laws of the Province of Alberta on October 11, 2012, and has its registered office at 15th Floor, 850 – 2nd Street, SW, Calgary Alberta T2P 0R8.

The primary business of the Company is to receive royalty revenue from oil and natural gas properties as reserves are produced by the operators over the economic life of the properties. The Company is exclusively focused on acquiring and managing oil and gas royalties and mineral title interests. The Company has a light oil focused portfolio of royalty interests concentrated in S.E. Saskatchewan, east-central Alberta, west-central Alberta and west-central Saskatchewan. The Company is focused on acquiring royalties in properties that have foreseeable future drilling potential and which are operated by fiscally and operationally prudent third parties. The Company is further focused on establishing relationships with third parties via its royalty interests, wherein mutual benefits can be derived from the near-term and medium-term development, and long-term enhancement, of the assets. The Company does not incur any ongoing costs to develop, operate or enhance the lands in which it has royalties, nor does it have any exposure to abandonment or reclamation obligations associated with its royalty lands.

These financial statements were authorized for issuance by the Company's Board of Directors on April 14, 2023.

2. BASIS OF PREPARATION

a) Statement of compliance

The financial statements of the Company 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 Interpretation Committee ("IFRIC") in effect as of January 1, 2022.

b) Basis of measurement

The financial statements have been prepared on a historical cost basis except for measurement of certain financial instruments at fair value through profit or loss.

c) Functional currency

These financial statements are presented in Canadian dollars, which is the Company's functional currency.

d) Use of judgments and estimates

Management is required to make estimates, judgments and assumptions that affect the application of policies and reported amounts of assets, liabilities, income and expenses. Management reviews these judgments, estimates and assumptions on an ongoing basis, including those related to depreciation, fair values of financial instruments, recoverability of assets and taxes. Actual results may differ from these estimates and these differences may be material.

The key estimates and judgments concerning the future and other key sources of estimation uncertainty at the reporting date that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities are outlined below. Readers are cautioned that the following list is not exhaustive and other items may also be affected by estimates and judgments.

Judgments

Judgment is used in situations when there is a choice and/or assessment required by management. The following are critical judgments apart from those involving estimations (disclosed below), that management has made in the process of applying the Company's accounting policies and that have a significant effect on the amounts recognized in the financial statements.

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Notes to the Financial Statements

For the years ended December 31, 2022 and December 31, 2021

- **Determining cash generating units ("CGU")** - For the purpose of assessing impairment of petroleum and natural gas interests, assets are grouped at the lowest level of separately identifiable cash flows which make up the CGU. Determination of what constitutes a CGU is subject to management judgment. The asset composition of a CGU can directly impact the recoverability of assets included within the CGU. In assessing the recoverability of tangible and intangible assets, each CGU's carrying value is compared to the greater of its fair value less costs of disposal and value in use. As at December 31, 2022, and 2021, the Company had four CGUs based on geographical location, being west-central Saskatchewan, south-east Saskatchewan, east-central Alberta and west-central Alberta.
- **Impairment** - The Company is required to make a judgment regarding whether indicators of impairment exist at each reporting date by evaluating conditions specific to the organization that may lead to the impairment of assets.
- **Taxes** - The Company applies judgment in determining the total provision for current and deferred taxes. There are many transactions and calculations for which the ultimate tax determination and timing of payment is uncertain due to interpretations of complex tax regulations, changes in tax laws, and the amounts and timing of future taxable income. Deferred tax assets, if any, are recognized to the extent it is considered probable that those assets will be recoverable. This involves an assessment of when those deferred tax assets are likely to reverse. Differences arising between the actual results and the assumptions made, or future changes to such assumptions, could necessitate future adjustments to income tax and expenses already recorded.
- **Contingencies** - Management uses judgment to assess the existence of contingencies. By their nature, contingencies will only be resolved when one or more future events occur or fail to occur. Management also uses judgment to assess the likelihood of the occurrence of one or more future events.

Estimates

Revisions to accounting estimates are recognized in the period in which the estimates are revised and in any future periods affected. Areas where there are significant estimates are as follows:

- **Reserves** - Reserves estimates are not recorded in the Source Rock's financial statements but they do affect net income and assets and liabilities through their impact on depletion, depreciation and amortization ("DD&A"), amounts used for impairment calculations and deferred income taxes. By their nature, proved and probable crude oil and natural gas reserves and the future cash flows derived from them are significant estimates, which are subject to measurement uncertainty, and include significant assumptions related to future royalty production from proved and probable crude oil and natural gas reserves and future realized commodity prices. Accordingly, the impact to amounts reported in the financial statements for future periods could be material. Reserves have been evaluated at December 31, 2022 by the Company's external independent qualified reserves evaluators and have been determined pursuant to National Instrument 51-101 Standards of Disclosure for Oil and Gas Activities.
- **Accounts receivables** - Accounts are recorded at the estimated recoverable amounts. For the year ended December 31, 2022, Source Rock recorded a credit loss of \$nil (2021 - \$nil).
- **Depletion and residual values of petroleum and natural gas interests** - The amounts recorded for the depletion of petroleum and natural gas interests are based on estimates of petroleum and natural gas reserves. By their nature, these estimates of reserves are subject to uncertainty, and the impact on the financial statements of future periods could be material.
- **Impairment** - Impairment exists when the carrying value of a CGU exceeds its recoverable amount, which is the higher of its fair value less cost of disposal ("FVLCD") and its value in use ("VIU"). The FVLCD calculation is based on available data from binding sales transactions, conducted at arm's length, for similar assets or observable market prices less incremental costs for disposing of the asset. If no such transactions can be identified, an appropriate valuation model is used.
- **Share-based compensation** - All equity-settled, share based awards issued by the Company are recorded at fair value using the Black-Scholes option pricing model. In assessing the fair value of the equity-based

Source Rock Royalties Ltd.

Notes to the Financial Statements

For the years ended December 31, 2022 and December 31, 2021

compensation, estimates have to be made regarding the expected volatility is based on comparable listed entities in share price, option life, risk-free rate and estimated forfeitures at the initial grant date.

- **Taxes** - Tax provisions are based on enacted or substantively enacted laws. Changes in those laws could affect amounts recognized in the statement of income and comprehensive income both in the period of change, which would include any impact on cumulative provisions, and future periods.

3. SIGNIFICANT ACCOUNTING POLICIES

The principal accounting policies applied in the preparation of these financial statements are set out below.

a) Cash and cash equivalents

Cash and cash equivalents are comprised of cash in banks, and all short-term investments that are readily convertible into known amounts of cash and have original maturities of three months or less.

b) Revenue recognition

Revenue is made up of royalty income. Royalty income is recognized when the Company's interest in the oil and gas rights is either produced or sold in the period by oil and gas producers on specific lands identified by various royalty interest agreements. Royalty income is measured at the fair value, using estimates, per the terms of various royalty interest agreements. Actual results could differ as a result of using estimates and any differences are recorded in the period in which actual amounts are received.

c) Petroleum and natural gas interests

Petroleum and natural gas interests are classified under IAS 16 as "Property, Plant and Equipment" and include royalty interests, stated at cost, less accumulated depletion and accumulated impairment losses. A gain or loss on disposal of a petroleum and natural gas interest is recognized to the extent that the net proceeds exceed or are less than the appropriate portion of the capitalized costs of the asset.

Petroleum and natural gas interests are depleted on the unit-of-production method based on estimated proved and probable oil and gas reserves.

d) Impairment of long-term assets

At each reporting date, the Company assesses groups of assets or CGUs for impairment whenever events or changes in circumstances indicate that the carrying value of the CGU may not be recoverable. If any such indication of impairment exists, the Company makes an estimate of its recoverable amount.

A CGU's recoverable amount is the higher of its FVLCD and its VIU. Where the carrying amount of a CGU exceeds its recoverable amount, the CGU is considered impaired and is written down. In assessing VIU, the estimated future cash flows are adjusted for the risks specific to the CGU and are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money. FVLCD is the amount obtainable from the sale of assets in an arm's length transaction less cost of disposal.

An assessment is made at each reporting date as to whether there is any indication that previously recognized impairment losses may no longer exist or have decreased. If such indication exists, the recoverable amount is estimated. A previously recognized impairment loss is reversed only if there has been a change in the estimates used to determine the CGU's recoverable amount since the last impairment loss was recognized.

If that is the case, the carrying amount of the CGU is increased to its recoverable amount. That increased amount cannot exceed the carrying amount that would have been determined, net of depletion, had no impairment loss been recognized for the CGU in prior years. Such a reversal is recognized in the statement of comprehensive income. After such a reversal, the depletion charge is adjusted in future periods to allocate the CGU's revised carrying amount, less any residual value, on a systematic basis over its remaining useful life.

e) Share-based compensation

The grant-date fair value of share-based payment awards granted to employees, directors or consultants is recognized as share-based compensation expense, with a corresponding increase in contributed surplus, over the period that the individuals become entitled to the awards. Any consideration received on exercise of stock options is credited to share capital along with the amounts originally recorded as contributed surplus.

f) Taxes

Tax expense comprises current and deferred tax. Current and deferred tax is recognized in the statement of comprehensive income except to the extent that it relates to a business combination, or items recognized directly in equity or in other comprehensive income.

Current tax is the expected tax payable or receivable on the taxable income or loss for the period, using tax rates enacted or substantively enacted at the reporting date, and any adjustment to tax payable in respect of previous years.

Deferred tax is recognized in respect of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is measured at the tax rates that are expected to be applied to temporary differences when they reverse, based on the laws that have been enacted or substantively enacted by the reporting date.

A deferred tax asset is recognized for unused tax losses, tax credits and deductible temporary differences, to the extent that it is probable that future taxable profits will be available against which they can be utilized. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realized.

g) Income per share

The calculation of basic income per share is based on net income divided by the weighted average number of common shares outstanding. Diluted income per share is determined by adjusting the income per share attributable to ordinary shareholders for the effects of all potentially dilutive ordinary shares, which comprise share options and warrants granted to employees and directors. All share purchase options are considered anti-dilutive when the Company is in a loss position.

h) Financial instruments

Classification

The Company classifies its financial assets and financial liabilities in the following measurement categories: (i) those to be measured subsequently at fair value through profit or loss ("FVTPL"); (ii) those to be measured subsequently at fair value through other comprehensive income ("FVOCI"); and (iii) those to be measured at amortized cost. Financial liabilities are classified as those to be measured at amortized cost unless they are designated as those to be measured subsequently at FVTPL (irrevocable election at the time of recognition). For assets and liabilities measured at fair value, gains and losses are either recorded in profit or loss or other comprehensive income.

The Company reclassifies financial assets when and only when its business model for managing those assets changes. Financial liabilities are not reclassified.

Impairment

The Company assesses all information available, including on a forward-looking basis the expected credit loss associated with its assets carried at amortized cost. The impairment methodology applied depends on whether there has been a significant increase in credit risk. To assess whether there is a significant increase in credit risk, the Company compares the risk of a default occurring on the asset as at the reporting date with the risk of default as at the date of initial recognition based on all information available, and reasonable and supportive forward-looking information. For trade and other receivables only, the Company applies the simplified approach as permitted by IFRS 9. The simplified approach to the recognition of expected losses does not require the Company to track the changes in credit risk; rather, the Company recognizes a loss allowance based on lifetime expected credit losses at each reporting date from the date of the trade receivable.

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Evidence of impairment may include indications that the counterparty debtor or a group of debtors is experiencing significant financial difficulty, default or delinquency in interest or principal payments, the probability that they will enter bankruptcy or other financial reorganization and where observable data indicates that there is a measurable decrease in the estimated future cash flows, such as changes in arrears or economic conditions that correlate with defaults. Receivables are reviewed qualitatively on a case-by-case basis to determine whether they need to be written off.

Expected credit losses are measured as the difference in the present value of the contractual cash flows that are due to the Company under the contract, and the cash flows that the Company expects to receive. The Company assesses all information available, including past due status, credit ratings, the existence of third-party insurance, and forward-looking macro-economic factors in the measurement of the expected credit losses associated with its assets carried at amortized cost.

The Company measures expected credit loss by considering the risk of default over the contract period and incorporates forward-looking information into its measurement.

Financial instrument de-recognition

Financial assets are de-recognized 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 de-recognized when the obligation is discharged, cancelled, or expired.

i) Provisions

A provision is recognized if, because of a past event, the Company has a present legal or constructive obligation that can be estimated reliably, and it is probable that an outflow of economic benefits will be required to settle the obligation. Provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the liability. Provisions are not recognized for future operating losses.

A provision for onerous contracts is recognized when the expected benefits to be derived by the Company from a contract are lower than the unavoidable cost of meeting its obligations under the contract. The provision is measured at the present value of the lower of the expected cost of terminating the contract and the expected net cost of continuing with the contract. Before a provision is established, the Company recognizes any impairment loss on associated assets.

j) Equity instruments

Equity instruments issued by the Company are recorded as the proceeds received net of direct issue costs.

k) Intangible assets

The Company purchased a right to acquire a 2% gross overriding royalty ("GORR") in all oil and natural gas interested purchased or earned by a certain company. Intangible assets with finite useful lives are tested for impairment when events or changes in circumstances indicate that the carrying amount may not be recoverable. Indefinite life intangible assets are reviewed for impairment annually or at any time if an indicator of impairment exists.

Source Rock Royalties Ltd.

Notes to the Financial Statements

For the years ended December 31, 2022 and December 31, 2021

4. TRADE AND OTHER RECEIVABLES

Accounts Receivable and Accrued Royalty Revenues	As at December 31, 2022	As at December 31, 2021
Trade receivable and accrued royalty revenue	\$ 1,100,678	\$ 854,228
Expected credit loss	(41,335)	(41,335)
GST and other receivable	35,483	9,660
	\$ 1,094,826	\$ 822,553

Trade receivable and accrued revenue relate to royalty production payments receivable.

The analysis of trade receivable and accrued royalty revenue that are past due but not impaired is as follows:

	Total	Neither past due nor Impaired	Past due but not impaired	
			3-6 Months	7- 12 Months
As at December 31, 2022	\$ 1,059,343	\$ 1,059,343	\$ -	\$ -
As at December 31, 2021	\$ 812,893	\$ 804,665	\$ 8,228	\$ -

In determining the collectability of trade receivables that are past due but not impaired, the Company considers the age of the outstanding receivable and the credit worthiness of the parties (note 11).

5. PETROLEUM AND NATURAL GAS INTERESTS

Cost	Total
Balance December 31, 2020	\$ 22,619,176
Additions	1,333,555
Impairment	(1,381,559)
Balance December 31, 2021	\$ 22,571,172
Additions	3,616,536
Balance December 31, 2022	\$ 26,187,708
Accumulated depletion	
Balance December 31, 2020	\$ 7,713,543
Depletion	2,235,533
Balance December 31, 2021	\$ 9,949,076
Depletion	2,181,041
Balance December 31, 2022	\$ 12,130,117
Carrying Amounts	
At December 31, 2021	12,622,096
At December 31, 2022	\$ 14,057,591

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Notes to the Financial Statements

For the years ended December 31, 2022 and December 31, 2021

2022:

On November 25, 2022, Source Rock acquired a 2% GORR in land located in S.E. Saskatchewan for gross proceeds of \$3,500,000 (the "November 2022 Acquisition"), with an effective date of October 1, 2022. Sales proceeds for royalty production between the effective date and the closing date amounting to \$85,268 was deducted from the purchase price. Transaction costs related to the November 2022 Acquisition amounting to \$75,148 were added to the purchase price.

On November 10, 2022, Source Rock acquired a 2% GORR in land located in S.E. Saskatchewan for proceeds of \$22,851.

On October 27, 2022, Source Rock acquired a 2% GORR in land located in S.E. Saskatchewan for proceeds of \$48,697.

On July 27, 2022, Source Rock acquired a 2% GORR in land located in S.E. Saskatchewan for proceeds of \$55,108.

2021:

On August 6, 2021, Source Rock acquired a 2% GORR in land located in S.E. Saskatchewan for proceeds of \$71,110.

On July 9, 2021, Source Rock acquired a 2% GORR in land located in S.E. Saskatchewan for proceeds of \$32,256.

On April 26, 2021, Source rock acquired various GORR's in S.E. Saskatchewan for proceeds of \$1,215,000, comprised of \$1,130,000 in cash and \$85,000 common shares at a price of \$1.00 per share.

On March 18, 2021, Source Rock acquired a 2% GORR in land located in S.E. Saskatchewan for proceeds of \$15,189.

Impairment

Source Rock groups its GORR's into cash generating units ("CGU's") for the purpose of evaluating the carrying value of its petroleum and natural gas interests. The recoverable amounts were determined using fair value less cost to sell. The estimated recoverable amount of the Company's assets involved certain significant estimates including the future cash flows expected to be derived from each CGU and the discount rate. The significant assumptions used by the Company in determining the future cash flow estimates related to future royalty production and future realized commodity prices. The fair value measurement is designated Level 3 on the fair value hierarchy. Changes in any of the significant estimates and assumptions, such as a downward revision in future royalty production, a decrease in future realized commodity prices, or an increase in the discount rate would have decreased the recoverable amounts of assets and any impairment charges would affect operating results. The other key assumptions used in determining the recoverable amount included the future cash flows using a market discount rate of 10%.

As at December 31, 2022 and December 31, 2021, there were no indicators of impairment.

As at March 31, 2021, there were indicators of impairment due to the continued underperformance of two CGU's. Despite improved commodity prices during Q1 2021, these CGU's did not see production volumes return to historical levels as anticipated as at December 31, 2020.

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Notes to the Financial Statements

For the years ended December 31, 2022 and December 31, 2021

As at March 31, 2021, the following benchmark reference price forecasts were used to calculate the recoverable amounts:

			2021	2022	2023	2024	2025
Canadian	Light	Sweet					
(\$Cdn/bbl)			56.12	61.69	66.79	68.14	69.50

As at March 31, 2021, the following impairment charges were taken:

CGU	Impairment
West-central Saskatchewan	\$668,819
West-central Alberta	\$712,740

6. INTANGIBLE

On January 27, 2020, Source Rock entered into an agreement with a S.E. Saskatchewan focused oil and gas company ("E&P Co."), whereby Source Rock paid \$250,000 for a right, but not an obligation, to acquire a 2% GORR in all oil and natural gas interests purchased or earned by E&P Co. The agreement is not subject to any geographical boundaries, does not expire and will be required to be assumed by future parties in any change of control scenarios relating to E&P Co.

7. RELATED PARTY TRANSACTIONS

Key personnel transactions

Key personnel includes the Chief Executive Officer, the Chief Financial Officer, the Corporate Secretary and the Directors of the Company. For the year ended December 31, 2022 and 2021, the Company had the following transactions with key personnel.

		2022	2021
Wages and consulting fees	\$	358,125	\$ 357,000
Share-based compensation		354,172	313,704
Total	\$	712,297	\$ 670,704

Share-based compensation includes share-based consulting fees and a charge for stock options, RSUs and DSUs, as defined herein. During the year ended December 31, 2022, nil (2021 - 190,312) common shares were issued as compensation to management and the Directors in lieu of cash compensation and was recorded as share-based compensation in the amount of \$nil (2021 - \$186,000). A share-based compensation expense was recorded for the vesting of issued stock options during the year ended December 31, 2022, in the amount of \$83,164 (2021 - \$127,704) (see note 8c). A share-based compensation expense was recorded relating to RSUs and DSUs granted during the year ended December 31, 2022, in the amount of \$72,229 (2021 - \$nil) and \$198,779 (2021 - \$nil), respectively.

In addition, during the year ended December 31, 2022, \$433,859 (2021 - \$199,602) of costs were incurred to a law firm at which the Corporate Secretary of the Company is a Partner. These fees primarily related to work associated with the Company's initial public offering ("IPO") and general corporate matters.

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Notes to the Financial Statements

For the years ended December 31, 2022 and December 31, 2021

All transactions were in the normal course of operations and were measured at the amount of consideration agreed to by both parties. As at December 31, 2022, there was \$1,895 (December 31, 2021 - \$98,873) in trade payables and accrued liabilities relating to these transactions.

8. SHARE CAPITAL

a) Common shares

	December 31, 2022		December 31, 2021	
	# of common shares	Amount	# of common shares	Amount
Balance, beginning of period	29,562,559	\$ 13,984,321	29,247,247	\$ 28,679,325
Shares issued for cash (i)	15,334,100	13,494,008	-	-
Share issuance costs, net of deferred tax benefit of \$354,290	-	(1,186,102)	-	-
Fractional shares canceled	(14)	-	-	-
Shares issued on acquisition of royalty interest (ii)	-	-	85,000	85,000
Shares issued for exercised stock options (note 7c)	-	-	40,000	33,996
Shares issued for compensation (note 6)	-	-	190,312	186,000
Return of capital (note 8f)	-	-	-	(443,438)
Reduction in stated capital	-	-	-	(14,556,562)
Balance, end of period	44,896,645	\$ 26,292,227	29,562,559	\$ 13,984,321

(i) On March 1, 2022, Source Rock closed an initial public offering (the "IPO"), through the issuance of 13,667,100 Units at a price of \$0.90 pursuant to a final prospectus dated February 23, 2022, for gross proceeds of \$12,300,390. Each Unit was comprised of one Common Share (with an ascribed value of \$0.88) and one half of one warrant (with an ascribed value of \$0.02) to purchase an additional Common Share at \$1.25 for a period of two years (the "Warrants"). The IPO was completed by a syndicate of underwriters co-led by PI Financial Corp (as Sole Bookrunner) and Acumen Capital Finance Partners Limited, together with Haywood Securities Inc., Canaccord Genuity Corp. and ATB Capital Markets Inc. On March 16, 2022, Source Rock closed the over-allotment portion of the IPO through the issuance of an additional 1,667,000 Units, for gross proceeds of \$1,500,300.

(ii) In Q2, 2021, the Company issued 85,000 common shares at \$1.00 per share as partial consideration for GORR's.

Reduction of stated capital

Under the Alberta Business Corporations Act ("ABCA"), a corporation is prohibited from taking certain actions, including declaring or paying a dividend, if, among other things, there are reasonable grounds for believing that the realizable value of its assets would, as a result of the declaration or payment of the dividend, be less than the aggregate of its liabilities and stated capital of all classes of its shares. The stated capital is the aggregate of all amounts received by a corporation upon the issuance of its shares, adjusted in certain circumstances in accordance with the provisions of the ABCA. The stated capital for a class of shares can be reduced in accordance with the restrictions in the ABCA. A corporation reducing its stated capital reduces the aggregate of the corporation's liabilities and stated capital of all classes of its shares to increase the difference between such amount and the realizable value of the corporation's assets, thereby providing the corporation with additional flexibility to pay dividends if, as and when declared.

On December 22, 2021, the Company's shareholders approved a reduction in the Company's stated capital by \$15,000,000. The Company subsequently reduced its stated capital by aggregate of \$15,000,000, which included the reduction associated with a return of capital of \$443,438.

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Notes to the Financial Statements

For the years ended December 31, 2022 and December 31, 2021

b) Contributed surplus

Balance, December 31, 2020	\$ 1,081,271
Share-based compensation (note 8c)	127,704
Exercised stock options (note 8c)	(33,996)
Reduction in stated capital (note 8a)	14,556,562
Balance, December 31, 2021	\$ 15,731,541
Share-based compensation (note 8c and 8d)	399,453
Balance, December 31, 2022	\$ 16,130,994

c) Stock options

The Company created a rolling 10% stock option plan which became effective July 2, 2013. The stock option plan provides options for directors, key management personnel and consultants. A summary of the Company's outstanding stock options as at December 31, 2021, and the changes for the current year, is as follows:

	Outstanding	Weighted Average Remaining Contractual Life		Weighted Average Exercise Price
Balance, December 31, 2020	2,490,000	2.1	\$	0.72
Granted	40,000	4.0		0.40
Exercised	(40,000)	-	\$	1.00
Balance, December 31, 2021	2,490,000	2.1	\$	0.72
Granted	400,000	4.6	\$	0.90
Expired	(650,000)	-		0.90
Balance, December 31, 2022	2,240,000	2.6	\$	0.67

For the year ended December 31, 2022, the Company has recorded \$118,534 (2021 - \$127,704) in share-based compensation expense for the vesting of granted stock options with a corresponding amount credited to contributed surplus. During 2022, 650,000 (2021 - nil) stock options expired. As of December 31, 2022, the Company has 1,956,667 (2020 - 2,175,000) exercisable (vested) stock options.

The fair value of stock options granted in 2022 and 2021 was estimated using the Black-Scholes option-pricing model with the following weighted average assumptions:

	2022	2021
Exercise price	\$0.90	\$Nil
Dividend yield	Nil	Nil
Expected volatility	35-45%	42.7%
Risk-free interest rate	2.5%	1.5%
Expected life	5 Year	5 Year
Forfeiture Rate	0.0%	0.0%

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For the years ended December 31, 2022 and December 31, 2021

d) Restricted Share Units ("RSU") and Deferred Share Units ("DSU")

On June 22, 2022, the Company's shareholders approved a fixed 10% RSU/DSU compensation plan (the "RSU/DSU Plan"). The RSU/DSU Plan provides RSU's and DSU's for directors, key management personnel and consultants.

Each RSU/DSU entitles the holder to acquire one common share of Source Rock, or a cash payment equal to the equivalent value of one common share of Source Rock at the time of vesting, or a combination of both (in the sole discretion of the Company's Board of Directors). RSUs will be settled within 30 days of vesting. DSUs will be settled within 30 days of the holder no longer being an officer, director, employee or consultant of the Company. Because the Company's Board of Directors has the ability to settle the RSUs/DSUs through equity and have not stated nor have any history of settling the RSUs/DSUs in cash, the RSU/DSU Plan will be classified as equity settled. Compensation expense is recognized at the market value of the Company's common shares at the time of grant and recognized over the vesting period with a corresponding increase to contributed surplus. Upon vesting of the RSU/DSU, the amount previously recognized in contributed surplus is recorded as an increase to shareholders' capital. The RSU's granted shall vest evenly over three years on the anniversary date of the grant and the DSU's granted shall vest after one year following the grant date.

RSUs and DSUs will be credited with dividend equivalents in the form of additional RSUs and DSUs, respectively, as of each dividend payment date in respect of which normal cash dividends are paid on common shares. Dividends are recognized as compensation expense at the market value on the record date at the time the dividend is paid. Dividend equivalents credited to a RSU/DSU holder's account shall vest in proportion to the RSUs and DSUs to which they relate.

A summary of the Company's outstanding RSUs as at December 31, 2022, and the changes for the current year, is as follows:

	Outstanding	Weighted Average Grant Price
Balance, December 31, 2021	-	\$ -
Granted	307,500	0.85
Dividends	6,318	0.73
Balance, December 31, 2022	313,818	\$ 0.85

For the year ended December 31, 2022, the Company has recorded \$78,380 (2021 - nil) in share-based compensation expense with respect to RSUs issued during the year, with a corresponding amount credited to contributed surplus.

A summary of the Company's outstanding DSUs as at December 31, 2022, and the changes for the current year, is as follows:

	Outstanding	Weighted Average Grant Price
Balance, December 31, 2021	-	\$ -
Granted	552,500	0.83
Dividends	9,709	0.73
Balance, December 31, 2022	562,209	\$ 0.83

For the year ended December 31, 2022, the Company has recorded \$202,539 (2021 - nil) in share-based compensation expense with respect to DSUs issued during the period, with a corresponding amount credited to contributed surplus.

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Notes to the Financial Statements

For the years ended December 31, 2022 and December 31, 2021

e) Deferred financing costs

During the fourth quarter of 2021, Source Rock initiated the IPO process and incurred legal costs of \$164,280, which were deferred until the IPO closed. Upon closing of the IPO these financing costs were capitalized against the proceeds as share issuance costs.

f) Dividends

During 2022, the Company declared dividends of \$2,693,798 (2021 - \$1,322,778). The total dividends paid during 2022 was \$2,020,348 (2021 - \$1,469,014). In addition, during the year ended December 31, 2022, the Company paid \$443,438 to shareholders in the form of a "return of capital".

9. REVENUES

As per note 3b), royalty and other revenue are measured at fair value of the consideration received or receivable, per the terms of various agreements. The transaction price used for crude oil, natural gas, natural gas liquids and other products is based on the commodity price in the month of production specific to the property or interest. The commodity price received, or receivable is based on market benchmarks adjusted for quality, location, allowable deductions, if any, and other factors. Typically, Source Rock would receive the cash payments 30 to 60 days following production or the sale of commodity by the producer.

Revenue and other revenue by product	2022	2021
Oil	\$ 6,218,233	\$ 4,141,265
Natural Gas	169,813	75,061
NGL	102,473	45,648
Total royalty revenue	\$ 6,490,519	\$ 4,261,974

As at December 31, 2022, there was outstanding trade accounts receivable of \$1,059,343 (2021 - \$812,893).

10. TAXES

The tax effects of deductible and taxable temporary differences that give rise to the Company's deferred tax are as follows:

	2022	2021
Share issue costs	283,432	\$ -
Non-capital loss carry forwards	-	-
Capital loss carry forwards	10,839	10,839
Petroleum and natural gas interest	(65,102)	(145,802)
Deferred tax asset not recognized	(10,839)	(10,839)
Deferred tax asset (liability)	\$ 218,330	\$ (145,802)

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The components of the Company's net tax expense which has been recorded in these financial statements are as follows:

	2022	2021
Net income (loss) before taxes	\$ 3,442,711	\$ (133,817)
Statutory rate	23.00%	46.67%
Expense/(recovery) at statutory rate	791,824	(62,452)
Share-based compensation	91,874	59,599
Refundable dividend on hand	-	(157,724)
Rate difference and other	959	(149,781)
Income tax recovery	\$ 884,657	\$ (310,358)

The continuity of deferred taxes is as follows:

	Balance December 31, 2021	Recognized in statement of comprehensive income	Recognized directly in shareholders' equity	Balance December 31, 2022
Petroleum and natural gas interest	(145,802)	80,700	-	(65,102)
Share issue costs	-	(70,858)	354,290	283,432
	(145,802)	9,842	354,290	218,330

The Company has \$nil (2021 - \$1,654,987) in non-capital loss carry forwards and \$94,255 (2021 - \$94,255) in capital loss carry forwards. As a result of the IPO, the Company is no longer subject to income tax rates applicable to Canadian Controlled Private Corporations and is now subject to 23% income tax rates as a public company.

11. FINANCIAL RISK MANAGEMENT

Financial instruments and risk management

The Company's activities expose it to a variety of financial risks: credit risk, liquidity risk and commodity risk. The Company's overall risk management program focuses on the unpredictability of financial markets and seeks to minimize potential adverse effects on the Company's financial performance.

Fair values

The Company's financial instruments recognized on the statement of financial position consist of current assets and liabilities of cash and cash equivalents, trade and other receivables, and trade and other payables and dividends payable. The fair values of the Company's current financial assets and liabilities approximate their carrying values due to their short-term maturities.

Credit risk

Credit risk arises when a failure by counter parties to discharge their obligations could reduce the amount of future cash inflows from financial assets on hand at the statement of financial position date. As at December 31, 2022, the Company's trade receivable balance was subject to normal industry credit risks and was primarily with two royalty payors which accounted for 76% (2021- 73%) of the trade and other receivable balance and 73% (2021 - 74%) of the revenue balance. The Company manages its exposure to credit risk through standard credit granting procedures and short payment terms. The Company attempts to monitor financial conditions of its royalty payors and the industry in which they operate. The carrying amounts of trade and other receivables and cash and cash equivalents represent the Company's maximum credit exposure. The Company has recorded an impairment of \$nil (2021 - \$nil) in trade and other receivables specific to two customers.

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Liquidity risk

Liquidity risk is the risk that the Company will not be able to meet financial obligations at the point at which they are due. The Company's operating cash requirements are continuously monitored by management. As factors impacting cash requirements change, liquidity risks may necessitate the need for the Company to raise capital by issuing equity or obtaining debt financing.

All of the Company's trade and other payables are due in less than one year.

Commodity risk

Commodity price risk is the risk that the fair value of future cash flows will fluctuate with changes in commodity prices. Commodity prices for oil and natural gas are influenced by the relationship between the Canadian and U.S. dollar as well as macroeconomic events that dictate the levels of supply and demand. During the years ended December 31, 2022 and 2021, the Company had no commodity price risk related derivative contracts in place.

For the year ended December 31, 2022, the average price realization on the Company's royalty interests was \$107.28/boe (2021 - \$81.52/boe). If the price realization increased (decreased) by 5%, with all other variables held constant, pre tax net income would have increased (decreased) by approximately \$324,526 (2020 - \$213,099).

12. CAPITAL MANAGEMENT

The Company's capital is comprised of cash and cash equivalents and shareholders' equity. The Board of Directors does not establish quantitative return on capital criteria for management but rather promotes a prudent, repeatable, scalable and sustainable corporate platform that minimizes operating costs, and aims to maximize returns to its shareholders through per share cash flow growth and ultimately payment of a sustainable and conservative dividend. The Company is not subject to any externally or internally imposed capital requirements as at December 31, 2022.

13. SUBSEQUENT EVENTS

In January 2023, Source Rock acquired a 2% GORR in land located in S.E. Saskatchewan for proceeds of \$342,515.

On January 11, 2023, Source Rock paid a \$0.015 per share dividend to shareholders of record on December 30, 2022, which was approved by Source Rock's Board of Directors on December 15, 2022. This dividend was designated as an "eligible dividend" for Canadian income tax purposes.

On March 24, 2023, Source Rock closed the acquisition of a 5% GORR in land (oil mineral interests only) located in Alberta for proceeds of \$1,600,000, with an effective date of January 1, 2023. Oil production from the Alberta lands (net to the royalty payor's working interest) in January 2023 was 420 bbl/d (21 bbl/d of net royalty production to Source Rock). Source Rock received a capital commitment to conduct \$3.2 million of operations on the royalty lands prior to December 31, 2024.

On April 12, 2023, Source Rock announced a transition to a monthly dividend and declared an inaugural monthly dividend of \$0.0055 per share, to be paid in cash on May 15, 2023 to shareholders of record on April 28, 2023.

On April 14, 2023, Source Rock paid a \$0.015 per share dividend to shareholders of record on March 31, 2023, which was approved by Source Rock's Board of Directors on March 15, 2023. This dividend was designated as an "eligible dividend" for Canadian income tax purposes.