CONDENSED INTERIM CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

THREE MONTHS ENDED MARCH 31, 2022 AND 2021

PERPETUAL ENERGY INC.
Condensed Interim Consolidated Statements of Financial Position

As at	March 31, 2022	December 31, 2021
(*Cdn$ thousands unaudited*)		
Assets		
Current assets		
Cash	**$ –**	$ 1,090
Accounts receivable	**13,457**	11,671
Marketable securities (note 3)	**7,056**	2,409
Prepaid expenses and deposits	**591**	910
Risk management contracts (note 19)	**45**	682
	21,149	16,762
Property, plant and equipment (note 4)	**158,269**	153,620
Exploration and evaluation (note 5)	**7,168**	7,329
Right-of-use assets (note 6)	**1,035**	1,140
Total assets	**$ 187,621**	$ 178,851
Liabilities		
Current liabilities		
Accounts payable and accrued liabilities	**$ 17,691**	$ 32,223
Other liability (note 10)	**63**	63
Risk management contracts (note 19)	**10,678**	321
Royalty obligations (note 12)	**4,899**	4,697
Lease liabilities (note 13)	**770**	778
Decommissioning obligations (note 14)	**1,667**	1,327
	35,768	39,409
Term loan (note 9)	**2,478**	2,469
Revolving bank debt (note 8)	**9,553**	2,487
Other liability (note 10)	**2,825**	1,324
Senior notes (note 11)	**34,486**	34,189
Lease liabilities (note 13)	**1,163**	1,324
Decommissioning obligations (note 14)	**28,205**	31,600
Total liabilities	**114,478**	112,802
Equity		
Share capital (note 15)	**94,501**	94,809
Contributed surplus	**45,971**	45,731
Deficit	**(67,329)**	(74,491)
Total equity	**73,143**	66,049
Total liabilities and equity	**$ 187,621**	$ 178,851
Contingencies (note 7)		

See accompanying notes to the condensed interim consolidated financial statements.

/s/ Robert A. Maitland

Robert A. Maitland

Director

/s/ Geoffrey C. Merritt

Geoffrey C. Merritt

Director

PERPETUAL ENERGY INC.
Condensed Interim Consolidated Statements of Income (Loss) and Comprehensive Income (Loss)

	Three months ended March 31, **2022**	2021
(*Cdn$ thousands, except per share amounts, unaudited*)		
Revenue		
Oil and natural gas (note 17)	**$ 24,953**	$ 11,536
Royalties	**(3,242)**	(2,131)
	21,711	9,405
Unrealized gain (loss) risk management contracts (note 19)	**(10,994)**	436
Realized gain (loss) risk management contracts (note 19)	**280**	(1,374)
Gas over bitumen royalty credit	**–**	238
Other income (note 14)	**20**	168
	11,017	8,873
Expenses		
Production and operating	**3,659**	3,286
Transportation	**692**	690
Exploration and evaluation (note 5)	**18**	20
General and administrative (note 4a)	**2,079**	2,055
Share-based payments (note 16)	**614**	480
Depletion and depreciation (note 4 and 6)	**4,018**	2,986
Impairment reversal (note 4b)	**(7,400)**	–
Net income (loss) from operating activities	**7,337**	(644)
Finance expense (note 18)	**(4,799)**	(2,062)
Change in fair value of marketable securities (note 3)	**4,624**	–
Net income (loss) and comprehensive income (loss)	**7,162**	(2,706)
Net income (loss) per share (note 15f)		
Basic	**$ 0.11**	$ (0.04)
Diluted	**$ 0.10**	$ (0.04)

See accompanying notes to the condensed interim consolidated financial statements.

PERPETUAL ENERGY INC.
Condensed Interim Consolidated Statements of Changes in Equity (Deficiency)

	Share capital *(thousands)*	Share capital *($thousands)*	Contributed surplus	Deficit	Total equity
(Cdn$ thousands unaudited)					
Balance at December 31, 2021	63,567	$ 94,809	$ 45,731	$ (74,491)	$ 66,049
Net income	–	–	–	7,162	7,162
Change in shares held in trust (note 15 and 16)	(436)	(308)	–	–	(308)
Share-based payments (note 16)	–	–	240	–	240
Balance at March 31, 2022	**63,131**	**$ 94,501**	**$ 45,971**	**$ (67,329)**	**$ 73,143**

	Share capital *(thousands)*	Share capital *($thousands)*	Contributed surplus	Deficit	Total equity (deficiency)
(Cdn$ thousands unaudited)					
Balance at December 31, 2020	61,305	$ 97,333	$ 45,217	$ (155,612)	$ (13,062)
Net loss	–	–	–	(2,706)	(2,706)
Common shares issued (note 15 and 16)	1,225	283	(53)	–	230
Share-based payments (note 16)	–	–	105	–	105
Balance at March 31, 2021	**62,530**	**$ 97,616**	**$ 45,269**	**$ (158,318)**	**$ (15,433)**

See accompanying notes to the condensed interim consolidated financial statements.

PERPETUAL ENERGY INC.
Condensed Interim Consolidated Statements of Cash Flows

(*Cdn$ thousands, unaudited*)	Three months ended March 31, 2022	2021
Cash flows from operating activities		
Net income (loss)	**$ 7,162**	$ (2,706)
Adjustments to add (deduct) non-cash items:		
Other income (note 14)	**(20)**	(168)
Depletion and depreciation (note 4 and 6)	**4,018**	2,986
Share-based payments (note 16)	**240**	105
Unrealized (gain) loss risk management contracts (note 19)	**10,994**	(436)
Change in fair value of marketable securities (note 3)	**(4,624)**	–
Finance expense (note 18)	**3,747**	2,999
Impairment reversal (note 4b)	**(7,400)**	–
Oil and natural gas revenue in-kind (note 12)	**–**	(1,133)
Decommissioning obligations settled (note 14)	**665**	(115)
Change in non-cash working capital	**(8,510)**	150
Net cash flows from operating activities	**6,272**	1,682
Cash flows from (used in) financing activities		
Change in revolving bank debt, net of issue costs (note 8)	**6,858**	(329)
Change in senior notes, net of issue costs (note 11)	**–**	(219)
Payments of lease liabilities (note 13)	**(169)**	(145)
Payments of royalties (note 12)	**(1,393)**	(236)
Shares purchased and held in trust	**(308)**	–
Common shares issues, net of issue costs	**–**	230
Net cash flows from (used in) financing activities	**4,988**	(699)
Cash flows used in investing activities		
Capital expenditures	**(4,837)**	(3)
Acquisitions (note 4)	**–**	(625)
Net proceeds from dispositions (note 4(a))	**–**	156
Purchase of marketable securities (note 3)	**(23)**	–
Change in non-cash working capital	**(7,490)**	(511)
Net cash flows used in investing activities	**(12,350)**	(983)
Change in cash and cash equivalents	**(1,090)**	–
Cash and cash equivalents, beginning of period	**1,090**	–
Cash and cash equivalents, end of period	**$ –**	$ –

See accompanying notes to the condensed interim consolidated financial statements.

1. REPORTING ENTITY

Perpetual Energy Inc. ("Perpetual" or the "Company") is an oil and natural gas exploration, production, and marketing company headquartered in Calgary, Alberta. Perpetual owns a diversified asset portfolio, including liquids-rich conventional natural gas assets in the deep basin of West Central Alberta, heavy crude oil and shallow conventional natural gas in Eastern Alberta, and undeveloped bitumen leases in Northern Alberta.

The address of the Company's registered office is 3200, 605 – 5 Avenue S.W., Calgary, Alberta, T2P 3H5.

The condensed interim consolidated financial statements of the Company as at and for the three months ended March 31, 2022 are comprised of the accounts of Perpetual Energy Inc. and its wholly owned subsidiaries: Perpetual Operating Corp., Perpetual Energy Partnership, and Perpetual Operating Trust, which are incorporated in Alberta.

2. BASIS OF PREPARATION

These condensed interim consolidated financial statements have been prepared in accordance with IAS 34 Interim Financial Reporting and do not include all of the information required for full annual financial statements. These condensed interim consolidated financial statements should be read in conjunction with the Company's consolidated financial statements as at and for the year ended December 31, 2021 which were prepared in conformity with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board.

The accounting policies, basis of measurement, critical accounting judgements and significant estimates used to prepare the annual consolidated financial statements as at and for the year ended December 31, 2021 have been applied in the preparation of these condensed interim consolidated financial statements.

These condensed interim consolidated financial statements of the Company were approved and authorized for issue by the Board of Directors on May 4, 2022.

3. MARKETABLE SECURITIES

	Amount *($thousands)*
December 31, 2020	$ –
Plan of Arrangement Rubellite shares and warrants received (note 4)	9
Plan of Arrangement warrants exercised	118
AIMCo Bonus Shares received (note 9)	1,361
AIMCo Bonus Shares delivered (note 9)	(1,361)
Rubellite Share Purchase Warrants received (1)	2,000
Change in fair value of marketable securities	282
December 31, 2021	$ 2,409
Purchase	23
Change in fair value of marketable securities	4,624
March 31, 2022	**$ 7,056**

(1) The Company used the Black Scholes option pricing model to calculate the estimated fair value of the Rubellite Share Purchase Warrants at the date of grant using an expected volatility of 40%, risk-free interest rate of 1.2%, dividend yield of nil, contractual life of 5-years, share price at grant date of $2.00 and exercise price of $3.00. The fair value was $0.50 per Rubellite Share Purchase Warrant.

On September 3, 2021, the Plan of Arrangement involving Perpetual Energy Inc, the shareholders of Perpetual, and Rubellite Energy Inc ("Rubellite") (the "Arrangement") was completed following approval of the plan by the shareholders of Perpetual at its special shareholder meeting held on August 31, 2021 and the receipt of the final order of the Court of Queen's Bench of Alberta approving the Plan of Arrangement on September 3, 2021. Under the terms of the Arrangement, for every 46 common shares of Perpetual held, shareholders received 1 common share of Rubellite and 12 warrants to purchase Rubellite common shares ("Rubellite Warrants"). Each Rubellite Warrant entitled the holder to subscribe for one Rubellite common share at a price of $2.00 per share until October 4, 2021. Through it's employee trust, Perpetual received 4,500 Rubellite common shares and 54,000 Rubellite Warrants as part of the Plan of Arrangement. In 2021, Perpetual exercised its 54,000 Rubellite Warrants for $0.1 million in exchange for 54,000 Rubellite shares. As at March 31, 2022 the Company holds 58,500 Rubellite shares valued at $0.2 million using the Rubellite common share price of $3.82 per share.

Under the terms of the Plan of Arrangement, Perpetual also received 4.0 million Rubellite Share Purchase Warrants that were initially valued at $2.0 million when received and revalued to $6.8 million as at March 31, 2022. The Company used the Black Scholes pricing model to calculate the estimated fair value of the Rubellite Share Purchase Warrants.

The following assumptions were used to arrive at the estimate of fair value at period end:

	March 31, 2022
Dividend yield (%)	–
Expected volatility (%)	40%
Risk-free interest rate (%)	2.37%
Contractual life (years)	4.4
Share price	$3.82
Exercise price	$3.00
Fair value	$1.70

In 2021, upon completion of the Arrangement, Perpetual executed its agreement with its Term Loan lender for the settlement of principal and all interest owing on the Term Loan ("Second Line Loan Settlement"). As part of the Second Lien Loan Settlement Perpetual delivered the AIMCo Bonus Shares at a value of $1.4 million.

4. PROPERTY, PLANT AND EQUIPMENT ("PP&E")

	Oil and Gas Properties	Corporate Assets	Total
Cost			
December 31, 2020	$ 564,959	$ 7,652	$ 572,611
Additions	19,060	2	19,062
Acquisitions	1,325	–	1,325
Change in decommissioning obligations related to PP&E (note 14)	2,689	–	2,689
Transfers from exploration and evaluation (note 5)	2,943	–	2,943
Dispositions (a)	(16,442)	–	(16,442)
December 31, 2021	$ 574,534	$ 7,654	$ 582,188
Additions	4,830	7	4,837
Change in decommissioning obligations related to PP&E (note 14)	(3,836)	–	(3,836)
Transfers from exploration and evaluation (note 5)	161	–	161
March 31, 2022	**$ 575,689**	**$ 7,661**	**$ 583,350**
Accumulated depletion and depreciation			
December 31, 2020	$ (441,059)	$ (7,567)	$ (448,626)
Depletion and depreciation	(13,500)	(67)	(13,567)
Dispositions (a)	3,025	–	3,025
Impairment reversal (b)	30,600	–	30,600
December 31, 2021	$ (420,934)	$ (7,634)	$ (428,568)
Depletion and depreciation	(3,913)	–	(3,913)
Impairment reversal (b)	7,400	–	7,400
March 31, 2022	**$ (417,447)**	**$ (7,634)**	**$ (425,081)**
Carrying amount			
December 31, 2021	$ 153,600	$ 20	$ 153,620
March 31, 2022	**$ 158,242**	**$ 27**	**$ 158,269**

For the period ended March 31, 2022, $0.6 million (March 31, 2021 – $0.02 million) of direct general and administrative expenses were capitalized. Future development costs for the period ended March 31, 2022 of $71.5 million (December 31, 2021 – $75.3 million) were included in the depletion calculation.

a) Clearwater Assets Disposition

At the time of the Arrangement, Rubellite exchanged 1.4 million Rubellite common shares and 16.7 million arrangement warrants with Perpetual shareholders for 8.2 million Perpetual common shares valued at $2.8 million. These 8.2 million Perpetual common shares held by Rubellite were delivered to Perpetual as part of the purchase consideration.

The disposition of all of Perpetual's Clearwater lands, wells, roads and facilities in northeast Alberta (the "Clearwater Assets"), working capital and associated cash, and decommissioning obligations to Rubellite was accounted for as being effective for consideration of $65.5 million, including $53.6 million in promissory notes, paid in cash on October 5, 2021, and the assumption of $5.8 million of promissory notes due to 1974918 Alberta Ltd. (a company controlled by the Company's CEO ("CEO") ("197Co"), the issuance of 680,485 Rubellite common shares valued at $1.3 million ("AIMCo Bonus Shares"), the return of 8.2 million Perpetual common shares exchanged in the Arrangement valued at $2.8 million and issuance of warrants to purchase 4.0 million Rubellite common shares at a price of $3.00 per share for a period of five years, valued at $2.0 million.

Perpetual also entered into a Management and Operating Services Agreement ("MSA") with Rubellite whereby Perpetual receives payment for certain technical and administrative services provided to Rubellite on a cost recovery basis. For the three months ended March 31, 2022, the amount of general and administrative costs billed to Rubellite was $0.3 million. As a result of various other transactions between the parties under the MSA, at March 31, 2022, the Company recorded an accounts receivable of $1.8 million owing from Rubellite.

The consideration received, and calculation of the gain recorded on disposition is summarized below:

($ thousands)	
Proceeds from disposition (i)	**65,514**
Transaction costs and closing adjustments (ii)	**(583)**
Carrying amount of assets disposed (iii)	**(19,085)**
Carrying amount of net working capital disposed, including cash (iv)	**823**
Carrying amount of decommissioning obligations disposed (v)	**853**
Gain on disposition	**47,522**

i) Total consideration — $65.5 million of consideration as outlined below:

($ thousands)	
Promissory note issued by Rubellite to Perpetual(1)	**53,600**
PEI-197Co note assumed by Rubellite(2)	**5,773**
AIMCo Bonus Shares(3)	**1,361**
8.2 million Perpetual common shares(4)	**2,780**
Rubellite Share Purchase Warrants(5)	**2,000**
Total consideration received	**$ 65,514**

(1) Demand promissory note, secured by the Clearwater Assets, and settled on October 5, 2021.
(2) On July 15, 2021, Perpetual exercised an option to acquire certain E&E lands located at Figure Lake in exchange for a demand promissory note secured by the Figure Lake lands in the amount of $5.8 million owing to 197Co (note 5). The acquired Figure Lake lands comprised part of the Clearwater Assets sold to Rubellite. The secured promissory note obligation owing to 197Co was assigned by Perpetual to Rubellite as part of the total consideration.
(3) Rubellite shares issued to Perpetual on September 3, 2021 valued at $1.4 million.
(4) Rubellite returned to Perpetual 8.2 million Perpetual common shares valued at $2.8 million. Pursuant to the Plan of Arrangement, Perpetual shareholders exchanged 8.2 million Perpetual common shares with Rubellite for Rubellite common shares and warrants. The Perpetual shares received were subsequently cancelled.
(5) Represents the estimated value of 4.0 million Rubellite Share Purchase Warrants at $3.00 per share exercise price (note 3) valued at $2.0 million.

ii)	Transaction costs and closing adjustments	$0.6 million of transaction costs and closing adjustments.
iii)	Carrying amount of assets disposed	$19.1 million of assets including oil and gas properties ($16.1 million of costs less $2.8 million of accumulated depletion) and exploration and evaluation assets ($5.8 million).
iv)	Carrying amount of net working capital disposed	$0.8 million of net working capital including cash ($4.1 million), accounts receivable ($0.7 million), and accounts payable ($5.6 million).
v)	Carrying amount of decommissioning obligations disposed	$0.9 million of decommissioning obligations associated with oil and gas properties disposed.

b) Cash-generating units and impairment and impairment reversals

The Company identified an indicator of impairment reversal at March 31, 2022 for the Eastern Alberta cash generating unit and performed an impairment reversal test to estimate the recoverable amount of the CGU. It was determined the recoverable amount of the Eastern Alberta CGU exceeded the CGU's carrying value, resulting in all remaining Eastern Alberta impairment, net of depletion, of $7.4 million being reversed and included in net income. No historical impairments remain for the Eastern Alberta CGU.

At March 31, 2022, indicators of impairment reversal for the Eastern Alberta CGU were primarily a result of increased forecasted benchmark commodity prices which positively impacted operating cash flows. There were no internal or external indicators of impairment for the West Central CGU as at March 31, 2022. The estimated recoverable amount of the Eastern Alberta CGU was determined using the value-in-use methodology, based on the estimates of proved and probable oil and gas reserves and the related cash flows at March 31, 2022, as updated by internal reserve evaluators, along with forecasted oil and gas commodity prices based on an average of three independent third party reserve evaluators, and an estimate of market discount rates between 10% and 20% to consider risks specific to the Eastern Alberta CGU.

Forecasted oil and gas commodity prices based on an average of three independent third party reserve evaluators were used in the VIU calculation as at March 31, 2022:

Year	West Texas Intermediate ("WTI") Crude Oil *(US$/bbl)*	USD/CDN exchange rate *(US$/Cdn$)*	Alberta Heavy Crude Oil *(Cdn$/bbl)*	AECO Gas *(Cdn$/MMBtu)*	NYMEX Gas *(Cdn$/MMBtu)*
2022	94.53	1.25	95.13	5.13	5.48
2023	84.15	1.25	77.65	4.28	4.44
2024	77.51	1.25	70.24	3.69	3.75
2025	71.63	1.25	64.45	3.45	3.56
2026	73.06	1.25	65.74	3.52	3.63
2027	74.53	1.25	67.06	3.59	3.70
2028	76.02	1.25	68.40	3.66	3.77
2029	77.54	1.25	69.77	3.73	3.85
2030	79.09	1.25	71.16	3.81	3.93
2031	80.67	1.25	72.58	3.88	4.00
2032	82.28	1.25	74.04	3.96	4.08
2033	83.93	1.25	75.52	4.04	4.17
2034	85.61	1.25	77.03	4.12	4.25
2035	87.32	1.25	78.57	4.20	4.33
2036(1)	89.06	1.25	80.14	4.29	4.42

(1) Forecasted oil and gas commodity prices escalate 2.0% per year thereafter.

As at March 31, 2022, if discount rates used in the calculation of impairment reversal changed by 1% with all other variables held constant, the impairment reversal would be unchanged. As at March 31, 2022, if commodity price estimates changed by 5% with all other variables held constant, the impairment reversal would be unchanged.

During the year ended December 31, 2021, the Company reversed $30.6 million of historical impairments, net of depletion.

The Company identified an indicator of impairment reversal at June 30, 2021 for the West Central and Eastern Alberta cash generating units and additionally at December 31, 2021 for the Eastern Alberta CGU and performed impairment reversal tests to estimate the recoverable amount of each CGU. It was determined the recoverable amount of the West Central and Eastern Alberta CGUs exceeded each CGU's carrying value, resulting in all previous West Central impairment, net of depletion, of $22.6 million and Eastern Alberta impairment of $8.0 million, respectively, being reversed. No historical impairments remain for the West Central CGU.

5. EXPLORATION AND EVALUATION ("E&E")

	March 31, 2022	December 31, 2021
Balance, beginning of period	**$ 7,329**	$ 10,272
Acquisitions	**–**	5,773
Dispositions	**–**	(5,773)
Transfers to property, plant and equipment (note 4)	**(161)**	(2,943)
Balance, end of period	**$ 7,168**	$ 7,329

During the three months ended March 31, 2022, a nominal amount (Q1 2021 – a nominal amount) in costs were charged directly to E&E expense in the condensed interim consolidated statements of income (loss) and comprehensive income (loss).

On July 15, 2021, Perpetual exercised an option to acquire lands located at Figure Lake in exchange for a demand promissory note secured by the Figure Lake lands in the amount of $5.8 million owing to 197Co. The acquired Figure Lake lands comprised part of the Clearwater Assets sold to Rubellite. The secured promissory note obligation owing to 197Co was assigned by Perpetual to Rubellite as part of the disposition of the Clearwater Assets.

Impairment of E&E assets

E&E assets are tested for impairment both at the time of any triggering facts and circumstances as well as upon their eventual reclassification to oil and gas properties in PP&E.

At March 31, 2022, the Company transferred Mannville undeveloped land value to PP&E, at a value of $0.2 million, which was equal to the book value in E&E. As a result of the transfer and the impairment test required at transfer, there were no impairments recorded to E&E in the first quarter of 2022.

At March 31, 2021, the Company conducted an assessment of indicators of impairment and impairment reversal for the Company's E&E assets. There were no triggers identified and therefore, no impairments or impairment reversals recognized during the first quarter of 2021.

6. RIGHT-OF-USE ASSETS

The Company leases several assets including office space, vehicles, and other leases. Information about leases for which the Company is a lessee is presented below:

	Head office	Vehicles	Other leases	Total
Cost				
January 1, 2021	$ 1,591	$ 389	$ 247	$ 2,227
Additions	–	221	–	221
December 31, 2021	$ 1,591	$ 610	$ 247	$ 2,448
March 31, 2022	**$ 1,591**	**$ 610**	**$ 247**	**$ 2,448**
Accumulated depreciation				
January 1, 2021	$ (497)	$ (215)	$ (143)	$ (855)
Depreciation	(258)	(134)	(61)	(453)
December 31, 2021	$ (755)	$ (349)	$ (204)	$ (1,308)
Depreciation	(64)	(34)	(7)	(105)
March 31, 2022	**$ (819)**	**$ (383)**	**$ (211)**	**$ (1,413)**
Carrying amount				
December 31, 2021	$ 836	$ 261	$ 43	$ 1,140
March 31, 2022	**$ 772**	**$ 227**	**$ 36**	**$ 1,035**

7. CONTINGENCIES

On August 3, 2018, the Company received a Statement of Claim that was filed by PricewaterhouseCoopers Inc. LIT ("PwC"), in its capacity as trustee in bankruptcy (the "Trustee") of Sequoia Resources Corp. ("Sequoia"), with the Alberta Court of Queen's Bench (the "Court"), against Perpetual (the "Sequoia Litigation"). The claim relates to a six-year-old transaction when, on October 1, 2016, Perpetual closed the disposition of shallow conventional natural gas assets in Eastern Alberta to an arm's length third party at fair market value at the time after an extensive and lengthy marketing, due diligence, and negotiation process (the "Sequoia Disposition"). This transaction was one of several completed by Sequoia. Sequoia assigned itself into bankruptcy on March 23, 2018. PwC is seeking an order from the Court to either set this transaction aside or declare it void, or damages of approximately $217 million. On August 27, 2018, Perpetual filed a Statement of Defence and Application for Summary Dismissal with the Court in response to the Statement of Claim. All allegations made by PwC have been denied and applications to the Court to dismiss all claims has been made on the basis that there is no merit to any of them.

On January 13, 2020, the Court issued its written decision related to the Sequoia Disposition. The decision dismissed and struck all claims against the Company's CEO and all but one of the claims filed against Perpetual. The Court did not find that the test for summary dismissal relating to whether the asset transaction was an arm's length transfer for purposes of section 96(1) of the Bankruptcy and Insolvency Act (the "BIA") was met, on the balance of probabilities. Accordingly, the BIA claim was not dismissed or struck and only that part of the claim could continue against Perpetual. The Trustee filed a notice of appeal with the Court of Appeal of Alberta, challenging the entire decision, and Perpetual filed a similar notice of appeal contesting the BIA claim portion of the decision (the "First Appeal").

On February 25, 2020, Perpetual filed a second application to strike and summarily dismiss the BIA claim on the basis that there was no transfer at undervalue, and Sequoia was not insolvent at the time of the asset transaction nor caused to be insolvent by the asset transaction (the "Second Summary Dismissal Application"). In July 2020, the Orphan Well Association ("OWA"), certain oil and gas companies, and six municipalities applied to intervene in the second BIA dismissal application proceedings. The OWA and certain oil and gas companies were permitted to intervene (the "Intervenors") in the proceedings which took place on October 1 and 2, 2020. The Intervenors were also permitted to intervene in the First Appeal proceedings. On January 14, 2021 the Court issued its decision, finding that the Trustee could not establish a necessary element of the BIA Claim as Sequoia was not insolvent at the time of, nor rendered insolvent by, the Sequoia Disposition. The Court therefore concluded there is "no merit" to the BIA Claim and it summarily dismissed the balance of the Statement of Claim. The Trustee appealed this decision, and the Court of Appeal hearing took place on February 10, 2022, with the panel reserving judgement. On March 25, 2022, the Court of Appeal issued their judgement with respect to this matter and allowed PwC's appeal on the basis that the Court of Queen's Bench erred in law in its handling of the end-of-life obligations and that based on the record, it could not be concluded the error was without consequence, and that the Court of Queen's Bench also erred in agreeing to hear the Second Summary Dismissal Application. On this basis, the BIA Claim has been directed to trial.

The First Appeal proceedings were heard on December 10, 2020. On January 25, 2021, the Court of Appeal of Alberta issued their judgement with respect to the First Appeal proceedings, dismissing the appeal filed by Perpetual and granting certain aspects of the appeals filed by the Trustee, thereby reinstating certain elements of the Sequoia Litigation for trial. On March 24, 2021, Perpetual applied for leave to appeal the First Appeal decision to the Supreme Court of Canada (the "SCC"). On July 8, 2021, the SCC dismissed Perpetual's application.

Management expects that the Company is more likely than not to be completely successful in defending against the Sequoia Litigation such that no damages will be awarded against it, and therefore, no amounts have been accrued as a liability in these financial statements.

8. REVOLVING BANK DEBT

As at March 31, 2022, the Company's Credit Facility had a Borrowing Limit of $17.0 million (December 31, 2021 – $17.0 million) under which $9.6 million was drawn (December 31, 2021 – $2.5 million) and $1.0 million of letters of credit had been issued (December 31, 2021 – $1.0 million). Borrowings under the Credit Facility bear interest at its lenders' prime rate or Banker's Acceptance rates, plus applicable margins and standby fees. The applicable Banker's Acceptance margins range between 3.0% and 5.5%. The effective interest rate on the Credit Facility at March 31, 2022 was

5.9%. For the period ended March 31, 2022 if interest rates changed by 1% with all other variables held constant, the impact on annual cash finance expense and net income would be $0.1 million.

During the third quarter of 2021, Perpetual entered into an agreement with its syndicate of lenders to extend its Credit Facility maturity to November 30, 2022 with the opportunity to extend the revolving period for a further six months subject to approval by the syndicate. If not extended on or before November 30, 2022 all outstanding advances will be repayable on May 31, 2023.

During the fourth quarter of 2021, the Credit Facility borrowing limit was reduced from $20.0 million to $17.0 million and on December 17, 2021 the semi-annual borrowing base redetermination of the Company's Credit Facility was completed and the existing $17.0 million borrowing limit and term of the credit facility was maintained. The next borrowing limit redetermination is scheduled to occur on or before May 31, 2022.

The Credit Facility is secured by general first lien security agreements covering all present and future property of the Company and its subsidiaries. The Credit Facility also contains provisions which restrict the Company's ability to repay Term Loan and senior note principal and interest, and to pay dividends on or repurchase its common shares.

At March 31, 2022, the Credit Facility was not subject to any financial covenants and the Company was in compliance with all customary non-financial covenants.

9. TERM LOAN

			March 31, 2022		December 31, 2021	
	Maturity date	**Interest rate**	**Principal**	**Carrying Amount**	Principal	Carrying amount
Term loan	December 31, 2024	8.1%	**$ 2,671**	**$ 2,478**	$ 2,671	$ 2,469

During the third quarter of 2021, Perpetual executed its agreement with its Term Loan lender for the settlement of principal and all interest owing on the Term Loan. Perpetual substantively modified the previous Term Loan with Alberta Investment Management Corporation ("AIMCo") in exchange for the payment of approximately $38.5 million in cash, the delivery by Perpetual of the AIMCo Bonus Shares at a value of $1.4 million, the issuance of a new $2.7 million second lien Term Loan (the "New Term Loan"), and up to an aggregate $4.5 million in contingent payments over the three year period ended June 30, 2024 in the event that Perpetual's annual average realized oil and natural gas prices exceed certain thresholds initially valued at $0.2 million (the "Second Lien Loan Settlement") (note 10). The New Term Loan bears interest at 8.1% annually, which Perpetual may elect to pay-in-kind and will mature on December 31, 2024. Perpetual has the ability to repay the Term Loan at any time without any repayment penalty. All amounts related to the Second Lien Loan Settlement were paid on October 5, 2021.

The New Term Loan has a cross-default provision with the Credit Facility and contains substantially similar provisions and covenants as the Credit Facility (note 8). The Term Loan is secured by a general security agreement over all present and future property of the Company and its subsidiaries on a second priority basis, subordinate only to liens securing loans under the Credit Facility.

At March 31, 2022, the Term Loan was not subject to any financial covenants and the Company was in compliance with all customary non-financial covenants.

10. OTHER LIABILITY

Pursuant to the terms of the Second Lien Loan Settlement, Perpetual was committed to pay up to $4.5 million in potential contingent payments in the event that the Company's annual average realized crude oil and natural gas prices exceed certain thresholds in each of the annual periods ended December 31, 2023. The payment for 2021 was capped at $1.3 million; the payment for 2022 is capped at $1.3 million; and the payment for 2023 is capped at $1.9 million. Of the 2021 payment cap, only $0.2 million was earned. This leaves a maximum remaining total obligation to be earned in 2022 and 2023 of $3.2 million. At March 31, 2022, the Company estimated the maximum total obligation owing to be $3.4 million, and after discounting the fair value of the contingent liability was recorded as $2.9 million. The change in fair value of this liability was recorded as a non-cash finance expense in the statements of income (loss) and comprehensive income (loss).

The table below summarizes the change in fair value of the contingent payments:

	March 31, 2022	December 31, 2021
Balance, beginning of period	**$ 1,387**	$ –
Initial recognition	**–**	228
Change in fair value	**1,501**	1,159
Balance, end of period	**$ 2,888**	$ 1,387

	March 31, 2022	December 31, 2021
Current	**$ 63**	$ 63
Non-current	**2,825**	1,324
Total other liability	**$ 2,888**	$ 1,387

The Company has designated the other liability as financial liabilities which are measured at fair value through profit and loss, estimated by discounting potential contingent payments. For the three months ended March 31, 2022, an unrealized loss of $1.5 million (Q1 2021 – nil) is included in non-cash finance expense related to the change in fair value of other liability (note 18).

At March 31, 2022, if forecasted natural gas commodity prices changed by $0.25 per GJ with all other variables held constant, the fair value of the total other liability and net income for the period would change by nil as the maximum remaining obligation has been met and this movement would not reduce the remaining obligation to less than it's maximum. If forecasted crude oil commodity prices changed by $5.00 per bbl with all other variables held constant, the fair value of the other liability and net income for the period would also change by nil for the same reason.

11. SENIOR NOTES

			March 31, 2022		December 31, 2021	
	Maturity date	**Interest rate**	**Principal**	**Carrying Amount**	Principal	Carrying amount
Senior notes	January 23, 2025	8.75%	**$ 36,583**	**$ 34,486**	$ 36,583	$ 34,189

On January 22, 2021, Perpetual announced the completion of a Court-approved plan of arrangement whereby the unsecured 2022 Senior Notes were exchanged for new 8.75% secured third lien notes due January 23, 2025. The 2025 Senior Notes have been issued under a trust indenture that contains substantially the same terms as the 2022 Senior Notes, other than the 2025 Senior Notes are secured on a third lien basis and allow for the semi-annual interest payments to be paid at Perpetual's option, in cash, or in additional 2025 Senior Notes (a "PIK Interest Payment"). In 2021, the Company elected to pay the semi-annual interest payments of $1.5 million by making PIK Interest Payments, increasing the principal amount to $36.6 million.

The Company satisfied the January 23, 2022 semi-annual interest payment of $1.6 million by making a cash payment.

At March 31, 2022, the senior notes are recorded at the present value of future cash flows, net of $2.1 million in issue and principal discount costs which are amortized over the remaining term using a weighted average effective interest rate of 13.7%

The senior notes are direct senior secured, third lien obligations of the Company. The Company may redeem the senior notes without any repayment penalty. The senior notes have a cross-default provision with the Company's Credit Facility. In addition, the senior notes indenture contains restrictions on certain payments including dividends, retirement of subordinated debt, and stock repurchases.

At March 31, 2022, the senior notes were not subject to any financial covenants and the Company was in compliance with all customary non-financial covenants.

Entities controlled by the Company's CEO hold $15.9 million of the 2025 Senior Notes outstanding. An entity that is associated with the Company's CEO, and entities associated with other Directors of the Company hold an additional $10.3 million and $0.8 million of the 2025 Senior Notes outstanding, respectively.

12. ROYALTY OBLIGATIONS

	Retained East Edson royalty obligation	**Gas over bitumen royalty financing**	**Total**
December 31, 2020	$ 5,714	$ 435	$ 6,149
Cash payments[1]	–	(558)	(558)
Non-cash payments in-kind	(4,995)	–	(4995)
Change in fair value (note 18)	3,978	123	4,101
December 31, 2021	4,697	–	4,697
Cash payments	(1,393)	–	(1,393)
Change in fair value (note 18)	1,595	–	1,595
March 31, 2022	**$ 4,899**	**$ –**	**$ 4,899**

(1) The final payment related to the gas over bitumen royalty financing was made on July 25, 2021.

The retained East Edson royalty obligation formed part of the net consideration received by Perpetual following the disposition transaction in 2020, whereby Perpetual agreed to retain the purchaser's 50% working interest in the existing gross overriding royalty obligation on the property, equivalent to 2.8 MMcf/d of natural gas and associated NGL production for the period April 1, 2020 to December 31, 2022. Prior to November 1, 2021, the retained East Edson royalty obligation was paid in-kind, and settled through non-cash delivery of contractual natural gas and NGL volumes to the royalty holder. As of November 1, 2021, the royalty obligation is settled through payment in cash.

The Company has designated the retained East Edson royalty obligation and the gas over bitumen royalty financing as financial liabilities which are measured at fair value through profit and loss, estimated by discounting future royalty obligations based on forecasted natural gas and NGL commodity prices multiplied by the royalty obligation volumes. For the three months ended March 31, 2022, an unrealized loss of $1.6 million (Q1 2021 – unrealized loss of $1.1 million) is included in non-cash finance expense related to the change in fair value of total royalty obligations (note 18).

As at March 31, 2022, if forecasted natural gas commodity prices changed by $0.25 per GJ with all other variables held constant, the fair value of the total royalty obligations and net income for the period would change by $0.2 million.

13. LEASE LIABILITIES

	March 31, 2022	December 31, 2021

Balance, beginning of period	**$**	**2,102**	$	2,501
Additions		**–**		221
Interest on lease liabilities (note 18)		**32**		148
Payments		**(201)**		(768)
Total lease liabilities	**$**	**1,933**	$	2,102
Current	**$**	**770**	$	778
Non-current		**1,163**		1,324
Total lease liabilities	**$**	**1,933**	$	2,102

Lease terms are negotiated on an individual basis and contain a wide range of terms and conditions. Incremental borrowing rates used to measure the present value of the future lease payments at March 31, 2022 were between 4.3% and 6.6% (2021 – 4.3% and 6.6%).

14. DECOMMISSIONING OBLIGATIONS

The following significant assumptions were used to estimate decommissioning obligations:

		March 31, 2022		December 31, 2021
Obligations incurred, including acquisitions	**$**	**161**	$	965
Change in risk free interest rate		**(3,293)**		(1,309)
Change in estimates		**(704)**		3,033
Change in decommissioning obligations related to PP&E (note 4)		**(3,836)**		2,689
Obligations settled (cash)		**665**		(1,760)
Obligations settled[(1)] (non-cash)		**(20)**		(704)
Obligations disposed (note 4(a)(v))		**-**		(853)
Accretion (note 18)		**136**		531
Change in decommissioning obligations		**(3,055)**		(97)
Balance, beginning of period		**32,927**		33,024
Balance, end of period	**$**	**29,872**	$	32,927
Decommissioning obligations – current	**$**	**1,667**	$	1,327
Decommissioning obligations – non-current		**28,205**		31,600
Total decommissioning obligations	**$**	**29,872**	$	32,927

(1) During the three months ended March 31, 2022, obligations settled (non-cash) of a nominal amount (Q1 2021 – $0.2 million) were funded by payments made directly to Perpetual's service providers from the Alberta Site Rehabilitation Program. These amounts have been recorded as other income.

Decommissioning obligations are estimated based on the Company's net ownership interest in all wells and facilities, estimated costs to reclaim and abandon these wells and facilities, and the estimated timing of the costs to be incurred in future periods.

The increase in the provision due to the passage of time, which is referred to as accretion, is recognized as non-cash finance expense in the condensed interim consolidated statements of income (loss) and comprehensive income (loss). Decommissioning obligations are further adjusted at each period end date for changes in the risk-free interest rate, after considering additions and dispositions of PP&E. Decommissioning obligations are also adjusted for revisions to future cost estimates and the estimated timing of costs to be incurred in future periods.

The following significant assumptions were used to estimate the Company's decommissioning obligations:

	March 31, 2022	December 31, 2021
Undiscounted obligations	**$ 33,057**	$ 32,254
Average risk-free rate	**2.4%**	1.7%
Inflation rate	**1.8%**	1.8%
Expected timing of settling obligations	**1 to 25 years**	1 to 25 years

15. SHARE CAPITAL

	March 31, 2022		December 31, 2021	
	Shares ***(thousands)***	**Amount** ***($thousands)***	Shares *(thousands)*	Amount *($thousands)*
Balance, beginning of period	**63,567**	**$ 94,809**	61,305	$ 97,333
Issued pursuant to share-based payment plans	**–**	**–**	1,828	243
Shares held in trust purchased (b)	**(436)**	**(308)**	(542)	(191)
Shares held in trust issued (b)	–	**–**	566	168
Treasury shares issued (c)	–	**–**	1,000	230
Shares held in trust sold pursuant to the Plan of Arrangement (d)	–	**–**	189	9
Shares held in trust split pursuant to the Plan of Arrangement (d)	–	**–**	(189)	–
Common share split (d)	–	**–**	8,158	–
Common share cancellation (d)	–	**–**	(8,158)	(2,779)
Common share odd-lot consolidation (e)	–	**–**	(590)	(204)
Balance, end of period	**63,131**	**$ 94,501**	63,567	$ 94,809

a) Authorized

Authorized capital consists of an unlimited number of common shares.

b) Shares held in trust

The Company has compensation agreements in place with employees whereby they may be entitled to receive shares of the Company purchased on the open market by a trustee (note 16). Share capital is presented net of the number and cumulative purchase cost of shares held by the trustee that have not yet been issued to employees. As at March 31, 2022, 1.0 million shares were held in trust (December 31, 2021 – 0.5 million).

c) Treasury shares issued

During the first quarter of 2021, 1.0 million common shares were issued to an Officer of the Company for $0.2 million of cash consideration at a price of $0.23 per share, representing the volume weighted average trading price of the shares for the 5 day period immediately preceding the issuance.

d) Common share split and common share cancellation

As part of the Plan of Arrangement, 8.2 million Perpetual common shares were received by Rubellite from Perpetual shareholders in exchange for Rubellite common shares and warrants, and Perpetual split its shares by a ratio such that the number of Perpetual shares exchanged to Rubellite was equal to the number of shares split. On September 3, 2021, Perpetual received 8.2 million Perpetual common shares held by Rubellite as part of the consideration for the disposition of the Clearwater Assets and these shares were cancelled.

e) Common share odd-lot consolidation

Pursuant to steps in the Plan of Arrangement, Perpetual consolidated its common shares on the basis of 1,000 to 1 (the "Consolidation") and subsequently split the Common Shares on the same ratio. Shareholders who owned a number of common shares less than 1 subsequent to the consolidation and preceding the split (the "Consolidated Shareholders") were paid an amount in cash of $0.3419 per pre consolidated common share, being the volume weighted average trading price of the common shares on the Toronto Stock Exchange for the 20-day period prior to the effective date. Based on the ratio, 590,000 Common Shares were cancelled as a result of the Consolidation and Perpetual paid an aggregate of $0.2 million to the Consolidated Shareholders.

f) Per share information

	Three months ended March 31,	
	2022	2021
(*thousands, except per share amounts*)		
Net income (loss) – basic	**$ 7,162**	$ (2,706)
Effect of dilutive securities	**–**	–
Net income (loss) – diluted	**$ 7,162**	$ (2,706)
Weighted average shares		
Issued common shares	**64,099**	62,159
Effect of shares held in trust	**(883)**	(556)
Weighted average common shares outstanding – basic	**63,216**	61,603
Weighted average common shares outstanding – diluted[1]	**74,348**	61,603
Net income (loss) per share – basic	**$ 0.11**	$ (0.04)
Net income (loss) per share – diluted	**$ 0.10**	$ (0.04)

(1) For the three months ended March 31, 2022, 5.5 million potentially issuable common shares through the share-based compensation plans were excluded as they were not dilutive (Q1 2021 – 18.2 million).

16. SHARE-BASED PAYMENTS

The components of share-based payment expense are as follows:

	Three months ended March 31,	
	2022	2021
Share options	**$ 22**	$ 29
Performance share rights	**439**	413
Compensation awards	**153**	38
Share-based payments	**$ 614**	$ 480

The following tables summarize information about options, rights, and awards outstanding:

	Compensation awards					
(thousands)	**Deferred options**	**Deferred shares**	**Share options**	**Performance share rights[1]**	**Restricted rights**	**Total**
December 31, 2020	5,057	2,401	5,397	3,420	–	16,275
Granted	2,448	1,367	1,258	1,715	1,436	8,224
Exercised for common shares	–	–	(398)	N/A	(1,428)	(1,826)
Exercised for shares held in trust	(198)	(161)	–	–	–	(359)
Exercised for restricted rights	(303)	(278)	–	(855)	–	(1,436)
Performance adjustment[4]	–	–	–	(855)	–	(855)
Cancelled/forfeited	(1,090)	(151)	(455)	(360)	(8)	(2,064)
Expired	(438)	(20)	(1,725)	–	–	(2,183)
December 31, 2021	5,476	3,158	4,077	3,065	–	15,776
Granted[2][3]	38	66	35	718	–	857
March 31, 2022	**5,514**	**3,224**	**4,112**	**3,783**	**–**	**16,633**

(1) Certain performance share rights contain monetary awards that may be settled in cash, in common shares of the Company, or a combination thereof at the discretion of the Board of Directors, equal to the monetary amount at the time of vesting. These awards are accounted for as cash-settled share-based payments in which the fair value of the amounts payable under the plan are recognized incrementally as an expense over the vesting period, with a corresponding change in liabilities. As at March 31, 2022, $0.6 million had been accrued pursuant to cash-settled share-based payment awards (December 31, 2021 – $0.3 million).

(2) Share options granted during the three months ended March 31, 2022 have an exercise price of $0.92 and vest evenly over four years, with expiry occurring five years after issuance. The Company used the Black Scholes option pricing model to calculate the estimated fair value of the outstanding deferred options and share options at the date of grant. Expected volatility of 60% and forfeiture rates of 5% were used to value the share options.

(3) During the three months ended March 31, 2022, 0.04 million deferred options, 0.1 million deferred shares, 0.04 million share options, and 0.7 million performance share rights, and were granted to Officers, Directors, and employees of the Company.

(4) Performance share rights are subject to a performance multiplier of 0.5 to 2.0.

17. REVENUE

The Company sells its production pursuant to fixed or variable price contracts. The transaction price for variable priced contracts is based on the commodity price, adjusted for quality, location, or other factors, whereby each component of the pricing formula can be either fixed or variable, depending on the contract terms. Under the contracts, the Company is required to deliver fixed or variable volumes of conventional natural gas, heavy crude oil or NGL as may be applicable to the contract counterparty. Revenue is recognized when a unit of production is delivered to the contract counterparty. The amount of revenue recognized is based on the agreed transaction price, whereby any variability in revenue relates specifically to the Company's efforts to transfer production, and therefore the resulting revenue is allocated to the production delivered in the period during which the variability occurs. As a result, none of the variable revenue is considered constrained.

Conventional natural gas, heavy crude oil and NGL are mostly sold under contracts of varying price and volume terms of up to one year. Revenues are typically collected on the 25th day of the month following production.

Natural gas volumes sold pursuant to the Company's market diversification contract are sold at fixed volume obligations and priced at daily index prices plus US$0.02/MMBtu until October 31, 2022 and less US$0.08/MMBtu thereafter, less transportation costs from AECO to each market price point as detailed in the table below.

In the first quarter of 2022, the Company eliminated 10,000 MMBtu/d of fixed volume obligations for the period commencing November 1, 2022 and ending on March 31, 2023 and will receive payment of $1.2 million over the term of the associated contract volumes. The amount was recognized as a realized gain on risk management contracts (note 19).

In the first quarter of 2021, the Company eliminated its remaining fixed volume obligations of 10,000 MMBtu/d for the period commencing April 1, 2021 and ending on October 31, 2021 in consideration for the payment of $1.4 million over the term of the associated contract volumes. The amount was recognized as a realized loss on risk management contracts (note 19).

In the third quarter of 2021, the Company eliminated its remaining fixed volume obligations of 25,400 MMBtu/d for the period commencing April 1, 2022 and ending on October 31, 2022 in consideration for the payment of $1.8 million over the term of the associated contract volumes.

Market/Pricing Point	**November 1, 2022 to March 31, 2023 Daily sales volume *(MMBtu/d)***	**April 1, 2023 to October 31, 2024 Daily sales volume *(MMBtu/d)***
Malin	5,000	15,000
Dawn	15,000	15,000
Emerson	10,000	10,000
Total sales volume obligation	**30,000**	**40,000**

Subsequent to March 31, 2022, the Company eliminated 5,000 MMBtu/d of fixed volume obligations for the period commencing November 1, 2022 and ending March 31, 2023, and will receive payment of $0.8 million over the term of the associated contract volumes.

The following table presents the Company's oil and natural gas sales disaggregated by revenue source:

	Three months ended March 31, **2022**	2021
Oil and natural gas revenue		
Natural gas	**$ 15,929**	$ 6,022
Oil	**5,861**	4,032
NGL	**3,163**	1,482
Total oil and natural gas revenue	**$ 24,953**	$ 11,536

(1) For the three months ended March 31, 2022, natural gas revenue includes $1.4 million cash revenue (Q1 2021 – $1.1 million non-cash revenue taken in-kind) related to production used in the settlement of the retained East Edson royalty obligation (note 12).

Included in accounts receivable at March 31, 2022 is $9.2 million of accrued oil and natural gas revenue related to March 2022 production (December 31, 2021 – $7.0 million related to December 2021 production).

18. FINANCE EXPENSE

The components of finance expense are as follows:

	Three months ended March 31, 2022	2021
Cash finance expense		
Interest on revolving bank debt	**$ 162**	$ 276
Interest on term loan	**54**	–
Interest on 2025 Senior Notes[(1)]	**804**	–
Interest on 2022 Senior Notes[(2)]	**–**	(1,253)
Interest on lease liabilities (note 13)	**32**	40
Total cash finance expense	**$ 1,052**	$ (937)
Non-cash finance expense		
Interest paid in-kind on term loan (note 9)	**–**	948
Interest paid in-kind on 2025 Senior Notes (note 11)[(2)]	**–**	2,057
Gain on senior note maturity extension (note 11)	**–**	(1,591)
Amortization of debt issue costs	**515**	378
Accretion on decommissioning obligations (note 14)	**136**	98
Change in fair value of other liability (note 10)	**1,501**	–
Change in fair value of royalty obligations (note 12)	**1,595**	1,109
Total non-cash finance expense	**$ 3,747**	$ 2,999
Finance expenses recognized in net income (loss)	**$ 4,799**	$ 2,062

(1) The Company satisfied the January 23, 2022 semi-annual interest payment of $1.6 million by making a cash payment.

(2) On January 22, 2021, Perpetual's 2022 Senior Notes were exchanged for 2025 Senior Notes, providing Perpetual the option to pay interest in-kind. Perpetual elected to pay the January 23, 2021 semi-annual interest of $1.5 million by a PIK Interest Payment. As a result, the previously accrued 2022 Senior Notes cash interest of $1.3 million was reversed and replaced by $1.3 million of 2025 Senior Note non-cash interest expense. The Company satisfied the semi-annual interest payment due July 23, 2021 by making a PIK Interest Payment and accrued $0.8 million of non-cash interest expense for the three months ended March 31, 2021.

19. FINANCIAL RISK MANAGEMENT

Natural gas contracts

At March 31, 2022 the Company had entered into the following financial fixed price natural gas sales arrangements at AECO:

Term	Sold/bought	Volumes (*GJ/d*)	Average price (*$/GJ*)	Fair Value (*$ thousands*)
April 2022	Bought	5,000	4.22	41
April 2022	Sold	5,000	4.52	4
April 2022 – December 2022	Sold	2,500	3.57	(1,121)
April 2022 – September 2022	Sold	17,500	3.66	(4,401)
October 2022 – December 2022	Sold	5,000	4.53	(414)
January 2023 – December 2023	Sold	5,000	4.62	(431)

Natural gas contracts - sensitivity analysis

As March 31, 2022, if future natural gas prices changed by $0.25 per GJ with all other variables held constant, net income for the period would change by $1.2 million due to changes in the fair value of risk management contracts. Fair value sensitivity was based on published forward AECO prices.

Oil contracts

At March 31, 2022, the Company had entered the following financial fixed price oil sales arrangements which settle in CAD$:

Term	Volumes (*bbls/d*)	Western Canadian Select ("WCS") (CAD*$/bbl*)	Fair Value (*$ thousands*)
April 2022 – June 2022	200	76.70	(833)
July 2022 – December 2022	200	70.80	(1,020)
April 2022 – December 2022	200	70.66	(2,006)

Term	Volumes (*bbls/d*)	WTI Fixed Price (CAD*$/bbl*)	Fair Value (*$ thousands*)
April 2022 – June 2022	100	104.50	(164)
July 2022 – December 2022	100	103.30	(195)

Term	Volumes (*bbls/d*)	WTI-WCS differential (CAD*$/bbl*)	Fair Value (*$ thousands*)
April 2022 – December 2022	100	(17.25)	(57)
January 2023 – December 2023	100	(17.30)	(36)

Oil contracts - sensitivity analysis

As at March 31, 2022, if future WCS oil prices changed by CAD$5.00 per bbl with all other variables held constant, net income for the period would change by $0.6 million due to changes in the fair value of risk management contracts.

As at March 31, 2022, if future WTI oil prices changed by CAD$5.00 per bbl with all other variables held constant, net income for the period would change by $0.1 million due to changes in the fair value of risk management contracts.

As at March 31, 2022, if future WTI-WCS differential oil prices changed by CAD$5.00 per bbl with all other variables held constant, net income for the period would change by $0.3 million due to changes in the fair value of risk management contracts.

The following table summarizes the risk management contracts by type:

	March 31, 2022	December 31, 2021
Financial natural gas contracts	**(6,322)**	682
Financial oil contracts	**(4,311)**	(321)
Risk management contracts	**$ (10,633)**	$ 361
Risk management contracts – current asset	**45**	682
Risk management contracts – current liability	**(10,678)**	(321)
Risk management contracts	**$ (10,633)**	$ 361

The following table details the gains (losses) on risk management contracts:

	Three months ended March 31, 2022	2021
Unrealized loss on financial natural gas contracts	**$ (7,004)**	$ –
Unrealized gain on physical natural gas contracts	**–**	905
Unrealized loss on financial oil contracts	**(3,990)**	–
Unrealized loss on physical oil contracts	**–**	(469)
Unrealized gain (loss) on risk management contracts	**$ (10,994)**	$ 436
Realized gain (loss) on financial natural gas contracts[(1)]	**1,267**	(1,374)
Realized loss on financial oil contracts	**(987)**	–
Realized gain (loss) on risk management contracts	**$ 280**	$ (1,374)
Net loss on risk management contracts	**$ (10,714)**	$ (938)

(1) Includes realized gain of $1.2 million for the three months ended March 31, 2022 (Q1 2021 – realized loss of $1.4 million) from the elimination of the Company's market diversification contract obligations.

Fair value of financial assets and liabilities

The Company's fair value measurements are classified into one of the following levels of the fair value hierarchy:

Level 1 – inputs represent unadjusted quoted prices in active markets for identical assets and liabilities. An active market is characterized by a high volume of transactions that provides pricing information on an ongoing basis.

Level 2 – inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly or indirectly. These valuations are based on inputs that can be observed or corroborated in the marketplace, such as market interest rates or forecasted commodity prices.

Level 3 – inputs for the asset or liability are not based on observable market data.

The Company aims to maximize the use of observable inputs when preparing calculations of fair value. Classification of each measurement into the fair value hierarchy is based on the lowest level of input that is significant to the fair value calculation.

The fair value of cash and cash equivalents, accounts receivable, prepaid expenses and deposits, and accounts payable and accrued liabilities approximate their carrying amounts due to their short terms to maturity. The Credit Facility bears interest at a floating market rate, and accordingly, the fair market value approximates the carrying amount.

The fair value of the other liability is estimated by discounting future cash payments based on Perpetual's annual average realized oil and natural gas prices exceeding certain thresholds. This fair value measurement is classified as level 3 as significant unobservable inputs, including the discount rate and Perpetual's forecasted annual average realized oil and natural gas prices, are used in determination of the carrying amount. A discount rate of 8.1% was determined on inception of the agreement based on the characteristics of the instrument.

The fair value of the royalty obligations is estimated by discounting future cash payments based on the forecasted natural gas and NGL commodity prices multiplied by the royalty volumes. This fair value measurement is classified as level 3 as significant unobservable inputs, including the discount rate and forecasted natural gas and NGL commodity prices, are used in determination of the carrying amount. Discount rates of 12.0% to 12.2% were determined on inception of the agreements based on the characteristics of the instruments.

The fair value of financial assets and liabilities, excluding working capital, is attributable to the following fair value hierarchy levels:

				Fair value		
As at March 31, 2022	**Gross**	**Netting[1]**	**Carrying Amount**	**Level 1**	**Level 2**	**Level 3**
Financial assets						
Fair value through profit and loss						
Marketable securities	7,056	–	7,056	–	7,056	–
Risk management contracts	45	–	45	–	45	–
Financial liabilities						
Financial liabilities at amortized cost						
Revolving bank debt	(9,553)	–	(9,553)	(9,553)	–	–
Senior notes	(34,486)	–	(34,486)	–	(34,486)	–
Term loan	(2,478)	–	(2,478)	–	–	(2,478)
Fair value through profit and loss						
Other liability	(2,888)	–	(2,888)	–	–	(2,888)
Risk management contracts	(10,678)	–	(10,678)	–	(10,678)	–
Royalty obligations	(4,899)	–	(4,899)	–	–	(4,899)

(1) Risk management contract assets and liabilities presented in the condensed interim consolidated statements of financial position are shown net of offsetting assets or liabilities where the arrangement provides for the legal right, and intention for net settlement exists.