# MANAGEMENT'S DISCUSSION AND ANALYSIS

**(All tabular amounts are stated in thousands of dollars, except per unit amounts)**

Distinction Energy Corp. ("Distinction" or the "Company") is an oil and natural gas company based in Calgary, Alberta, focused on the exploration, development, and production of crude oil, natural gas and natural gas liquids from properties located in Western Canada. Distinction's operations are concentrated in the Deep Basin of Northwest Alberta. Additional information about Distinction is available on the Canadian Securities Administrators' System for Electronic Distribution and Retrieval (SEDAR) at www.sedar.com and at the Company's website at www.distinctionenergy.ca.

Management's discussion and analysis ("MD&A") has been prepared by management and reviewed and approved by the Board of Directors of the Company. The discussion and analysis is a review of the financial position and results of operations of the Company. Its focus is primarily a comparison of the financial performance for the three months ended March 31, 2021 and 2020 and should be read in conjunction with the unaudited condensed consolidated interim financial statements and accompanying notes for the three months ended March 31, 2021 and 2020 and the audited consolidated financial statements and accompanying notes for the year ended December 31, 2020 and the related MD&A. The unaudited condensed consolidated interim financial statements have been prepared in accordance with International Accounting Standard ("IAS") 34, Interim Financial Reporting. The reporting currency is the Canadian dollar. The discussion and analysis has been prepared as of May 20, 2021. In April 2020, Delphi Energy Corp. (now Distinction) filed for protection under the Companies' Creditors Arrangement Act ("CCAA"). In October 2020, the Company emerged from CCAA and concurrently completed transactions contemplated in the Company's plan of compromise and arrangement (the "Plan").

## FIRST QUARTER 2021 HIGHLIGHTS

- Entered into agreements to participate as to 50 percent in a $320.0 million asset acquisition of oil and natural gas properties in the Simonette area of northwest Alberta (the "Simonette Acquisition"). The Simonette Acquisition consists of certain multi-zone, oil and liquids-rich natural gas producing assets in the Simonette area of northwest Alberta, including associated infrastructure and additional assets in the Willesden Green, Ferrier and other areas of Alberta. As of the first quarter of 2021, the Company's share of production prior to the closing date of April 28, 2021, would have been approximately 4,625 barrels of oil equivalent per day, weighted 43% to oil and natural gas liquids ("NGLs");

- Produced an average of 6,381 barrels of oil equivalent per day ("boe/d") down 3 percent from the 6,575 boe/d in the comparative quarter of 2020. Production in the first quarter of 2021 was weighted 41 percent condensate and natural gas liquids and 59 percent natural gas;

- Continued to deliver high liquids content with an average liquids yield of 116 barrels per million cubic feet ("bbls/mmcf"), up 4 percent from the 112 bbls/mmcf in the comparative quarter of 2020. Condensate and pentanes yields were approximately flat in the comparative quarters at 73 percent; 85 barrels ("bbls") of the 116 bbls/mmcf liquids yield as compared to 81 bbls of the 112 bbl/mmcf yield in the first quarter of 2020;

- Crude oil and natural gas revenue was $21.7 million, an increase of 52 percent from the first quarter of 2020. Field condensate contributed 46 percent of crude oil and natural gas revenue while natural gas and NGL contributed 40 percent and 14 percent, respectively. Revenues have increased due to significantly higher realized prices over the comparative period;

- Reduced operating costs by twelve percent to $8.96 per barrel of oil equivalent ("boe") in comparison to $10.13 per boe in the first quarter of 2020. The reduction in operating expenses is a result of reduced water hauling charges and continued field optimization;

- Reduced transportation costs by eleven percent to $3.62 per boe in comparison to $3.92 per boe in the first quarter of 2020. The decrease in transportation is largely due to reduced natural gas transportation as the Company has temporarily assigned approximately 17 mmcf/d of its Alliance service through to the end of October 2021, saving 50 per cent of the excess capacity toll costs. The costs associated with the temporary assignment of the 17 mmcf/d is recognized as a marketing activity;

- Adjusted funds flow in the three months ended March 31, 2021 increased 134 percent to $8.9 million compared to $3.8 million from the comparable period of 2020. The increase is primarily due to increase crude oil and natural gas prices, marketing income, reductions in operating, transportation and finance costs partially offset by realized losses on risk management contracts, higher general and administrative costs, as well as restructuring charges;

- The operating netback before risk management contracts increased 217 per cent to $22.85 per boe in the first quarter, up substantially from the $7.20 per boe in the comparative quarter of 2020. The increase is primarily due to the recovery of crude oil and associated natural gas liquids prices, gain on marketing versus a loss in the comparative quarter of 2020, realized savings on operating and transportation costs partially offset by an increase in royalties related to increased prices;

- The cash netback for the three months ended March 31, 2021 increased 144 per cent to $15.58 per boe compared to $6.38 per boe from the first quarter of 2020 primarily due to the significant decrease in finance charges, as the Company emerged from CCAA proceedings in October 2020 with no indebtedness, partially offset by ongoing restructuring costs;
- Kiwetinohk Resources Corp. (“Kiwetinohk”) exercised approximately 3.3 million warrants (“New Warrants”) to purchase approximately 3.3 million Class A common shares of the Company for an aggregate exercise price of $40.0 million. Kiwetinohk and Luminus Energy IE Designated Activity Company (“Luminus Energy”) now hold 51.6 percent and 27.6 percent, respectively, of the issued and outstanding Class A common shares of the Company;
- Closed a private placement of 265,331 special warrants (“Special Warrants”) issued at a price of $15 per Special Warrant for gross proceeds of approximately $4.0 million. Each Special Warrant is exercisable into one Class A common share of the Company without payment of any additional consideration;
- Subsequent to the quarter, on April 6, 2021, the Company announced the appointment of new executive officers pursuant to previously disclosed plans to rebuild Distinction from last year’s CCAA process. Mr. Patrick Carlson was appointed President and Chief Executive Officer of the Company in place of Mr. Timothy Schneider, Mr. Jakub Brogowski was appointed Chief Financial Officer of the Company in place of Mr. Peter Eric Gallie and Mr. Glen Nevokshonoff was appointed Chief Operating Officer of the Company; and
- Subsequent to the quarter, on April 28, 2021, the Company closed its previously announced Simonette Acquisition. The Company participated as to 50 percent in the $320 million Simonette Acquisition (excluding up to $15 million in potential contingent payments payable over the next two years based on future commodity prices) which was funded by cash on hand and approximately $63.3 million of bank indebtedness. Concurrently with the closing of the Simonette Acquisition, the Company obtained a $127.5 million credit facility (“New Credit Facility”) provided by a syndicate of chartered banks.

## FINANCIAL AND OPERATIONAL HIGHLIGHTS

| | Three months ended Mar. 31 | | |
|---|---|---|---|
| | **2021** | 2020 | % Change |
| **Financial** | | | |
| ($ thousands, except per share) | | | |
| Crude oil and natural gas revenues | **21,665** | 14,259 | 52 |
| Net loss | **(5,175)** | (109,970) | (95) |
| Per share – basic & diluted | **(0.58)** | (18.06) | (97) |
| Cash flow from operating activities | **6,233** | 6,830 | (9) |
| Per share – basic & diluted (1)(2) | **0.70** | 1.12 | (38) |
| Adjusted funds flow(1) | **8,939** | 3,819 | 137 |
| Per share – basic and diluted(1)(2) | **1.01** | 0.63 | 60 |
| Net debt (surplus)(1) | **(88,986)** | 164,403 | (154) |
| Capital expenditures, net of dispositions | **864** | 22,288 | (96) |
| Weighted average shares (000s) | | | |
| Basic and diluted(2) | **8,879** | 6,089 | 51 |
| **Operating** | | | |
| (boe conversion – 6:1 basis) | | | |
| Production: | | | |
| Field condensate (bbls/d) | **1,740** | 1,683 | 3 |
| Natural gas liquids (bbls/d) | **880** | 958 | (8) |
| Natural gas (mcf/d) | **22,566** | 23,601 | (4) |
| Total (boe/d) | **6,381** | 6,575 | (3) |
| Average realized sales prices, before financial instruments | | | |
| Field condensate ($/bbl) | **63.73** | 50.79 | 25 |
| Natural gas liquids ($/bbl) | **38.06** | 16.01 | 138 |
| Natural gas ($/mcf) | **4.26** | 2.37 | 80 |
| Netbacks ($/boe) | | | |
| Crude oil and natural gas revenues | **37.73** | 23.83 | 58 |
| Marketing income (loss)(1) | **0.37** | (0.71) | - |
| Realized gain (loss) on financial instruments | **(1.44)** | 8.17 | (118) |
| Revenue, after realized financial instruments | **36.66** | 31.29 | 17 |
| Royalties | **(2.67)** | (1.87) | 43 |
| Operating expense | **(8.96)** | (10.13) | (12) |
| Transportation expense | **(3.62)** | (3.92) | (8) |
| Operating netback (1) | **21.41** | 15.37 | 39 |
| General and administrative expenses | **(4.03)** | (2.48) | 63 |
| Other income | **0.07** | - | - |
| Restructuring costs | **(1.51)** | - | - |
| Finance charges | **(0.36)** | (6.23) | (94) |
| Settlement of unutilized take-or-pay contract | **-** | (0.28) | - |
| **Cash netback(1)** | **15.58** | 6.38 | 144 |

*(1) Refer to non–GAAP measures*

*(2) In accordance with Earnings per Share ("IAS 33"), per share calculations presented should be based on the new number of outstanding common shares if the number of outstanding common shares changes as a result of a recapitalization. Accordingly, the weighted average common shares used for the periods presented have been adjusted to reflect the Class A common shares outstanding as a result of the Company's restructuring under the Plan.*

## COVID-19

Since the World Health Organization declared novel coronavirus COVID-19 ("COVID-19") a global pandemic in 2020, global economies have experienced varying degrees of economic recovery and subsequent virus outbreak. Vaccination programs have commenced around the globe, however the pace with which vaccines are being administered is dependent on the supply access and logistics organized by individual nations. Domestically, Canada has vaccinated a relatively small percentage of its population and many regions across the country are experiencing a third wave of COVID-19. The greatest potential impact to Distinction is the effect on demand for commodities and the subsequent impact on commodity prices. At March 31, 2021, Distinction’s management has incorporated the current and anticipated impacts of COVID-19 in its preparation of the MD&A.

## SIMONETTE ACQUISTION

In February 2021, the Company entered into agreements to participate as to 50 percent in a $320.0 million asset acquisition of oil and natural gas properties in the Simonette area of northwest Alberta, and paid a $7.5 million deposit. The Simonette Acquisition consists of certain multi-zone, oil and liquids-rich natural gas producing assets in the Simonette area of northwest Alberta, including associated infrastructure and additional assets in the Willesden Green, Ferrier and other areas of Alberta. As of the first quarter of 2021, the Company’s share of production prior to closing would have been approximately 4,625 barrels of oil equivalent per day, weighted 43% to oil and natural gas liquids (“NGLs”).

The purchase price of $320.0 million excludes up to $15 million of contingent payments ($7.5 million for the Company’s share) that will be required if average crude oil prices exceed the reference price for WTI of USD $56.00 per barrel in 2021 and USD $62.00 per barrel in 2022. The transaction closed on April 28, 2021 and was subject to standard closing adjustments from the effective date of January 1, 2021, through to April 28, 2021. Distinction funded its $160.0 million ($148.0 million net of interim closing adjustments) share of the purchase price with cash on hand and approximately $63.3 million of bank indebtedness provided by the New Credit Facility (see Senior Credit Facility).

## 2021 DRILLING AND COMPLETIONS OPERATIONS

Distinction did not drill or complete any wells in the period ended March 31, 2021. In comparison, in the first three months of 2020, Distinction drilled three wells in liquids-rich West Bigstone.

## CAPITAL EXPENDITURES

| | Three Months Ended Mar. 31 | | |
|---|---|---|---|
| | **2021** | 2020 | % Change |
| Drilling, completions and equipping | **277** | 20,639 | (99) |
| Facilities | **448** | 1,310 | (66) |
| Land | **-** | 50 | - |
| Capitalized expenses | **139** | 273 | (49) |
| Other | **-** | 16 | - |
| Total capital | **864** | 22,288 | (96) |

During the first three months of 2021, Distinction spent $0.9 million on capital expenditures. Approximately $0.5 million was incurred on artificial lift projects and $0.2 million on a planned turnaround for its 07-11 battery and amine facility which commenced operations mid-April 2021.

During the first quarter of 2020, the Company spent $22.3 million primarily on the drilling, completions and equipping operations on three (3.0 net) wells.

## PRODUCTION

| | Three Months Ended Mar. 31 | | |
|---|---|---|---|
| | **2021** | 2020 | % Change |
| Field condensate (bbls/d) | **1,740** | 1,683 | 3 |
| Ethane (bbls/d) | **2** | 5 | (60) |
| Propane (bbls/d) | **382** | 384 | (1) |
| Butane (bbls/d) | **314** | 335 | (6) |
| Pentanes & plant condensate (bbls/d) | **182** | 234 | (28) |
| Total field condensate and natural gas liquids | **2,620** | 2,641 | (1) |
| Natural gas (mcf/d) | **22,566** | 23,601 | (4) |
| Total (boe/d) | **6,381** | 6,575 | (3) |

Production in the first three months of 2021 averaged 6,381 boe/d, down three percent from the comparative period in 2020. Although no new production has been brought on-stream since September 2020, the production declines associated with the winter 2020 program are partially offset by bringing previously shut-in production back on, improved well performance from artificial lift projects and field optimization activities.

Production from the Montney continues to deliver high liquids content. During the first quarter ended March 31, 2021, the liquids yield averaged 116 bbls/mmcf up from the 112 bbls/mmcf in the comparative quarter of 2020.

The Company's production portfolio for the first quarter of 2021 was weighted 27 percent to field condensate, 14 percent to natural gas liquids and 59 percent to natural gas. The production portfolio for the comparative quarter in 2020 was weighted 26 percent to field condensate, 14 percent to natural gas liquids and 60 percent to natural gas.

## BUSINESS ENVIRONMENT

### Benchmark Prices and Economic Parameters

| | Three Months Ended Mar. 31 | | |
|---|---|---|---|
| | **2021** | 2020 | % Change |
| **Natural Gas** | | | |
| Chicago City Gate MI (US $/mmbtu) | **2.69** | 1.95 | 38 |
| Chicago City Gate DI (US $/mmbtu) | **8.80** | 1.74 | 406 |
| AECO 5A (CDN $/mcf) | **3.12** | 2.04 | 53 |
| AECO 7A (CDN $/mcf) | **2.93** | 2.14 | 37 |
| **Crude Oil** | | | |
| West Texas Intermediate (US $/bbl) | **57.80** | 46.08 | 25 |
| West Texas Intermediate (CDN$/bbl) | **73.16** | 61.53 | 19 |
| Edmonton condensate to WTI Differential (CDN $/bbl) | **(0.01)** | (0.38) | (97) |
| **Foreign Exchange** | | | |
| Canadian to U.S. dollar | **0.79** | 0.74 | 6 |
| U.S. to Canadian dollar | **1.27** | 1.34 | (6) |

Although the influence of the COVID-19 pandemic continues, commodity pricing has improved due to the rise in global demand as economies restart as COVID-19 vaccines rollout.

### Natural Gas

Prior to the Simonette Acquisition, approximately half of Distinction's natural gas production was shipped through the Alliance pipeline system into the Chicago market. Production from the Simonette Acquisition will be shipped through the Alliance pipeline system into the Chicago market.  Chicago City Gate is the primary benchmark for Distinction's natural gas sales in the United States. The remainder of Distinction's natural gas production is sold in Alberta on the NGTL system. The AECO 5A price is the primary benchmark for the Company's natural gas sales in Alberta.

The Chicago City Gate benchmark natural gas prices for the three months ended March 31, 2021 increased significantly in comparison to the same period in 2020. The significant increase in the Chicago daily index benchmark price was a result of high demand in February for heating purposes while export demand continued at record levels due to a supply shortfall in the global gas market. Local spot pricing in Chicago reached record levels but forward prices remained mostly unchanged due to the short-lived nature of the event.

The average daily AECO benchmark natural gas price increased 53 percent the three months ended March 31, 2021 in comparison to the same period in 2020. AECO natural gas prices have strengthened during 2021 as compared to 2020, due to strong local demand and high utilization of export pipeline capacity drew heavily on Alberta natural gas inventories.

**Crude Oil**

West Texas Intermediate ("WTI") oil prices increased 25 percent over the WTI benchmark for the three months ended March 31, 2020. The increase is primarily related to improvement of global economic activity and crude oil demand related to the continuing recovery from the global pandemic. The curtailment agreements from OPEC and lower than expected US supply growth has also assisted with the recovery of oil prices. The March 2021 WTI price increased 120 percent compared to the March 2020 WTI price which reflected the onset of the COVID-19 global shutdown coupled with the Russia-Saudi Arabia oil price war.

**Natural Gas Liquids**

Natural gas liquids, including ethane, propane, butane, pentane and plant condensate, are generally priced off light oil and natural gas prices. Ethane prices are correlated to natural gas prices while propane and butane prices trade at a discount to light oil prices depending on supply and demand conditions.

**Canadian/United States Exchange Rate**

The value of the Canadian dollar against its U.S. counterpart increased six percent in the three months ended March 31, 2021 over the comparative period in 2020. As a producer of natural gas sold in the United States, an increase in the Canadian dollar relative to its U.S. counterpart has a negative effect on the price received for production.

**REALIZED SALES PRICES**

| | Three Months Ended Mar. 31 | | |
|---|---|---|---|
| | **2021** | 2020 | % Change |
| **Chicago** | | | |
| Chicago City Gate MI (CDN$/mcf) | **3.31** | 2.61 | 27 |
| Heating content and marketing ($/mcf) | **1.90** | (0.09) | - |
| Realized price before risk management contracts ($/mcf) | **5.21** | 2.52 | 107 |
| **AECO** | | | |
| AECO 5A ($/mcf) | **3.12** | 2.04 | 53 |
| Heating content and marketing ($/mcf) | **0.22** | 0.18 | 22 |
| Realized price before risk management contracts ($/mcf) | **3.34** | 2.22 | 50 |
| **Combined Natural Gas** | | | |
| Realized natural gas price before risk management contracts ($/mcf) | **4.26** | 2.37 | 80 |
| Realized gain (loss) on financial contracts ($/mcf) | **(0.07)** | 0.28 | (125) |
| Realized natural gas price ($/mcf) | **4.19** | 2.65 | 58 |
| Marketing income (loss) ($/mcf) (1) | **0.10** | (0.20) | - |
| Natural gas price including marketing income (loss) ($/mcf) | **4.29** | 2.45 | 75 |

| | Three Months Ended Mar. 31 | | |
|---|---|---|---|
| | **2021** | 2020 | % Change |
| **Field Condensate** | | | |
| WTI (CDN$/bbl) | **73.16** | 61.53 | 19 |
| Edmonton condensate to WTI Differential ($/bbl) | **(0.01)** | (0.38) | (97) |
| Edmonton condensate | **73.15** | 61.15 | 20 |
| Differential and marketing ($/bbl) | **(9.42)** | (10.36) | (9) |
| Realized price before risk management contracts ($/bbl) | **63.73** | 50.79 | 25 |
| Realized gain (loss) on financial contracts ($/bbl) | **(4.32)** | 26.56 | (116) |
| Realized field condensate price ($/bbl) | **59.41** | 77.35 | (23) |
| **Natural Gas Liquids** | | | |
| Realized natural gas liquids price ($/bbl) | **38.06** | 16.01 | 138 |
| Realized gain on financial contracts ($/bbl) | **-** | 2.57 | - |
| Realized natural gas liquids price ($/bbl) | **38.06** | 18.58 | 105 |
| Total realized sales price ($/boe) | **36.28** | 32.00 | 13 |

*(1) Refer to non–GAAP measures.*

Distinction sells natural gas in the Chicago market through the Alliance pipeline system and in the AECO market through the NGTL system. Natural gas that is sweetened at the Company's amine facility is further processed at its 25 percent owned Bigstone sweet natural gas plant ("Bigstone Sweet Plant") which is currently only connected to the NGTL pipeline system. The meter station at the Bigstone Sweet Plant is expected to be upgraded in the first quarter of 2022 which will allow the Company to ship its natural gas on the NGTL and Alliance transportation systems. In the first three months of 2021, Distinction sold 50 percent of its natural gas in the Chicago market which is comparable to the proportion of volumes sold in Chicago in the first quarter of 2020.

Natural gas differentials for marketing are caused by differences between the daily and monthly benchmark price indices, as well the premium the Company receives over benchmark pricing for heat content. The majority of the natural gas volumes that were shipped on the Alliance pipeline system were sold with reference to the monthly index and the remainder of the volumes were sold with reference to the daily index. The majority of natural gas volumes shipped on NGTL are sold with reference to AECO 5A index and the remainder with reference to AECO 7A.

For the three months ended March 31, 2021, Distinction's realized natural gas price before risk management contracts increased 80 percent over the comparable period in 2020. The increase in the average realized price for natural gas is due to an improvement in benchmark prices, in particular the Chicago monthly index as a result of an extreme weather event.

Realized field condensate prices before risk management contracts were 25 percent higher in the three months ended March 31, 2021 compared to the same period in 2020. The increase in the field condensate realized price before risk management is due to the increase in the WTI benchmark. Differentials and marketing for field condensate include quality adjustments and marketing arrangements.

Distinction's realized price for natural gas liquids before risk management contracts increased 138 percent as compared to the same period in 2020. Natural gas liquids are generally priced off of WTI; the increase reflects significantly higher benchmark prices for propane, butane and pentane prices which correlates with the increase in natural gas, oil and condensate benchmark prices in the period.

## RISK MANAGEMENT ACTIVITIES

In an effort to mitigate commodity price fluctuations for natural gas, crude oil and natural gas liquids, Distinction enters into financial commodity contracts as part of its risk management program designed to protect cash flows through to simple payout on the drilling and completion portion of its capital program.

The Company currently has the following commodity risk management contracts outstanding:

**Crude Oil Contracts**

| Time Period | Type of Contract | Quantity Contracted | Price ($/unit) | Reference |
|---|---|---|---|---|
| May 2021 – December 2021 | Fixed price swap | 125 bbls/d | $58.50 Cdn | WTI |
| May 2021 – December 2021 | Fixed price swap | 125 bbls/d | $56.20 Cdn | WTI |
| May 2021 – December 2021 | Fixed price swap | 125 bbls/d | $55.70 Cdn | WTI |
| May 2021– December 2021 | Fixed price swap | 750 bbls/d | $75.05 Cdn | WTI |
| January 2022 – December 2022 | Fixed price swap | 750 bbls/d | $69.95 Cdn | WTI |

**Natural Gas Contracts**

| Time Period | Type of Contract | Quantity Contracted | Price ($/unit) | Reference |
|---|---|---|---|---|
| May 2021 – December 2021 | Fixed price swap | 1,575 gj/d | $2.43 Cdn | AECO |
| May 2021 – December 2021 | Fixed price swap | 1,575 gj/d | $2.27 Cdn | AECO |
| May 2021 – December 2021 | Fixed price swap | 1,575 gj/d | $2.27 Cdn | AECO |
| January 2022 – June 2022 | Fixed price swap | 750 gj/d | $2.49 Cdn | AECO |
| January 2022 – June 2022 | Fixed price swap | 750 gj/d | $2.37 Cdn | AECO |
| January 2022 – June 2022 | Fixed price swap | 750 gj/d | $2.30 Cdn | AECO |
| July 2022 – December 2022 | Fixed price swap | 675 gj/d | $2.25 Cdn | AECO |
| July 2022 – December 2022 | Fixed price swap | 675 gj/d | $2.24 Cdn | AECO |
| July 2022 – December 2022 | Fixed price swap | 675 gj/d | $2.13 Cdn | AECO |
| May 2021 – December 2021 | Fixed price swap | 1,475 mmbtu/d | $3.81 Cdn | NYMEX |
| May 2021 – December 2021 | Fixed price swap | 1,475 mmbtu/d | $3.59 Cdn | NYMEX |
| May 2021 – December 2021 | Fixed price swap | 1,475 mmbtu/d | $3.56 Cdn | NYMEX |
| January 2022 – June 2022 | Fixed price swap | 700 mmbtu/d | $3.69 Cdn | NYMEX |
| January 2022 – June 2022 | Fixed price swap | 700 mmbtu/d | $3.59 Cdn | NYMEX |
| January 2022 – June 2022 | Fixed price swap | 700 mmbtu/d | $3.51 Cdn | NYMEX |
| July 2022 – December 2022 | Fixed price swap | 650 mmbtu/d | $3.41 Cdn | NYMEX |
| July 2022 – December 2022 | Fixed price swap | 650 mmbtu/d | $3.44 Cdn | NYMEX |
| July 2022 – December 2022 | Fixed price swap | 650 mmbtu/d | $3.31 Cdn | NYMEX |
| May 2021 – December 2021 | Fixed price swap | 7,500 mmbtu/d | $3.61 Cdn | NYMEX |
| January 2022 – December 2022 | Fixed price swap | 2,500 mmbtu/d | $3.30 Cdn | NYMEX |

**Basis Differential Contracts**

Distinction ships approximately half of its natural gas production through the Alliance pipeline system into the Chicago market. As a result, the Company has entered into NYMEX to Chicago basis differential contracts in order to fix the basis on a portion of its natural gas sales in the Chicago market.

| Time Period | Type of Contract | Quantity Contracted | Differential (U.S. $/unit)) |
|---|---|---|---|
| May 2021 – December 2021 | Fixed price swap | 1,475 mmbtu/d | ($0.240) |
| May 2021 – December 2021 | Fixed price swap | 1,475 mmbtu/d | ($0.255) |
| May 2021 – December 2021 | Fixed price swap | 1,475 mmbtu/d | ($0.260) |
| January 2022 – June 2022 | Fixed price swap | 700 mmbtu/d | ($0.100) |
| January 2022 – June 2022 | Fixed price swap | 700 mmbtu/d | ($0.110) |
| January 2022 – June 2022 | Fixed price swap | 700 mmbtu/d | ($0.195) |
| July 2022 – December 2022 | Fixed price swap | 650 mmbtu/d | ($0.225) |
| July 2022 – December 2022 | Fixed price swap | 650 mmbtu/d | ($0.210) |
| July 2022 – December 2022 | Fixed price swap | 650 mmbtu/d | ($0.250) |
| May 2021 – December 2021 | Fixed price swap | 7,500 mmbtu/d | ($0.190) |
| January 2022– December 2022 | Fixed price swap | 2,500 mmbtu/d | ($0.095) |

In connection with the Simonette Acquisition, the Company has entered into the following risk management contracts:

**Crude Oil Contracts**

| Time Period | Type of Contract | Average Quantity Contracted | Swap Price ($/unit) | Bought Put Price ($/unit) | Sold Call Price ($/unit) | Reference |
|---|---|---|---|---|---|---|
| June 2021 to December 2021 | Price swap | 1,018 bbls/d | $77.00 Cdn | - | - | WTI |
| January 2022 to December 2022 | Collar | 999 bbls/d | - | $65.00 Cdn | $78.00 Cdn | WTI |

**Natural Gas Contracts**

| Time Period | Type of Contract | Quantity Contracted | Price ($/unit) | Reference |
|---|---|---|---|---|
| June to October 2021 | Price swap - buyer | 33,658 gj/d | $2.7691 Cdn | AECO |
| June to October 2021 | Price swap - seller | 31,902 mmbtu/d | $2.7809 USD | Chicago |

**U.S. Dollar Forward Exchange Contract**

| Time Period | Monthly Average Notional U.S. $ | Average Exchange Rate (U.S.$ to Cdn$) |
|---|---|---|
| June to October 2021 | $2,715,572 | 1.22709 |

**Fair value of Distinction's risk management contracts**

With respect to financial contracts, which are derivative financial instruments, management has elected not to use hedge accounting and consequently records the fair value of its natural gas and crude oil financial contracts on the statement of financial position at each reporting period with the change in the fair value being classified as unrealized gains and losses in the consolidated statement of earnings (loss).

The fair value of Distinction's risk management contracts outstanding as at March 31, 2021 is estimated to be a net liability of $0.9 million. The fair values of these contracts are based on an approximation of the amounts that would have been paid to or received from counterparties to settle the contracts outstanding at the end of the period having regard to forward prices and market values provided by independent sources. Due to the inherent volatility in commodity prices, foreign exchange and interest rates, actual amounts realized may differ from these estimates.

For the three months ended March 31, 2021, Distinction recorded an unrealized loss on its risk management contracts of $1.0 million. The unrealized loss recognized for the three months ended March 31, 2021 is the difference between the fair values of the risk management contracts outstanding as at March 31, 2021 and the fair values as at December 31, 2020. The decrease in the fair value of the risk management contracts as at March 31, 2021 reflects higher forward pricing for WTI crude oil contracts compared to the Company's contracted prices.

For the three months ended March 31, 2021, Distinction recorded a realized loss on its risk management contracts of $0.8 million compared to a realized gain of $4.9 million in the first quarter of 2021. The realized loss in the first quarter of 2021 is primarily due to a lower average contracted WTI price compared to benchmark pricing.

## REVENUES

### CRUDE OIL AND NATURAL GAS REVENUES

| | Three Months Ended Mar. 31 | | |
|---|---|---|---|
| | **2021** | 2020 | % Change |
| Field condensate | **9,980** | 7,780 | 28 |
| Natural gas | **8,653** | 5,091 | 70 |
| Natural gas liquids | **3,014** | 1,396 | 116 |
| Sulphur | **18** | (8) | - |
| Total | **21,665** | 14,259 | 52 |
| Per boe | **37.73** | 23.83 | 58 |

For the three months ended March 31, 2021, Distinction generated $21.7 million of revenues from the sale of its crude oil and natural gas, up $7.4 million or 52 percent over the comparative period. Field condensate contributed 46 percent of total revenues in the three months ended March 31, 2021, compared to 55 percent in the same period in 2020.

The impact on revenues due to variance of volumes and realized prices before risk management is as follows:

| | Three Months Ended Mar. 31 | | |
|---|---|---|---|
| | 2021 | 2020 | **($000's)** |
| **Crude oil and natural gas revenues, March 31, 2020** | | | **14,259** |
| Revenue change due to: | | | |
| Field condensate | | | |
| Volume (bbl/d) | 1,740 | 1,683 | **219** |
| Realized price (1) ($/bbl) | 63.73 | 50.79 | **1,980** |
| Natural gas | | | |
| Volume (mcf/d) | 22,566 | 23,601 | **(497)** |
| Realized price (1) ($/mcf) | 4.26 | 2.37 | **4,059** |
| Natural gas liquids | | | |
| Volume (bbl/d) | 880 | 958 | **(303)** |
| Realized price (1) ($/bbl) | 38.06 | 16.01 | **1,922** |
| Sulphur | | | **26** |
| **Crude oil and natural gas revenues, March 31, 2021** | | | **21,665** |

*(1) Realized price before gains or losses on commodity price risk management contracts.*

## MARKETING

| Marketing Revenue | Three Months Ended Mar. 31<br>2021 | <br>2020 | <br>% Change |
|---|---|---|---|
| Sale of purchased natural gas | **2,112** | 951 | 122 |
| Total | **2,112** | 951 | 122 |

| Marketing Expense | Three Months Ended Mar. 31<br>2021 | <br>2020 | <br>% Change |
|---|---|---|---|
| Cost of purchased natural gas | **691** | 950 | (27) |
| Transportation of purchased natural gas | **265** | 432 | (39) |
| Transportation on temporary assignment of service | **943** | - | - |
| Total | **1,899** | 1,382 | 37 |

| Marketing Income (loss) (1) | Three Months Ended Mar. 31<br>2021 | <br>2020 | <br>% Change |
|---|---|---|---|
| Gain (loss) on marketing of purchased natural gas | **1,156** | (431) | - |
| Temporary assignment of service loss | **(943)** | - | - |
| Total | **213** | (431) | - |
| Marketing income (loss) per boe | **0.37** | (0.71) | - |

*(1) Refer to non–GAAP measures*

Distinction has approximately 29.8 mmcf/d of firm transportation service and 7.5 mmcf/d of priority interruptible service on the Alliance pipeline system from Alberta to Chicago. In order to mitigate the cost of transportation service in excess of its needs, Distinction either temporarily assigns the excess service to other shippers or purchases natural gas in Alberta or British Columbia for sale in Chicago. In the fourth quarter of 2020, the Company temporarily assigned approximately 17.0 mmcf/d of excess Alliance service through to October 31, 2021 for approximately 50 percent of the associated tariff. In the first quarter of 2020, the Company had 14.0 mmcf/d of excess Alliance service temporarily assigned for 100 percent of the associated tariff.

In the three months ended March 31, 2021, the Company realized a gain on its marketing activities associated with purchasing natural gas to fulfill its transmission commitment on the Alliance pipeline system. The Chicago benchmark increased substantially in February compared to the AECO benchmark due to the extreme weather events coupled with supply issues, creating a favourable arbitrage for marketing activities.

On April 28, 2021 Distinction entered into three marketing agreements with Kiwetinohk for natural gas, condensate and NGLs production volumes associated with the Simonette Acquisition. Kiwetinohk will market all of Distinction's production from the Simonette Acquisition and will also purchase natural gas volumes above production required to fill Distinction's net 45 mmcf/d of contracted capacity on the Alliance Pipeline. Natural gas purchases required to fill the capacity above expected production have been fully contracted through October 31, 2021. The marketing profits based upon actual revenues and costs will be shared equally with Distinction and Kiwetinohk for their respective volumes.

## ROYALTIES

| | Three Months Ended Mar. 31 | | |
|---|---|---|---|
| | **2021** | 2020 | % Change |
| Crown royalties | **2,047** | 1,242 | 65 |
| Royalty credits | **(1,110)** | (634) | 75 |
| Crown royalties – net | **937** | 608 | 54 |
| Gross overriding royalties | **594** | 509 | 17 |
| Total | **1,531** | 1,117 | 37 |
| Per boe | **2.67** | 1.87 | 43 |

| | Three Months Ended Mar. 31 | | |
|---|---|---|---|
| | **2021** | 2020 | % Change |
| Crown rate – before royalty credits | **9.4%** | 8.7% | 8 |
| Crown rate – net of royalty credits | **4.3%** | 4.3% | - |
| Gross overriding rate | **2.7%** | 3.6% | (25) |
| Average rate | **7.1%** | 7.8% | (9) |

The royalty rate calculations above exclude gains or losses on risk management activities from revenue as the denominator.

For the three months ended March 31, 2021, royalties totaled $1.5 million compared to $1.1 million for the same period in 2020. Royalties in the three months of 2021 have increased due to improvements in benchmark pricing for crude oil and natural gas liquids largely offset by an increase in Crown royalty credits.

The average Crown royalty rate before royalty credits has increased to 9.4 percent in the three months ended March 31, 2021, in comparison to 8.7 percent for the same period in 2020. Some of the Company's Montney field condensate production, drilled prior to January 1, 2017, which fall under the old royalty regime, have come off of royalty holidays which increases the royalty rate from zero percent to an average of approximately 40 percent (depending on individual well factors and benchmark prices). All of Distinction's production from wells drilled subsequent to January 1, 2017 qualify for reduced Crown royalty rates under the Modern Royalty Framework which currently imposes a five percent royalty rate on all products until certain conditions are met. The Company's three new wells drilled in the first quarter of 2020 qualify for the lower rates under the Modern Royalty Framework. In addition, the Company's average royalty rate for natural gas has increased due to improved AECO benchmark prices.

Crown royalty credits are largely based on the amortization of historical capital and operating costs of gas facilities and do not fluctuate based on commodity prices but are limited to Crown royalties paid on natural gas and natural gas liquids and exclude royalties paid on field condensate. Crown royalty credits increased in the three months ended March 31, 2021 compared to the three months ended March 31, 2020 as the Company was able to utilize more of its royalty credits to offset the increased royalties.

Gross overriding royalties were 2.7 percent in the three months ended March 31, 2021 in comparison to 3.6 percent for the same period in 2020. Production from the Company's 2020 winter drilling program are not encumbered by gross overriding royalties, reducing the average gross overriding royalty rate.

## OPERATING EXPENSES

| | Three Months Ended Mar. 31 | | |
|---|---|---|---|
| | **2021** | 2020 | % Change |
| Production costs | **5,324** | 6,375 | (16) |
| Processing recoveries | **(177)** | (316) | (44) |
| Total | **5,147** | 6,059 | (15) |
| Per boe | **8.96** | 10.13 | (12) |

Operating expense decreased by $0.9 million in the first quarter of 2021 to $5.1 million as compared to $6.1 million in the first quarter of 2020. The decrease in operating expenses is due to a reduction in water trucking charges, lower equalization charges for natural gas processing and continued cost control efforts. Commencing in the second quarter of 2020, with lower production levels, the Company was able to eliminate trucking water from West Bigstone by using its existing infrastructure to move natural gas and liquids to its 07-11 battery for further handling.

Distinction recovers processing costs on partner production volumes processed at facilities it owns. The processing recoveries represent a reduction of the Company's costs to operate these facilities and hence is deducted in determining operating expenses. The reduction in processing recoveries is primarily due to partner's share of West Bigstone production that was processed at the Company's 100 percent owned Negus gas processing facility which is now being processed at a jointly owned facility.

**TRANSPORTATION EXPENSES**

| | Three Months Ended Mar. 31 | | |
|---|---|---|---|
| | **2021** | 2020 | % Change |
| Transportation [(1)] | **2,081** | 2,343 | (11) |
| Transportation per boe | **3.62** | 3.92 | (8) |

(1) *Pipeline tariffs are classified as transportation expenses when the Company has firm commitments or contractual arrangements on the pipeline. Pipeline tariffs may also be incurred indirectly by way of deduction from the base price paid by the purchasers of the Company's commodities. In the latter case, and in the absence of a firm contractual obligation on the pipeline, the pipeline tariffs are presented as a reduction of revenue rather than as a transportation expense.*

Transportation expenses in the three months ended March 31, 2021 decreased eleven percent in comparison to the same period in 2020. The decrease in transportation expense is largely due to lower natural gas fixed transportation charges associated with the volumes shipped via the Alliance pipeline system. In an effort to mitigate excess transportation on the Alliance transmission system, the Company temporarily assigns excess service to other producers or marketers. In the fourth quarter of 2020, the Company temporarily assigned approximately 17 mmcf/d of its excess Alliance service through to October 31, 2021. This compares to 14 mmcf/d of its Alliance service temporarily assigned in the first quarter of 2020.

**GENERAL AND ADMINISTRATIVE**

| | Three Months Ended Mar. 31 | | |
|---|---|---|---|
| | **2021** | 2020 | % Change |
| Gross expenses | **2,455** | 1,839 | 33 |
| Capitalized | **(139)** | (356) | (61) |
| General and administrative expenses | **2,316** | 1,483 | 56 |
| Per boe | **4.03** | 2.48 | 63 |

General and administrative expenses ("G&A") before capitalization for the three months ended March 31, 2021 increased 33 per cent compared to the same period in 2020. The $0.6 million increase in G&A expenses before capitalization is primarily related to $0.6 million for management service fees (see "Related Party Transactions") and $0.2 million of higher legal fees partially offset by a $0.2 million decrease in personnel costs. Capitalized expenses were lower in the current quarter due to significantly lower capital activity combined with lower personnel costs.

**RESTRUCTURING COSTS**

| | Three Months Ended Mar. 31 | | |
|---|---|---|---|
| | **2021** | 2020 | % Change |
| Restructuring costs | **868** | - | - |
| Per boe | **1.51** | - | - |

Restructuring costs are comprised of legal fees, monitor fees, financial advisory fees, investor relations, consultant fees and termination payments.

In the first three months of 2021, the Company incurred $0.9 million in restructuring costs primarily related to termination benefits associated with the implementation of the Company's Plan (as defined below).

## SHARE-BASED COMPENSATION

| | Three Months Ended March 31 | | |
|---|---|---|---|
| | **2021** | 2020 | % Change |
| Share-based compensation - Options | **1,575** | (2) | - |
| Capitalized costs | **-** | (2) | - |
| Net | **1,575** | (4) | - |
| Per boe | **2.74** | (0.01) | - |

Share-based compensation expense is the amortization over the vesting period of the fair value of stock options granted to employees and directors of the Company. The fair value of all options granted is estimated at the date of grant using the Black-Scholes option pricing model.

In connection with the Plan, all pre-existing outstanding stock options of the Company were cancelled and extinguished for nil consideration. Concurrently, on October 16, 2020, the Company granted to certain officers and directors options and restricted share units entitling them to acquire in the aggregate ten percent of the then issued and outstanding Class A common shares. Each option and restricted share unit entitles the holder to purchase one common share per option or restricted share unit at the grant price.

The Company incurred $1.6 million of share-based compensation for certain officers and directors in the first 3 months of 2021 compared to a recovery in the three months of 2020. The recovery in 2020 was related to the departure of some employees and the related forfeiture of the outstanding stock options.

The stock options have an exercise price of $15 per option and are fully vested. The options have a maximum term of 10 years but contain an early termination clause to expire 100 days from the date when the Company is listed on an approved exchange listing within a date that is approved by the board of directors.

The restricted share units have an exercise price of $0.01 per restricted share unit, vested in full on grant date and are exercisable during the time period commencing on January 1, 2021 to December 31, 2025 when they expire. The restricted share units contain an early termination clause to expire two years from date the Company is listed on an approved exchange listing.

As at March 31, 2021, there were 0.3 million stock options and 0.3 million restricted share units outstanding.

## FINANCE COSTS

| | Three Months Ended Mar. 31 | | |
|---|---|---|---|
| | **2021** | 2020 | % Change |
| Interest | **121** | 3,825 | (97) |
| Finance charges in relation to lease obligations | **18** | 31 | (42) |
| Accretion of decommissioning liabilities | **155** | 111 | 40 |
| Finance charges | **-** | 648 | - |
| Foreign exchange (gain) loss | **70** | (130) | - |
| Total finance costs | **364** | 4,485 | (92) |
| Per boe | **0.63** | 7.50 | (92) |

On October 16, 2020, in accordance with the Plan, the Company compromised $27.0 million of first lien indebtedness and $119.7 million face value of senior secured notes. The interest charged in the first three months of 2021 relates to standby fees on the Company's $30.0 million credit facility and interest related to the $6.0 million of letters of credit issued and outstanding.

Accretion is non-cash and is an expense on the Company's decommissioning liabilities that relates to the passing of time until the Company estimates it will retire its assets and restore the asset locations to a condition which meets or exceeds environmental standards. Due to the long term nature of certain assets of the Company, this accretion expense is estimated to extend over a term of one to 49 years. The increase in accretion expense in the three months ended March 31, 2021 compared to the same period in 2020 is primarily a result of higher decommissioning as a result of change in estimates in the fourth quarter of 2020.

Finance charges in the prior period include the amortization of transaction costs related to the issue of senior secured notes and the accretion of the debt to its face value. The senior secured notes were compromised on October 16, 2020 pursuant to the Plan.

Distinction's foreign exchange gains and losses primarily relate to the conversion of US dollars to Canadian dollars for the settlement of transactions denominated in US dollars, primarily consisting of natural gas sales and pipeline tolls.

**EXPLORATION AND EVALUATION**

During the first three months of 2021, Distinction wrote-down $5.8 million of exploration and evaluation assets. As at March 31, 2021, the Company evaluated upcoming land expiries, the related book value and all capitalized general and administrative costs and determined that the recoverability of the exploration and evaluation assets are no longer supportable as the Company does not intend to develop the associated assets primarily as a result of competing investment opportunities.

**DEPLETION AND DEPRECIATION**

| | Three Months Ended Mar. 31 | | |
|---|---|---|---|
| | **2021** | 2020 | % Change |
| Depletion and depreciation | **5,598** | 7,747 | (28) |
| Impairment | **-** | 114,857 | - |
| Total | **5,598** | 122,604 | (95) |
| Depletion, depreciation per boe | **9.75** | 12.95 | (25) |
| Impairment per boe | **-** | 191.96 | - |

Depletion and depreciation in the three months ended March 31, 2021 decreased in comparison to the same period in 2020 primarily related to a $49.9 million lower net book value subject to depletion. The decrease in net book value subject to depletion decreased due to a $114.9 million impairment recognized in the first quarter of 2020, partially offset by a $65.0 million impairment reversal at December 31, 2020.

At March 31, 2020, the Company identified indicators of impairment on its Bigstone cash generating unit ("CGU") due to the outbreak of the COVID-19 pandemic coupled with the Saudi Arabia - Russia oil price war resulting in both a decrease in oil demand and a significant drop in the forward commodity price curves.

The Company performed an impairment test on its Bigstone CGU, based on the recoverable amount estimated using a value in use calculation derived from expected future cash flows generated from proved and probable reserves using a blended pre-tax discount rate of approximately 15 percent which resulted in the recognition of a $114.8 million impairment. In addition, an impairment related to a change in estimates of decommissioning obligations for non-producing properties of $0.1 million was also recognized.

At December 31, 2020, the Company evaluated its CGU for indicators of impairment or reversal of previously recognized impairment and determined that as a result of the improvement in commodity prices, the Company's improved liquidity, increase in reserves and decrease in future development costs, indicators of a reversal of impairment were identified. The Company performed an impairment test on its Bigstone CGU, based on the recoverable amount estimated using a value in use calculation derived from expected future cash flows generated from proved and probable reserves using a blended pre-tax discount rate of approximately 20 percent which resulted in the recognition of a $65.0 million recovery.

**INCOME TAXES**

Distinction has concluded that it is not probable that the deferred income tax asset will be realized and as a result, it has not been recognized at March 31, 2021. Therefore, no deferred income tax recovery was recorded against the loss for the three months ended March 31, 2021.

Distinction does not have current income taxes payable and has estimated tax pools available at March 31, 2021 of $309.1 million (December 31, 2020 – $316.9 million).

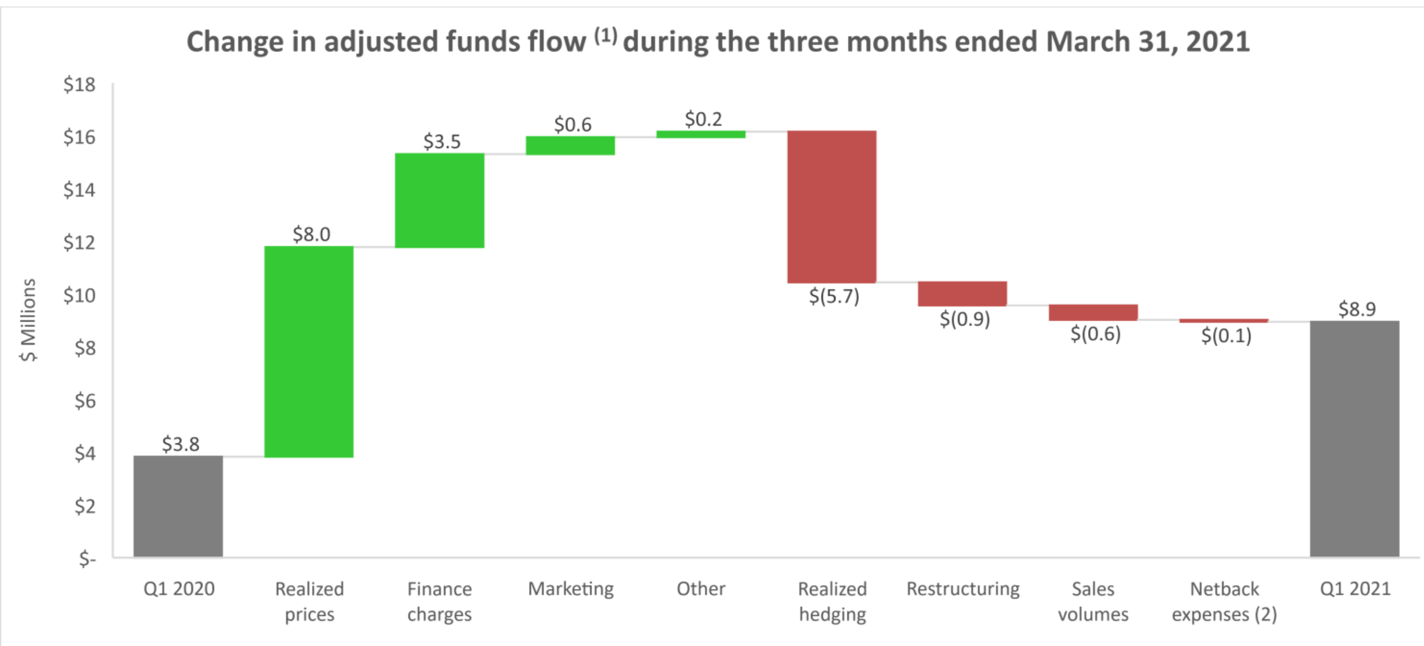
## ADJUSTED FUNDS FLOW

| | Three Months Ended Mar. 31 | | |
|---|---|---|---|
| | **2021** | 2020 | % Change |
| Cash flow from operating activities | **6,233** | 6,830 | (9) |
| Decommissioning expenditures | **17** | 574 | (97) |
| Change in non-cash working capital | **2,689** | (3,585) | - |
| Adjusted funds flow(1) | **8,939** | 3,819 | 134 |

*(1) Refer to non–GAAP measures*

Distinction's cash flow from operating activities decreased 9 percent in the three months ended March 31, 2021, down to $6.2 million from the $6.8 million in the comparative period in 2020. Distinction's adjusted funds flow increased to $8.9 million, up 134% from the $3.8 million in the three months ended March 31, 2021.

The increase in adjusted funds flow is primarily due to increased crude oil and natural gas revenues and a decrease in finance charges partially offset by realized losses on risk management contracts as well as restructuring costs.




*(1) Refer to non–GAAP measures*
*(2) Netback expenses include royalties, operating expenses, transportation and general & administrative costs.*

## NET LOSS AND CASH NETBACK ANALYSIS

| | Three Months Ended Mar.31 | | |
|---|---|---|---|
| | **2021** | 2020 | % Change |
| Net loss | **(5,175)** | (109,970) | (95) |
| Per boe | **(9.01)** | (183.80) | (95) |
| Per basic & diluted share (1) | **(0.58)** | (18.06) | (97) |

*(1) In accordance with IAS 33, per share calculations are based on the new number of outstanding shares if the number of outstanding shares changes as a result of a recapitalization.*

Distinction recorded a net loss of $5.2 million ($0.58 per diluted share) in the first three months of 2021, down from a net loss of $110.0 million ($18.07 per basic and diluted share) recorded in the comparative period of 2020. The net loss in the first quarter of 2021 is primarily due to the $5.8 million write-down of exploration and evaluation assets the Company does not intend to develop as a result of competing investment opportunities partially offset by higher crude oil and natural gas revenues, marketing income and lower finance costs in the current quarter. In addition, depletion and impairment charges were significantly reduced as the Company recorded a $114.8 million impairment charge in the comparative quarter in 2020.

| | Three Months Ended Mar. 31 | | |
|---|---|---|---|
| Barrels of oil equivalent ($/boe) | **2021** | 2020 | % Change |
| Realized sales price | **37.73** | 23.83 | 58 |
| Marketing income (loss) (1) | **0.37** | (0.71) | - |
| Royalties | **(2.67)** | (1.87) | 43 |
| Operating expenses | **(8.96)** | (10.13) | (12) |
| Transportation | **(3.62)** | (3.92) | (8) |
| **Operating netback before risk management contracts** (1) | **22.85** | 7.20 | 217 |
| Realized gain (loss) on risk management contracts | **(1.44)** | 8.17 | (118) |
| **Operating netback** (1) | **21.41** | 15.37 | 39 |
| General and administrative expenses | **(4.03)** | (2.48) | 63 |
| Restructuring costs | **(1.51)** | - | - |
| Finance charges | **(0.36)** | (6.23) | (94) |
| Other income | **0.07** | - | - |
| Settlement of unutilized take-or-pay contract | **-** | (0.28) | - |
| **Cash netback** (1) | **15.58** | 6.38 | 144 |

*(1) Refer to non–GAAP measures*

The Company's netback will continue to be impacted by swings in oil and natural gas prices and the realized gains or losses on the Company's risk management contracts.

In the first quarter, due to the increase in commodity prices, the Company was able to bring back shut-in production and was able to further reduce operating expenses by using its own infrastructure for handling liquids and continued efforts in the field to manage costs.

The increase in the operating netback before risk management is reflective of the increase in commodity prices combined with savings in operating and transportation. In addition to the increased operating netback, reductions in finance charges as a result of no outstanding indebtedness, have contributed to an increase in the cash netback.

## LIQUIDITY AND CAPITAL RESOURCES

In October 2020, the Company emerged from its CCAA proceedings and concurrently, completed transactions contemplated in the Company's plan of compromise and arrangement (the "Plan"). As part of the Plan, the Company issued Class A common shares for gross proceeds of $31.7 million and compromised $185.9 million of indebtedness. In addition, as part of the Plan, the Company issued 3.3 million New Warrants to Kiwetinohk, which were exercised in January 2021, for aggregate gross proceeds of $40.0 million. In February 2021, the Company closed a private placement of 265,331 Special Warrants issued at a price of $15 per Special Warrant for gross proceeds of $4.0 million.

In February 2021, the Company entered into agreements with Kiwetinohk to participate as to 50 percent in the Simonette Acquisition which closed on April 28, 2021. The Company's share of the purchase price of $160.0 million ($148 million, net of interim closing adjustments), was funded by cash on hand and bank indebtedness of $63.3 million from the Company's New Credit Facility (see "Senior Credit Facility"). The purchase price excludes up to $15 million of contingent payments ($7.5 million for the Company's share) that will be required if the average WTI price, expressed in USD per barrel (calendar month average) of the New York Mercantile Exchange (NYMEX) 1st nearby month Light, Sweet Crude Oil Futures Contract, exceeds USD $56.00 per barrel in 2021 and USD $62.00 per barrel in 2022. Concurrently, with the closing of the Simonette Acquisition, the Company, Kiwetinohk and 1266580 B.C. Ltd., an affiliate of Luminus Energy, entered into a settlement agreement to terminate the rights and obligations under a participation agreement made effective by the parties October 16, 2020. The Company's share of the settlement agreement was $5.75 million and was settled as part of the closing procedures of the Simonette Acquisition.

The Company generally relies on cash flow, equity issuances and its credit facility to fund its capital requirements and provide liquidity. As an oil and natural gas business, Distinction has a declining asset base and therefore relies on oil and natural gas property development and acquisitions to replace produced reserves. Future oil and natural gas production and growth in reserves are highly dependent on the success of exploiting the Company's existing asset base and/or acquiring additional lands or reserves. To the extent Distinction is successful or unsuccessful in these operations, cash flow could be increased or reduced. In addition, Distinction's cash flow depends on a number of factors, including commodity prices, sales volumes, production expenses, transportation expenses and royalties.

Liquidity risk is the risk that Distinction will not be able to meet its financial obligations as they become due. The Company's financial liabilities arise through the cost of operations and the capital program in order to maintain or increase production and develop reserves, the acquisition of crude oil and natural gas assets, financial instrument contracts and borrowings under the Company's credit facility.

Distinction actively manages its liquidity through daily, short term and long-term cash, debt and equity management strategies. Such strategies encompass, among other factors: having adequate sources of financing available through its bank credit facility, forecasting future cash generated from operations based on reasonable production and pricing assumptions and monitoring economic risk management opportunities.

Future liquidity depends primarily on cash flow generated from operations, existing credit facilities and the ability to access debt and equity markets. From time to time, the Company accesses capital markets to meet its additional financing needs and to maintain flexibility in funding its capital expenditure programs or acquisitions. There can be no assurance that future debt financings, equity financings or cash generated from operations will be available or sufficient to meet these or other corporate requirements. If debt or equity financing is available, there is no assurance that it will be on terms acceptable to Distinction.

As at March 31, 2021, the Company had an adjusted net working capital surplus of $89.0 million and currently has a $127.5 million revolving New Credit Facility. Currently, the Company is approximately 50 percent drawn on its New Credit Facility. Together with anticipated cash flow generated from operations, the working capital surplus and undrawn credit facility capacity, the Company anticipates to be in a position that it will be able to meet its working capital requirements.

| **Adjusted net working capital** (1) | **As at March 31, 2021** |
|---|---|
| Current assets | 100,951 |
| Exclusion of the current fair value of financial instruments | - |
| | 100,951 |
| | |
| Current liabilities | 13,209 |
| Exclusion of the current fair value of financial instruments | (1,244) |
| | 11,965 |
| **Adjusted net working capital surplus** | **88,986** |

*(1) Refer to non-GAAP measures*

**Senior Credit Facility**

| | **March 31, 2021** | December 31, 2020 |
|---|---|---|
| Senior Credit Facility | | |
| Bankers' acceptances, net of discount | **-** | - |
| **Balance as at March 31, 2021** | **-** | - |

As at March 31, 2021, the Company had a $30.0 million senior secured revolving credit facility available from a financial institution. The Company did not have an outstanding balance on its senior credit facility during the three months ended March 31, 2021, with the exception of $6.0 million outstanding letters of credit. The senior secured facility was available on a revolving basis until May 31, 2021, with an option to extend, at the lender's discretion. If the revolving period was not extended, the undrawn portion of the facility would be cancelled and the amount outstanding would be required to be repaid at the end of the non-revolving term being May 29, 2022.

Subsequent to March 31, 2021 and concurrently with the closing of the Simonette Acquisition, the Company's credit facility was amended and restated. The New Credit Facility has a borrowing base of $127.5 million and is provided by a syndicate of lenders. The New Credit Facility is a 364 day committed facility available on a revolving basis until May 31, 2022 at which time it may be extended at the lenders' option. If the revolving period is not extended, the undrawn portion of the New Credit Facility will be cancelled and the amount outstanding would be required to be repaid at the end of the non-revolving term being May 31, 2023. The non-extension provisions are applicable to the lenders on an individual basis. The borrowing base of the New Credit Facility will be based on the lenders' evaluation of the Company's petroleum and natural gas reserves at the time and commodity prices. A decrease in the borrowing base could result in a reduction to the New Credit Facility, which may require a repayment to the lenders.

Interest payable on amounts drawn under the New Credit Facility is at the prevailing bankers' acceptance or LIBOR rates plus stamping fees, lenders' prime rate or U.S. base rate plus the applicable margins, depending on the form of borrowing by the Company. The applicable margins and stamping fees are based on a sliding scale pricing grid tied to the Company's debt to earnings before interest, taxes, depreciation and amortization ratio: from a minimum of the bank's prime rate or U.S. base rate plus an applicable margin ranging from 1.75 percent to 5.25 percent or from a minimum of bankers' acceptances or LIBOR rate plus a stamping fee ranging from 2.75 percent to 6.25 percent.

The New Credit Facility is secured by a $300.0 million demand floating charge debenture and a general security agreement over all assets of the Company.

The Company was not subject to financial covenants under the credit facility existing as at March 31, 2021 and is not subject to financial covenants under the New Credit Facility.

### Share Capital

In accordance with the policies of the TSX, in connection with the CCAA proceedings, the common shares and other securities of the Company were delisted from the TSX effective at the close of market trading on May 21, 2020.

As at May 20, 2021, the Company had 9.7 million Class A common shares outstanding, 0.3 million stock options outstanding, 0.3 million restricted share units convertible into Class A common shares, and 0.3 million Special Warrants outstanding. The stock options and restricted share units have an average exercise price of $15.00 per option and $0.01 per restricted share unit, respectively. The Special Warrants are automatically converted into one Class A common share of the Company on June 25, 2021.

## CONTRACTUAL OBLIGATIONS OUTSTANDING

The future minimum commitments over the next five years ending on December 31 are as follows:

| | 2021 | 2022 | 2023 | 2024 | 2025 | Thereafter |
|---|---|---|---|---|---|---|
| Gathering, processing and transportation (1) | 8,439 | 14,138 | 14,148 | 14,176 | 12,036 | 305 |
| Office, equipment and software leases | 458 | 448 | 375 | 287 | - | - |
| Accounts payable and accrued liabilities | 11,413 | - | - | - | - | - |
| Decommissioning obligations (2) | 428 | 2,898 | 3,738 | 57 | 177 | 24,768 |
| Management services fee (3) | 2,672 | 2,685 | 2,233 | 1,950 | 1,681 | 204 |
| Transportation related to Simonette Acquisition | 12,400 | 18,600 | 18,600 | 18,600 | 15,500 | - |
| Total | 35,810 | 38,769 | 39,094 | 35,070 | 29,394 | 25,277 |

*(1) Balances denominated in U.S. dollars have been translated at the March 31, 2021 exchange rate.*
*(2) Amounts represent the inflated, discounted future abandonment and reclamation expenditures anticipated to be incurred over the life of the Company's properties.*
*(3) In accordance with the Management Services Agreement between the Company and Kiwetinohk dated July 5, 2020 and amended and restated April 28, 2021 as filed on www.sedar.com.*

## GUARANTEES AND OFF-BALANCE SHEET ARRANGEMENTS

Distinction has not entered into any guarantees or off-balance sheet arrangements other than those previously disclosed in the future minimum commitments table above.

## RELATED PARTIES

As part of the restructuring contemplated under the Plan, in October 2020, the Company issued Kiwetinohk 25 percent of the issued and outstanding Class A common shares (on a non-diluted basis) plus 3.3 million New Warrants exercisable into Class A common shares of the Company. On January 15, 2021, Kiwetinohk exercised their 3.3 million New Warrants to purchase 3.3 million Class A common shares of the Company at an aggregate exercise price of $11.94 per warrant, increasing their ownership to 51.6 percent of the outstanding Class A common shares of the Company. The Chief Executive Officer of Kiwetinohk is also the Chief Executive Officer and board member of Distinction.

The Company and Kiwetinohk are parties to a Management Services Agreement (the "MSA"). The MSA, among other things, requires Kiwetinohk to provide management services to the Company in exchange for a monthly fee payable to Kiwetinohk. The MSA had a termination date of October 16, 2021. Concurrently, with the closing of the Simonette Acquisition, the MSA was amended and restated, among other things, to extend the termination date to February 17, 2026. In the three months ended March 31, 2021, the Company has recognized $0.6 million of monthly MSA fees payable to Kiwetinohk.

Concurrently, with the closing of the Simonette Acquisition, the Company, Kiwetinohk and 1266580 B.C. Ltd., an affiliate of Luminus Energy, entered into a settlement agreement to terminate the rights and obligations under a participation agreement made effective by the parties October 16, 2020. The Company's share of the settlement agreement is $5.75 million and was settled and paid to 1266580 B.C. Ltd. as part of the closing procedures of the Simonette Acquisition.

On April 28, 2021 Distinction entered into three marketing agreements with Kiwetinohk for natural gas, condensate and NGLs production volumes associated with the Simonette Acquisition. Kiwetinohk will market all of Distinction's production from the Simonette Acquisition and will also purchase natural gas volumes above production required to fill Distinction's net 45 mmcf/d of contracted capacity on the Alliance Pipeline. Natural gas purchases required to fill the capacity above expected production have been fully contracted through October 31, 2021. The marketing profits based upon actual revenues and costs will be shared equally with Distinction and Kiwetinohk for their respective volumes.

## SELECTED INFORMATION

The following table summarizes the Company's financial and operating results over the past eight quarters:

| | Mar 31, 2021 | Dec 31, 2020 | Sep 30, 2020 | Jun 30, 2020 | Mar 31, 2020 | Dec 31, 2019 | Sep 30, 2019 | Jun 30, 2019 |
|---|---|---|---|---|---|---|---|---|
| **Production**<br>(boe conversion – 6:1 basis) | | | | | | | | |
| Field condensate (bbls/d) | 1,740 | 2,065 | 2,153 | 2,300 | 1,683 | 1,747 | 2,154 | 2,762 |
| Natural gas liquids (bbls/d) | 880 | 944 | 849 | 840 | 958 | 1,027 | 1,299 | 1,245 |
| Natural gas (mcf/d) | 22,566 | 22,691 | 21,800 | 20,897 | 23,601 | 25,487 | 29,600 | 30,897 |
| Barrels of oil equivalent (boe/d) | 6,381 | 6,791 | 6,635 | 6,623 | 6,575 | 7,022 | 8,386 | 9,157 |
| **Financial**<br>($ thousands, except per share) | | | | | | | | |
| Crude oil and natural gas sales | 21,665 | 17,048 | 15,750 | 9,316 | 14,259 | 19,147 | 20,612 | 27,026 |
| Net loss | (5,175) | 130,601 | (9,212) | (22,164) | (109,970) | (13,082) | 10,628 | (53,620) |
| Per share – basic (2) | (0.58) | 21.45 | (1.51) | (3.64) | (18.06) | (2.15) | 1.75 | (8.81) |
| Per share – diluted(2) | (0.58) | 20.54 | (1.51) | (3.64) | (18.06) | (2.15) | 1.75 | (8.81) |
| Adjusted funds flow(1) | 8,939 | 579 | (1,381) | 9,025 | 3,819 | 6,573 | 21,291 | 11,963 |
| Per share – basic & diluted (1)(2) | 1.01 | 0.09 | (0.23) | 1.48 | 0.18 | 1.08 | 3.50 | 1.96 |

*(1) Refer to non-GAAP measures*
*(2) Per share amounts have been adjusted to reflect the Company's restructuring activities under the Plan.*

Over the past two years, the changes in revenue and funds from operations from quarter to quarter primarily reflect the change in production and the volatility of commodity prices. Production has been impacted by production performance, shut-in production and new wells through successful drilling.

In the first quarter of 2019, Distinction concluded drilling the last well on its four-well pad, completed fracturing operations and commenced equipping operations. The four-well pad was tied in and brought on-stream throughout the second quarter of 2019, increasing production to 9,157 boe/d from 8,759 boe/d in the first quarter of 2019. The Company did not drill additional wells in 2019. Production in the third and fourth quarter of 2019 decreased to 8,386 boe/d and 7,022 boe/d, respectively.

In the first three months of 2020, Distinction drilled three wells in liquids-rich West Bigstone. Two of the three wells have been brought on-stream and produced throughout the second quarter. These wells are the only new wells brought on production since the Company brought on production a four-well (2.6 net) pad in West Bigstone in the second quarter of 2019. In response to the steep decline in crude oil prices, the Company delayed the start-up of the third well from the winter 2020 program and shut-in production throughout the month of April and May. Production in the second quarter averaged 6,623 boe/d, up marginally from the 6,575 boe/d produced in the first quarter of 2020 and down 28 percent from the comparative quarter in 2019. As commodity prices started to improve throughout the third quarter of 2020, the third well from the winter 2020 program was brought onstream on September 3, 2020. Production in the third quarter and fourth quarter of 2020 averaged 6,635 boe/d and 6,791 boe/d. In the first quarter of 2021, the Company brought six (4.6 net) wells on-stream that were previously shut-in, contributing to the 6,381 boe/d produced in the quarter.

## CRITICAL ACCOUNTING ESTIMATES

The reader is advised that the critical accounting estimates, judgments, policies and practices as described in the Company's Management's Discussion and Analysis for the year ended December 31, 2020 continue to be critical in determining Distinction's financial results.

The condensed consolidated interim financial statements have been prepared in conformity with IAS 34, Interim Financial Reporting, which requires management to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, shareholders' equity, revenue and expenses. Actual results may differ from these estimates.

## CORPORATE GOVERNANCE

The shareholders' interests are a critical factor in the operations and management of Distinction. The Company is committed to maintaining the highest level of investor confidence in the Company through the application of its corporate policies and procedures. Distinction's Board of Directors consists of four independent directors and one officer of the Company who meet regularly to discuss matters of strategy and execution of the business plan. See Distinction's Management Information Circular and Annual Information Form for a listing of committees that oversee specific aspects of the Company's operating and financial strategy.

## NON-GAAP MEASURES

Management uses certain measures that are not recognized under International Financial Reporting Standards ("IFRS") to help evaluate the performance of the Company. The following are terms and definitions contained within this MD&A that are not recognized measures under IFRS:

The use of the boe unit of measurement may be misleading, particularly if used in isolation. A boe conversion ratio of 6 mcf of natural gas to 1 barrel of oil is based on an energy equivalency conversion method primarily applicable at the burner tip and does not represent a value equivalency at the wellhead. In addition, given that the value ratio based on the current price of oil as compared with natural gas is significantly different from the energy equivalent of six to one, utilizing a BOE conversion ratio of 6 Mcf: 1 bbl would be misleading as an indication of value. Distinction's reported production is a mix of shale gas and natural gas liquids. This conversion conforms to the Canadian Securities Administrators' National Instrument 51-101 when boes are disclosed.

Adjusted funds flow - cash flow from operating activities before decommissioning expenditures and changes in non-cash working capital from operating activities. Management uses adjusted funds flow to analyze performance and considers it a key measure as it demonstrates the Company's ability to generate the cash necessary to fund future capital investments, abandonment obligations and to repay debt. Distinction's determination of adjusted funds flow may not be comparable to that reported by other companies nor should it be viewed as an alternative to cash flow from operating activities, net earnings (loss) or other measures of financial performance calculated in accordance with IFRS.

Adjusted funds flow per share – adjusted funds flow divided by the number of common shares outstanding calculated using weighted average shares outstanding consistent with the calculation of earnings (loss) per share.

Adjusted working capital – current assets and current liabilities exclude the current portion of the fair value of the financial instruments. This definition is used by the Company to monitor normal course working capital and in determining its net debt.

Cash flow from operating activities per share – cash flow from operating activities divided by the number of common shares outstanding calculated using weighted average shares outstanding consistent with the calculation of earnings (loss) per share.

Marketing income (loss) - the margin earned on the sale of purchased third party natural gas volumes and premiums or discounts on the assignment of capacity on the Alliance pipeline system to a third party. Management considers marketing income (loss) important measures of the Company's ability to mitigate the cost of excess committed capacity.

Net debt (surplus) – the sum of senior credit facility plus (minus) the adjusted working capital deficit (surplus). Net debt is used by management to monitor its leverage levels.

Management considers netbacks as an important measure of the cash generating capability of the produced volumes. Netbacks are generally discussed and presented on a per boe basis.

Operating netbacks – crude oil and natural gas sales plus realized gains (losses) on financial instruments and marketing income (loss) less royalties, operating and transportation costs. Management considers operating netbacks per boe an important measure of profitability relative to current commodity prices and costs of production.

Cash netbacks - operating netbacks less interest on bank debt and senior secured notes, finance charges associated with lease obligations, foreign exchange, general and administrative costs, restructuring costs, and the settlement of the unutilized take-or-pay contract. Management considers cash netbacks per boe an important measure as it demonstrates the cash realized on each unit of production to be reinvested in future capital investment or repay debt.

## FORWARD-LOOKING STATEMENTS

This management discussion and analysis contains forward-looking statements and forward-looking information within the meaning of applicable Canadian securities laws. These statements relate to future events or the Company's future performance and are based upon the Company's internal assumptions and expectations. All statements other than statements of present or historical fact are forward-looking statements. Forward-looking statements are often, but not always, identified by the use of any of the words "expect", "anticipate", "continue", "estimate", "may", "will", "should", "believe", "intends", "forecast", "plans", "guidance", "budget" and similar expressions.

More particularly and without limitation, this management discussion and analysis contains forward-looking statements and information relating to the impact of COIVD-19 on the operations of the Company, petroleum and natural gas production estimates and weighting, projected crude oil and natural gas prices, future exchange rates, expectations as to royalty rates, expectations as to transportation and operating costs, expectations as to general and administrative costs and interest expense, expectations as to capital expenditures and net debt, planned capital spending, future liquidity and Distinction's ability to fund ongoing capital requirements through operating cash flows and its credit facilities, estimated tax pools and expectations regarding current income taxes payable by Distinction, supply and demand fundamentals for oil and gas commodities, timing and success of development and exploitation activities, cash availability for the financing of capital expenditures, access to third-party infrastructure, treatment under governmental regulatory regimes and tax laws and future environmental regulations.

Furthermore, statements relating to "reserves" are deemed to be forward-looking statements as they involve the implied assessment, based on certain estimates and assumptions that the reserves described can be profitable in the future.

The forward-looking statements and information contained in this management discussion and analysis are based on certain key expectations and assumptions made by Distinction. The following are certain material assumptions on which the forward-looking statements and information contained in this management discussion and analysis are based: the stability of the global and national economic environment, the stability of and commercial acceptability of tax, royalty and regulatory regimes applicable to Distinction, exploitation and development activities being consistent with management's expectations, production levels of Distinction being consistent with management's expectations, the absence of significant project delays, the stability of oil and gas prices, the absence of significant fluctuations in foreign exchange rates and interest rates, the stability of costs of oil and gas development and production in Western Canada, including operating costs, the timing and size of development plans and capital expenditures, availability of third party infrastructure for transportation, processing or marketing of oil and natural gas volumes, prices and availability of oilfield services and equipment being consistent with management's expectations, the availability of, and competition for, among other things, pipeline capacity, skilled personnel and drilling and related services and equipment, results of development and exploitation activities that are consistent with management's expectations, the availability of capital, weather affecting Distinction's ability to develop and produce as expected, contracted parties providing goods and services on the agreed timeframes, Distinction's ability to manage environmental risks and hazards and the cost of complying with environmental regulations, the accuracy of operating cost estimates, the accurate estimation of oil and gas reserves, future exploitation, development and production results and Distinction's ability to market oil and natural gas successfully to current and new customers. Additionally, estimates as to expected average annual production rates assume that no unexpected outages occur in the infrastructure that the Company relies on to produce its wells, that existing wells continue to meet production expectations and any future wells scheduled to come on in the coming year meet timing and production expectations.

Commodity prices used in the determination of forecast revenues are based upon general economic conditions, commodity supply and demand forecasts and publicly available price forecasts.

Financial outlook information contained in this management discussion and analysis about prospective results of operations, financial position or cash flows is based on assumptions about future events, including economic conditions and proposed courses of action, based on management's assessment of the relevant information currently available. This financial outlook is included to provide readers with an understanding of the Company's operations for 2021 and readers are cautioned that such financial outlook information contained in this management discussion and analysis should not be used for purposes other than for which it is disclosed.

Although the Company believes that the expectations reflected in such forward-looking statements and information are reasonable, it can give no assurance that such expectations will prove to be correct and such forward-looking statements should not be unduly relied upon. Since forward-looking statements and information address future events and conditions, by their very nature they involve inherent known and unknown risks and uncertainties. Distinction's actual results, performance or achievements could differ materially from those expressed in, or implied by, these forward-looking statements and, accordingly, no assurance can be given that any of the events anticipated by the forward-looking statements will transpire or occur, or if any of them do so, what benefits Distinction will derive therefrom. Should one or more of these risks or uncertainties materialize, or should assumptions underlying forward-looking statements prove incorrect, actual results may vary materially from those currently anticipated due to a number of factors and risks. These include, but are not limited to, the impact of COVID-19 on the operations of the Company, the oil and gas industry in general such as operational risks in development, exploration and production, delays or changes in plans with respect to exploration or development projects or capital expenditures, the uncertainty of estimates and projections relating to production rates, costs and expenses, commodity price and exchange rate fluctuations, marketing and transportation risks, environmental risks, competition from others for scarce resources, the inability to access sufficient capital from internal and external sources, adverse changes in governmental regulation of the oil and gas industry and adverse changes in tax, royalty and environmental legislation. Additional information on these and other factors that could affect the Company's operations or financial results are included in the Company's most recent Annual Information Form and other reports on file with the applicable securities regulatory authorities and may be accessed through the SEDAR website (www.sedar.com).

Readers are cautioned that the foregoing list of factors is not exhaustive. Furthermore, the forward-looking statements contained in this MD&A are made as of the date of this MD&A for the purpose of providing the readers with the Company's expectations for the coming year. The forward-looking statements and information may not be appropriate for other purposes. Distinction undertakes no obligation to update publicly or revise any forward-looking statements or information, whether as a result of new information, future events or otherwise, unless so required by applicable securities laws. The forward-looking statements contained in this management discussion and analysis are expressly qualified in their entirety by this cautionary statement.

# DISTINCTION ENERGY CORP.

**Condensed Consolidated Interim Statements of Financial Position**
**As at**

| (thousands of dollars) | **March 31, 2021** | December 31, 2020 |
|---|---|---|
| (unaudited) | | |
| **Assets** | | |
| Current assets | | |
| Cash | **87,531** | 45,912 |
| Accounts receivable | **9,719** | 8,127 |
| Prepaid expenses | **3,701** | 3,017 |
| | **100,951** | 57,056 |
| Deposit on Simonette Acquisition (Note 15) | **7,500** | - |
| Fair value of financial instruments (Note 5) | **387** | 166 |
| Exploration and evaluation (Note 6) | **3,256** | 9,072 |
| Property, plant and equipment (Note 7) | **219,620** | 227,225 |
| Total assets | **331,714** | 293,519 |
| **Liabilities** | | |
| Current liabilities | | |
| Accounts payable and accrued liabilities | **11,413** | 11,736 |
| Lease obligations | **124** | 123 |
| Fair value of financial instruments (Note 5) | **1,244** | 53 |
| Decommissioning obligations (Note 8) | **428** | 147 |
| | **13,209** | 12,059 |
| Lease obligations | **597** | 628 |
| Decommissioning obligations (Note 8) | **31,638** | 34,652 |
| Total liabilities | **45,444** | 47,339 |
| **Shareholders' equity** | | |
| Share capital (Note 10) | **175,955** | 131,454 |
| Warrants (Note 10) | **3,783** | 4,594 |
| Contributed surplus | **396,977** | 395,402 |
| Deficit | **(290,445)** | (285,270) |
| Total shareholders' equity | **286,270** | 246,180 |
| Total liabilities and shareholders' equity | **331,714** | 293,519 |

See accompanying notes to the condensed consolidated interim financial statements.

Subsequent events (Notes 9, 10, 12, 15)

# DISTINCTION ENERGY CORP.

**Condensed Consolidated Interim Statements of Loss and Comprehensive Loss**
**For the three months ended March 31,**

| (thousands of dollars, except per share amounts) | **2021** | 2020 |
|---|---|---|
| (unaudited) | | |
| **Revenues** | | |
| Crude oil and natural gas sales (Note 11) | **21,665** | 14,259 |
| Marketing revenue | **2,112** | 951 |
| Royalties | **(1,531)** | (1,117) |
| Other income | **38** | - |
| | **22,284** | 14,093 |
| Realized gain (loss) on financial instruments (Note 5) | **(825)** | 4,889 |
| Unrealized gain (loss) on financial instruments (Note 5) | **(970)** | 9,400 |
| | **20,489** | 28,382 |
| **Expenses** | | |
| Operating | **5,147** | 6,059 |
| Transportation | **2,081** | 2,343 |
| Marketing | **1,899** | 1,382 |
| General and administrative | **2,316** | 1,483 |
| Restructuring costs (note 13) | **868** | - |
| Share-based compensation (recovery) | **1,575** | (4) |
| Exploration and exploration (Note 6) | **5,816** | - |
| Depletion, depreciation and impairment (Note 7) | **5,598** | 122,604 |
| | **25,300** | 133,867 |
| Finance costs | **364** | 4,485 |
| Net loss and comprehensive loss | **(5,175)** | (109,970) |

| | | |
|---|---|---|
| Net loss per share (Note 10) | | |
| Basic and diluted (note 2(d)) | **(0.58)** | (18.06) |

See accompanying notes to the condensed consolidated interim financial statements.

# DISTINCTION ENERGY CORP.

**Condensed Consolidated Interim Statements of Changes in Shareholders' Equity**
**For the three months ended March 31,**

| (thousands of dollars) | **2021** | 2020 |
|---|---|---|
| (unaudited) | | |
| **Share capital** (Note 10) | | |
| **Common shares** | | |
| Balance, beginning of period | **131,454** | 353,842 |
| Issued on exercise of warrants | **40,000** | - |
| Transferred on exercise of warrants | **4,594** | - |
| Private placement | **-** | 10,000 |
| Share issue costs | **(93)** | (159) |
| Balance, end of period | **175,955** | 363,683 |
| **Warrants** | | |
| Balance, beginning period | **4,594** | 5,627 |
| Issued | **3,980** | - |
| Warrant issue costs | **(197)** | - |
| Transferred on exercise of warrants | **(4,594)** | - |
| Balance, end of period | **3,783** | 5,627 |
| **Contributed surplus** | | |
| Balance, beginning of period | **395,402** | 22,201 |
| Share-based compensation | **1,575** | (2) |
| Balance, end of period | **396,977** | 22,199 |
| **Deficit** | | |
| Balance, beginning of period | **(285,270)** | (274,411) |
| Net loss | **(5,175)** | (109,970) |
| Balance, end of period | **(290,445)** | (384,381) |
| Total shareholders' equity | **286,270** | 7,128 |

See accompanying notes to the condensed consolidated interim financial statements.

# DISTINCTION ENERGY CORP.

**Condensed Consolidated Interim Statements of Cash Flows**
**For the three months ended March 31,**

| (thousands of dollars) | **2021** | 2020 |
|---|---|---|
| (unaudited) | | |
| **Cash flow from (used in) operating activities** | | |
| Net loss | **(5,175)** | (109,970) |
| Adjustments for: | | |
| Depletion, depreciation and impairment (Note 7) | **5,598** | 122,604 |
| Exploration and evaluation (Note 6) | **5,816** | - |
| Accretion and finance charges | **155** | 759 |
| Share-based compensation (recovery) | **1,575** | (4) |
| Unrealized (gain) loss on financial instruments | **970** | (9,400) |
| Settlement of unutilized take-or-pay contract | **-** | (170) |
| Decommissioning expenditures (Note 8) | **(17)** | (574) |
| Change in non-cash working capital (Note 14) | **(2,689)** | 3,585 |
| | **6,233** | 6,830 |
| **Cash flow from (used in) financing activities** | | |
| Decrease in senior credit facility | **-** | (1,884) |
| Issue of shares, net of transaction costs (Note 10) | **39,907** | 9,841 |
| Issue of warrants, net of transaction costs (Note 10) | **3,783** | - |
| Payment of lease obligations | **(30)** | (153) |
| Issue of senior secured notes, net of issue costs | **-** | 5,414 |
| | **43,660** | 13,218 |
| **Cash flow from (used in) investing activities** | | |
| Additions to exploration and evaluation assets | **-** | (97) |
| Additions to property, plant and equipment | **(864)** | (22,191) |
| Deposit on Simonette Acquisition (Note 15) | **(7,500)** | - |
| Change in non-cash working capital (Note 14) | **90** | 21,171 |
| | **(8,274)** | (1,117) |
| Increase in cash and cash equivalents | **41,619** | 18,931 |
| Cash and cash equivalents, beginning of period | **45,912** | 526 |
| Cash and cash equivalents, end of period | **87,531** | 19,457 |
| Cash interest paid | **102** | 2,922 |

See accompanying notes to the condensed consolidated interim financial statements.

## 1) STRUCTURE OF DISTINCTION

Distinction Energy Corp. ("Distinction" or the "Company") is a reporting issuer engaged in the exploration for, development and production of crude oil and natural gas from properties and assets located in Western Canada in which it holds an interest. The Company's operations are concentrated in the Deep Basin of Northwest Alberta, from which in excess of 95 percent of the Company's production is obtained. The head office of the Company is located at Suite 2300, 333 – 7th Avenue S.W., Calgary, Alberta, T2P 2Z1.

In April 2020, Delphi Energy Corp. (now Distinction) filed for protection under the Companies' Creditors Arrangement Act ("CCAA"). In October 2020, the Company emerged from CCAA and concurrently completed transactions (see notes 10, 12 and 13) contemplated in the Company's plan of compromise and arrangement (the "Plan").

The condensed consolidated interim financial statements as at and for the three months ended March 31, 2021 and 2020 comprise the accounts of the Company, its wholly-owned subsidiaries and a partnership. As further disclosed in Note 12, Kiwetinohk Resources Corp. ("Kiwetinohk") and Luminus Energy IE Designated Activity Company ("Luminus Energy") hold approximately 51.6 percent and 27.6 percent, respectively, of the issued and outstanding common shares of the Company as at March 31, 2021.

## 2) BASIS OF PRESENTATION

### (a) Statement of compliance and authorization

These condensed consolidated interim financial statements are unaudited and prepared in accordance with International Accounting Standard 34, "Interim Financial Reporting" as issued by the International Accounting Standards Board, and do not include all of the information and disclosures normally provided in annual financial statements and should be read in conjunction with the Company's consolidated financial statements for the year ended December 31, 2020.

These condensed consolidated interim financial statements were approved and authorized for issuance by the Board of Directors on May 20, 2021.

### (b) Basis of measurement and functional currency

The condensed consolidated interim financial statements have been prepared using historical costs, except for derivative financial instruments which are measured at fair value. The financial statements are presented in Canadian dollars, the Company's functional currency, and are rounded to the nearest thousand (unless stated otherwise).

### (c) Basis of presentation

The consolidated financial statements have been prepared on a going concern basis, using historical costs, except for derivative financial instruments which are measured at fair value. The financial statements are presented in Canadian dollars, the Company's functional currency and rounded to the nearest thousand (unless stated otherwise).

### (d) Loss per share presentation

As part of the Plan, all of the previously existing common shares, options and warrants of Distinction were cancelled and extinguished for no consideration and a new class A common shares were issued on October 16, 2020. In accordance with International Accounting Standards 33 – Earnings per Share ("IAS 33"), per share calculations presented should be based on the new number of outstanding shares if the number of outstanding shares changes as a result of a recapitalization. Accordingly, the weighted average common shares used for the comparative periods presented have been adjusted to reflect the Class A common shares outstanding as a result of the Company's restructuring under the Plan.

### (e) Use of estimates and judgments

The preparation of the condensed consolidated interim financial statements in conformity with International Financial Reporting Standards ("IFRS") requires management to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amounts in the condensed consolidated interim financial statements and accompanying notes. By their nature, these estimates are subject to measurement uncertainty and the effect on the financial statements of changes in such estimates in future periods could be material. Actual results may differ from these estimates. Estimates and judgments are continuously evaluated and are based on management's experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

Since the World Health Organization declared novel coronavirus COVID-19 ("COVID-19") a global pandemic in 2020, global economies have experienced varying degrees of economic recovery and subsequent virus outbreak. The COVID-19 pandemic and the anticipated subsequent economic recovery continues to drive the global demand for crude oil and natural gas and related prices, which in turn has had a significant impact on Distinction's commodity sales from production. The COVID-19 pandemic is an evolving situation that will continue to have widespread implications for our business environment, operations and financial conditions. Management cannot reasonably estimate the length or severity of this pandemic, or the extent to which the disruption may materially impact our consolidated statement of loss and comprehensive loss, statement of financial position, or statement of cash flows in fiscal 2021. The potential direct and indirect impacts of the economic downturn have been considered in management's estimates and assumptions at period end and have been reflected in our results.

In preparing these condensed consolidated interim financial statements, other than the critical judgments noted above that management has incorporated into the process, Distinction's accounting policies were the same as those applied to the consolidated financial statements as at and for the year ended December 31, 2020.

**3) SIGNIFICANT ACCOUNTING POLICIES**

The accounting policies applied by the Company in these condensed consolidated interim financial statements are the same as those applied by the Company in its consolidated financial statements as at and for the year ended December 31, 2020.

**4) DETERMINATION OF FAIR VALUES**

A number of the Company's accounting policies and disclosures require the determination of fair value for both financial and non-financial assets and liabilities. IFRS establishes a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The three levels of the fair value hierarchy are described as follows:

*Level 1* – Quoted prices are available in active markets for identical assets or liabilities as of the reporting date. Active markets are those in which transactions occur in sufficient frequency and volume to provide pricing information on an ongoing basis.

*Level 2* – Valuations are based on inputs, including quoted forward prices for commodities, time value and volatility factors which can be substantially observed or corroborated in the marketplace.

*Level 3* – Valuations in this level are those with inputs for the asset / or liability that are not based on observable market data.

Fair values have been determined for measurement and/or disclosure purposes based on the following methods:

**(a) Cash and cash equivalents, accounts receivable and accounts payable and accrued liabilities:**

The fair value of cash and cash equivalents, accounts receivable and accounts payable and accrued liabilities approximate their carrying value due to their short term to maturity.

**(b) Derivatives:**

Distinction's foreign exchange, basis differential and commodity contracts are measured at level 2 of the fair value hierarchy. The fair value of commodity contracts is determined by discounting the remaining contracted petroleum and natural gas volumes by the difference between the contracted price and published forward price curves as at the consolidated financial position date. The fair value of foreign exchange rate swap contracts is determined by discounting the net future cash flows based on the fixed and floating rates associated with the notional amounts.

**(c) Share Awards:**

The fair values of share awards are measured using a Black-Scholes option pricing model. Measurement inputs include share price on measurement date, exercise price of the instrument, expected volatility, weighted average expected life of the instruments, expected dividends and the risk-free interest rate.

**5) FINANCIAL RISK MANAGEMENT**

In an effort to mitigate commodity price fluctuations for natural gas, crude oil and natural gas liquids, Distinction enters into financial commodity contracts as part of its risk management program designed to protect cash flows associated with base production.

With respect to financial contracts, which are derivative financial instruments, management has elected not to use hedge accounting and consequently records the fair value of its natural gas, basis differential contracts and crude oil financial contracts on the statement of financial position at each reporting period with the change in the fair value of the financial contracts being classified as unrealized gains and losses in the consolidated statement of loss.

| **Contract Type** | **March 31, 2021** | **December 31, 2020** |
|---|---|---|
| Natural gas contracts asset (liability) | **(173)** | 805 |
| Crude oil contracts liability | **(684)** | (692) |
| Net risk management contracts asset (liability) | **(857)** | 113 |

For the three months ended March 31, 2021, Distinction realized a $0.8 million loss on its risk management contracts (2020: $4.9 million gain).

For the three months ended March 31, 2021, Distinction recorded an unrealized loss on its risk management contracts of $1.0 million (2020: $9.4 million gain). The unrealized loss recognized for the three months ended March 31, 2021 is the difference between the fair values of the risk management contracts outstanding as at March 31, 2021 and the fair values as at December 31, 2020.

As at March 31, 2021, the Company had the following commodity risk management contracts outstanding:

**Crude Oil Contracts**

| Time Period | Type of Contract | Quantity Contracted | Price ($/unit) | Reference |
|---|---|---|---|---|
| April 2021 – December 2021 | Fixed price swap | 125 bbls/d | $58.50 Cdn | WTI |
| April 2021 – December 2021 | Fixed price swap | 125 bbls/d | $56.20 Cdn | WTI |
| April 2021 – December 2021 | Fixed price swap | 125 bbls/d | $55.70 Cdn | WTI |
| April 2021 | Fixed price swap | 150 bbls/d | $78.45 Cdn | WTI |
| May 2021– December 2021 | Fixed price swap | 750 bbls/d | $75.05 Cdn | WTI |
| January 2022 – December 2022 | Fixed price swap | 750 bbls/d | $69.95 Cdn | WTI |

**Natural Gas Contracts**

| Time Period | Type of Contract | Quantity Contracted | Price ($/unit) | Reference |
|---|---|---|---|---|
| April 2021 – December 2021 | Fixed price swap | 1,575 gj/d | $2.43 Cdn | AECO |
| April 2021 – December 2021 | Fixed price swap | 1,575 gj/d | $2.27 Cdn | AECO |
| April 2021 – December 2021 | Fixed price swap | 1,575 gj/d | $2.27 Cdn | AECO |
| January 2022 – June 2022 | Fixed price swap | 750 gj/d | $2.49 Cdn | AECO |
| January 2022 – June 2022 | Fixed price swap | 750 gj/d | $2.37 Cdn | AECO |
| January 2022 – June 2022 | Fixed price swap | 750 gj/d | $2.30 Cdn | AECO |
| July 2022 – December 2022 | Fixed price swap | 675 gj/d | $2.25 Cdn | AECO |
| July 2022 – December 2022 | Fixed price swap | 675 gj/d | $2.24 Cdn | AECO |
| July 2022 – December 2022 | Fixed price swap | 675 gj/d | $2.13 Cdn | AECO |
| April 2021 – December 2021 | Fixed price swap | 1,475 mmbtu/d | $3.81 Cdn | NYMEX |
| April 2021 – December 2021 | Fixed price swap | 1,475 mmbtu/d | $3.59 Cdn | NYMEX |
| April 2021 – December 2021 | Fixed price swap | 1,475 mmbtu/d | $3.56 Cdn | NYMEX |
| January 2022 – June 2022 | Fixed price swap | 700 mmbtu/d | $3.69 Cdn | NYMEX |
| January 2022 – June 2022 | Fixed price swap | 700 mmbtu/d | $3.59 Cdn | NYMEX |
| January 2022 – June 2022 | Fixed price swap | 700 mmbtu/d | $3.51 Cdn | NYMEX |
| July 2022 – December 2022 | Fixed price swap | 650 mmbtu/d | $3.41 Cdn | NYMEX |
| July 2022 – December 2022 | Fixed price swap | 650 mmbtu/d | $3.44 Cdn | NYMEX |
| July 2022 – December 2022 | Fixed price swap | 650 mmbtu/d | $3.31 Cdn | NYMEX |
| April 2021 – December 2021 | Fixed price swap | 7,500 mmbtu/d | $3.61 Cdn | NYMEX |
| January 2022 – December 2022 | Fixed price swap | 2,500 mmbtu/d | $3.30 Cdn | NYMEX |

**Basis Differential Contracts**

Prior to the closing of the Simonette Acquisition (Note 15), approximately half of Distinction's natural gas production was shipped through the Alliance pipeline system into the Chicago market. As a result, the Company has entered into NYMEX to Chicago basis differential contracts in order to fix the basis on a portion of its natural gas sales in the Chicago market.

| Time Period | Type of Contract | Quantity Contracted | Differential (U.S. $/unit)) |
|---|---|---|---|
| April 2021 – December 2021 | Fixed price swap | 1,475 mmbtu/d | ($0.240) |
| April 2021 – December 2021 | Fixed price swap | 1,475 mmbtu/d | ($0.255) |
| April 2021 – December 2021 | Fixed price swap | 1,475 mmbtu/d | ($0.260) |
| January 2022 – June 2022 | Fixed price swap | 700 mmbtu/d | ($0.100) |
| January 2022 – June 2022 | Fixed price swap | 700 mmbtu/d | ($0.110) |
| January 2022 – June 2022 | Fixed price swap | 700 mmbtu/d | ($0.195) |
| July 2022 – December 2022 | Fixed price swap | 650 mmbtu/d | ($0.225) |
| July 2022 – December 2022 | Fixed price swap | 650 mmbtu/d | ($0.210) |
| July 2022 – December 2022 | Fixed price swap | 650 mmbtu/d | ($0.250) |
| April 2021 – December 2021 | Fixed price swap | 7,500 mmbtu/d | ($0.190) |
| January 2022– December 2022 | Fixed price swap | 2,500 mmbtu/d | ($0.095) |

## 6) EXPLORATION AND EVALUATION ASSETS

| | |
|---|---|
| Balance at December 31, 2019 | 8,963 |
| Additions | 109 |
| **Balance at December 31, 2020** | **9,072** |
| Land expiries and write-offs | (5,816) |
| **Balance as at March 31, 2021** | **3,256** |

Exploration and evaluation assets consist of the Company's exploration projects which are pending the determination of proven and probable reserves.

During the first three months of 2021, Distinction wrote-down $5.8 million of exploration and evaluation. As at March 31, 2021, the Company evaluated upcoming land expiries, the related book value and all capitalized general and administrative costs and determined that the recoverability of the exploration and evaluation assets are no longer supportable as the Company does not intend to develop the associated assets primarily as a result of competing investment opportunities.

## 7) PROPERTY, PLANT AND EQUIPMENT

| Cost | Crude oil and natural gas properties | Production equipment | Other assets | Total |
|---|---|---|---|---|
| Balance at December 31, 2019 | 663,006 | 64,860 | 2,183 | 730,049 |
| Additions | 21,669 | 1,259 | 16 | 22,944 |
| Decommissioning obligations | 8,835 | 1,232 | - | 10,067 |
| Right of use assets | - | 45 | 9 | 54 |
| Disposals and derecognition | - | - | (47) | (47) |
| **Balance at December 31, 2020** | **693,510** | **67,396** | **2,161** | **763,067** |
| Additions | 506 | 358 | - | 864 |
| Decommissioning obligations | (2,005) | (866) | - | (2,871) |
| **Balance as at March 31, 2021** | **692,011** | **66,888** | **2,161** | **761,060** |

| Accumulated depletion and depreciation | Crude oil and natural gas properties | Production equipment | Other assets | Total |
|---|---|---|---|---|
| Balance as at December 31, 2019 | (425,267) | (31,406) | (1,257) | (457,930) |
| Depletion and depreciation | (27,819) | (76) | (207) | (28,102) |
| Impairment loss | (45,446) | (4,261) | (150) | (49,857) |
| Disposals | - | - | 47 | 47 |
| **Balance as at December 31, 2020** | **(498,532)** | **(35,743)** | **(1,567)** | **(535,842)** |
| Depletion and depreciation | (5,372) | (176) | (50) | (5,598) |
| **Balance as at March 31, 2021** | **(503,904)** | **(35,919)** | **(1,617)** | **(541,440)** |
| | | | | |
| Net book value as at December 31, 2020 | 194,978 | 31,653 | 594 | 227,225 |
| **Net book value as at March 31, 2021** | **188,107** | **30,969** | **544** | **219,620** |

Distinction has included $385.6 million (March 31, 2020: $475.5 million) of future development costs and excluded $1.0 million (March 31, 2020: $1.0 million) for estimated salvage to its costs subject to depletion and depreciation.

For the three months ended March 31, 2021, Distinction capitalized $0.1 million (March 31, 2020: $0.3 million) of general and administrative expenses directly related to exploration and development activities.

**Impairment and Impairment Reversal**

The Company performed an assessment of possible indicators of impairment or impairment reversal on its cash-generating unit (CGU) as at March 31, 2021. Based on management’s assessment, there were no indicators of impairment or impairment reversal for the Company’s CGU and no impairment calculation was performed.

At March 31, 2020, the Company identified indicators of impairment on its Bigstone CGU due to the outbreak of the COVID-19 pandemic coupled with the Saudi Arabia - Russia oil price war resulting in both a decrease in oil demand and a significant drop in the forward commodity price curves.

The Company performed an impairment test on its Bigstone CGU, based on the recoverable amount estimated using a value in use calculation derived from expected future cash flows generated from proved and probable reserves using a blended pre-tax discount rate of approximately 15 percent which resulted in the recognition of a $114.8 million impairment. In addition, an impairment related to a change in estimates of decommissioning obligations for non-producing properties of $0.1 million was also recognized.

At December 31, 2020, the Company evaluated its CGU for indicators of impairment or reversal of previously recognized impairment and determined that as a result of the improvement in commodity prices, the Company’s improved liquidity, increase in reserves and decrease in future development costs, indicators of a reversal of impairment were identified. The Company performed an impairment test on its Bigstone CGU, based on the recoverable amount estimated using a value in use calculation derived from expected future cash flows generated from proved and probable reserves using a blended pre-tax discount rate of approximately 20 percent which resulted in the recognition of a $65.0 million recovery.

## 8) DECOMMISSIONING OBLIGATIONS

The Company's decommissioning obligations result from working interests in crude oil and natural gas assets including well sites, gathering systems and processing facilities. The total decommissioning obligation is estimated based on the Company's net ownership interest in all wells and facilities, estimated costs to reclaim and abandon the wells and facilities and the estimated timing of the costs to be incurred in future years. The Company estimates the undiscounted total future liability of $32.5 million (December 31, 2020 - $32.5 million) to be settled on an ongoing basis over a period of approximately 36 years. A risk-free rate of 1.97 percent (December 31, 2020 – 1.21 percent) and an inflation rate of 1.69 percent (December 31, 2020 – 1.49 percent) were used to calculate the estimated fair value of the decommissioning obligations.

| | **March 31, 2021** | December 31, 2020 |
|---|---|---|
| **Balance, beginning of period** | **34,799** | **25,254** |
| Liabilities incurred | **-** | **125** |
| Liabilities settled | **(17)** | **(886)** |
| Accretion expense | **155** | **364** |
| Change in estimates | **(2,871)** | **9,942** |
| **Balance, end of period** | **32,066** | **34,799** |
| | | |
| Current portion | **428** | **147** |
| Long term portion | **31,638** | **34,652** |

## 9) SENIOR CREDIT FACILITY

| | **March 31, 2021** | December 31, 2020 |
|---|---|---|
| Senior Credit Facility | | |
| Bankers' acceptances, net of discount | **-** | - |
| **Balance as at March 31, 2021** | **-** | - |

As at March 31, 2021, the Company had a $30.0 million senior secured revolving credit facility available from a financial institution. The Company did not have an outstanding balance on its senior credit facility during the three months ended March 31, 2021, with the exception of $6.0 million outstanding letters of credit. The senior secured facility was available on a revolving basis until May 31, 2021, with an option to extend, at the lender's discretion. If the revolving period was not extended, the undrawn portion of the facility would be cancelled and the amount outstanding would be required to be repaid at the end of the non-revolving term being May 29, 2022.

Subsequent to March 31, 2021 and concurrently with the closing of the Simonette Acquisition (see Note 15), the Company's credit facility was amended and restated (the "New Credit Facility"). The New Credit Facility has a borrowing base of $127.5 million and is provided by a syndicate of lenders. The New Credit Facility is a 364 day committed facility available on a revolving basis until May 31, 2022 at which time it may be extended at the lenders' option. If the revolving period is not extended, the undrawn portion of the New Credit Facility will be cancelled and the amount outstanding would be required to be repaid at the end of the non-revolving term being May 31, 2023. The non-extension provisions are applicable to the lenders on an individual basis. The borrowing base of the New Credit Facility will be based on the lenders' evaluation of the Company's petroleum and natural gas reserves at the time and commodity prices. A decrease in the borrowing base could result in a reduction to the New Credit Facility, which may require a repayment to the lenders.

Interest payable on amounts drawn under the New Credit Facility is at the prevailing bankers' acceptance or LIBOR rates plus stamping fees, lenders' prime rate or U.S. base rate plus the applicable margins, depending on the form of borrowing by the Company. The applicable margins and stamping fees are based on a sliding scale pricing grid tied to the Company's debt to earnings before interest, taxes, depreciation and amortization ratio: from a minimum of the bank's prime rate or U.S. base rate plus an applicable margin ranging from 1.75 percent to 5.25 percent or from a minimum of bankers' acceptances or LIBOR rate plus a stamping fee ranging from 2.75 percent to 6.25 percent.

The New Credit Facility is secured by a $300.0 million demand floating charge debenture and a general security agreement over all assets of the Company.

The Company was not subject to financial covenants under the credit facility existing as at March 31, 2021 and is not subject to financial covenants under the New Credit Facility.

## 10) SHARE CAPITAL

Distinction is authorized to issue an unlimited number of common shares. All shares are issued as fully paid and non-assessable and have no par value. The holders of common shares are entitled to receive dividends as declared by the Company and are also entitled to one vote per share.

In accordance with the Company's Plan, on October 16, 2020, all of the Company's outstanding common shares, options and warrants were cancelled and extinguished for nil consideration and 6.1 million Class A common shares were issued.

### Issued and outstanding

| | March 31, 2021 | | December 31, 2020 | |
|---|---|---|---|---|
| | **Outstanding shares (000's)** | **Amount** | Outstanding shares (000's) | Amount |
| **Balance, beginning of period** | **6,089** | **131,454** | 18,429 | 353,842 |
| Issued on exercise of warrants | **3,349** | **40,000** | 6,060 | 10,000 |
| Transferred from exercise of warrants | **-** | **4,594** | - | - |
| Share issue costs | | **(93)** | - | (159) |
| Cancelled in accordance with the Plan | **-** | **-** | (24,489) | (363,683) |
| Issued Class A common shares | **-** | **-** | 2,106 | 27,025 |
| Issued Class A common shares in exchange for compromise of debt | **-** | **-** | 3,983 | 105,518 |
| Class A common shares issue cost | **-** | **-** | - | (1,089) |
| **Balance, end of period** | **9,438** | **175,955** | 6,089 | 131,454 |

On October 16, 2020, in accordance with the Plan, the Company issued 4.0 million shares in exchange for the compromise of $155.7 million of secured indebtedness. In addition, the Company issued 0.6 million Class A common shares at a price of $15 per Class A common share to plan sponsors for gross proceeds of $8.8 million and 1.5 million Class A common shares together with 3.3 million warrants ("New Warrants") to Kiwetinohk for gross proceeds of $22.9 million.

On January 15, 2021, Kiwetinohk exercised their 3.3 million New Warrants to purchase 3.3 million Class A common shares of the Company at an aggregate exercise price of $11.94 per warrant. As a result of the exercise of the warrants, $4.6 million has been transferred to share capital.

In February 2020, the Company issued 6.1 million common shares at a price of $1.65 per common share through a private placement. The common shares were subsequently cancelled and extinguished for nil consideration on October 16, 2020, in accordance with the Plan.

### (a) Warrants

| | March 31, 2021 | | December 31, 2020 | |
|---|---|---|---|---|
| | **Outstanding warrants (000's)** | **Amount** | Outstanding warrants (000's) | Amount |
| **Balance, beginning of period** | **3,349** | **4,594** | 88,200 | 5,627 |
| Issued | **265** | **3,980** | - | - |
| Transaction costs | **-** | **(197)** | - | - |
| Exercise of warrants | **(3,349)** | **(4,594)** | - | - |
| Cancelled in accordance with the Plan | **-** | **-** | (88,200) | (5,627) |
| Issued in accordance with the Plan | **-** | **-** | 3,349 | 4,642 |
| Allocation of Plan transaction costs | **-** | **-** | - | (48) |
| **Balance, end of period** | **265** | **3,783** | 3,349 | 4,594 |

On October 16, 2020, in accordance with the Plan, all previously outstanding warrants were cancelled and extinguished for no consideration. Concurrently, the Company issued 1.5 million Class A common shares together with 3.3 million New Warrants to Kiwetinohk for gross proceeds of $22.9 million. The New Warrants entitled Kiwetinohk to purchase one Class A common share of the Company for an aggregate exercise price of $11.94 per New Warrant.

On January 15, 2021, Kiwetinohk exercised their 3.3 million New Warrants to purchase 3.3 million Class A common shares for gross proceeds of $40.0 million. As a result of the exercise of the warrants, $4.6 million has been transferred to share capital.

On February 24, 2021, the Company closed a private placement of 265,331 special warrants ("Special Warrants") issued at a price of $15 per Special Warrant for gross proceeds of $4.0 million. Each Special Warrant is, subject to adjustments in certain circumstances, exercisable into one Class A common share of the Company without payment of any additional consideration.

All unexercised Special Warrants shall be deemed exercised on behalf of, and without any required action on the part of the holders (including payment of additional consideration) on June 25, 2021.

**(b) Options**

The following table summarizes information about the stock options and restricted share units outstanding and exercisable at March 31, 2021:

| | Outstanding and Exercisable | | | |
|---|---|---|---|---|
| | Outstanding and exercisable options (000's) | Weighted average exercise price | Weighted average remaining term (years) | Early termination – from date of listing (1) |
| Options (2) | 304 | 15.00 | 9.5 | 100 days |
| Restricted share units | 304 | 0.01 | 4.8 | 2 years |
| **Total** | **608** | **7.51** | **7.15** | |

1. The Company's stock options and restricted share units outstanding, contain an early termination clause to expire 100 days and two years, respectively, from the date the Company is listed on an approved exchange.
2. Early termination period for the stock options was amended in January 2021 from 90 days to 100 days.

No stock options or restricted share units were granted, exercised or forfeited during the quarter.

**(c) Net loss per share**

Net loss per share has been calculated based on the following weighted average common shares:

| | Three Months Ended March 31 | |
|---|---|---|
| | **2021** | 2020 |
| Weighted average common shares – basic | **8,879** | 6,089 |
| Net loss per basic and diluted share | **(0.58)** | (18.06) |

In accordance with IAS 33, per share calculations are based on the new number of outstanding shares if the number of outstanding shares changes as a result of a recapitalization. Accordingly, the weighted average common shares used for the comparative periods presented have been adjusted to reflect the number of Class A common shares as a result of the restructuring under the Plan and exclude any potentially dilutive securities as all securities outstanding prior to the Plan were cancelled and extinguished for nil consideration.

As at March 31, 2021, the Company excluded 0.3 million stock options and 0.3 million restricted share units from the dilutive calculation as they were anti-dilutive.

**11) REVENUE**

Crude oil and natural gas sales are comprised of the following:

| | Three Months Ended March 31 | |
|---|---|---|
| | **2021** | 2020 |
| Natural gas | **8,653** | 5,091 |
| Field condensate | **9,980** | 7,780 |
| Natural gas liquids | **3,014** | 1,396 |
| Sulphur | **18** | (8) |
| Total crude oil and natural gas sales | **21,665** | 14,259 |

**12) RELATED PARTY TRANSACTIONS**

In October 2020, as part of the restructuring contemplated under the Plan, the Company issued Kiwetinohk 25 percent of the then issued and outstanding Class A common shares (on a non-diluted basis) plus 3.3 million New Warrants exercisable into Class A common shares of the Company. On January 15, 2021, Kiwetinohk exercised their 3.3 million New Warrants to purchase 3.3 million Class A common shares of the Company at an aggregate exercise price of $11.94 per warrant, increasing their ownership to 51.6 percent of the outstanding Class A common shares of the Company. The Chief Executive Officer of Kiwetinohk is also the Chief Executive Officer and board member of Distinction.

The Company and Kiwetinohk are parties to a Management Services Agreement (the “MSA”). The MSA, among other things, requires Kiwetinohk to provide management services to the Company in exchange for a monthly fee payable to Kiwetinohk. The MSA had a termination date of October 16, 2021. Concurrently, with the closing of the Simonette Acquisition (see Note 15), the MSA was amended and restated, among other things, to extend the termination date to February 17, 2026. In the three months ended March 31, 2021, the Company has recognized $0.6 million of monthly MSA fees payable to Kiwetinohk.

**13) RESTRUCTURING COSTS**

Restructuring costs are comprised of legal fees, monitor fees, financial advisory fees, investor relations, consultant fees and termination payments.

In the first three months of 2021, the Company incurred $0.9 million in restructuring costs primarily related to termination benefits associated with the implementation of the Company’s Plan.

**14) SUPPLEMENTAL CASH FLOW INFORMATION**

Changes in non-cash working capital are comprised of the following:

| | Three Months Ended March 31 | |
|---|---|---|
| | **2021** | 2020 |
| Source (use) of cash | | |
| Accounts receivable | **(1,592)** | 3,854 |
| Prepaid expenses | **(684)** | (1,016) |
| Accounts payable and accrued liabilities | **(323)** | 21,918 |
| Total change in non-cash working capital | **(2,599)** | 24,756 |
| | | |
| Relating to: | | |
| Operating activities | **(2,689)** | 3,585 |
| Investing activities | **90** | 21,171 |
| | **(2,599)** | 24,756 |

**15) SUBSEQUENT EVENT**

On February 17, 2021, the Company and Kiwetinohk entered into agreements to participate equally in a $320 million asset acquisition of oil and natural gas properties (the “Simonette Acquisition”) and paid a $7.5 million deposit. The Company’s share of the purchase price was $160 million (less a deposit of $7.5 million) and was subject to standard closing adjustments from the effective date of January 1, 2021, through to closing. The price excludes up to $15 million of contingent payments, of which the Company’s share is up to $7.5 million, that will be required if the average WTI price, expressed in USD per barrel (calendar month average) of the New York Mercantile Exchange (NYMEX) 1st nearby month Light, Sweet Crude Oil Futures Contract, exceeds USD $56.00 per barrel in 2021 and USD $62.00 per barrel in 2022. The transaction had an effective date of January 1, 2021 and closed on April 28, 2021. Alongside the closing of the Simonette Acquisition, the Company’s credit facility was amended and restated with a borrowing base of $127.5 million (Note 9).

Concurrently, with the closing of the Simonette Acquisition, the Company, Kiwetinohk and 1266580 B.C. Ltd., an affiliate of Luminus Energy, entered into a settlement agreement to terminate the rights and obligations under a participation agreement made effective by the parties October 16, 2020. The Company’s share of the settlement agreement is $5.75 million and was settled and paid to 1266580 B.C. Ltd. as part of the closing procedures of the Simonette Acquisition.

In connection with the Simonette Acquisition, the Company entered into the following risk management contracts:

**Crude Oil Contracts**

| Time Period | Type of Contract | Average Quantity Contracted | Swap Price ($/unit) | Bought Put Price ($/unit) | Sold Call Price ($/unit) | Reference |
|---|---|---|---|---|---|---|
| June 2021 to December 2021 | Price swap | 1,018 bbls/d | $77.00 Cdn | - | - | WTI |
| January 2022 to December 2022 | Collar | 999 bbls/d | - | $65.00 Cdn | $78.00 Cdn | WTI |

**Natural Gas Contracts**

| Time Period | Type of Contract | Quantity Contracted | Price ($/unit) | Reference |
|---|---|---|---|---|
| June to October 2021 | Price swap - buyer | 33,658 gj/d | $2.7691 Cdn | AECO |
| June to October 2021 | Price swap - seller | 31,902 mmbtu/d | $2.7809 USD | Chicago |

**U.S. Dollar Forward Exchange Contract**

| Time Period | Monthly Average Notional U.S. $ | Average Exchange Rate (U.S.$ to Cdn$) |
|---|---|---|
| June to October 2021 | $2,715,572 | 1.22709 |

On April 28, 2021 Distinction entered into three marketing agreements with Kiwetinohk for natural gas, condensate and NGLs production volumes associated with the Simonette Acquisition. Kiwetinohk will market all of Distinction's production from the Simonette Acquisition and will also purchase natural gas volumes above production required to fill Distinction's net 45 mmcf/d of contracted capacity on the Alliance Pipeline. Natural gas purchases required to fill the capacity above expected production have been fully contracted through October 31, 2021. The marketing profits based upon actual revenues and costs will be shared equally with Distinction and Kiwetinohk for their respective volumes.

**DIRECTORS**

Timothy Schneider (1)(5)

Kevin Brown (2)(3)(4)(5)
Co-Chair and Director of ARC Financial Corp.

Pat Carlson (3)
President and CEO of Distinction Energy Corp. and Kiwetinohk Resources Corp.

Glenn Koach (2)(4)
Co-Founder and Principal, Concise Capital

Steven Sinclair (2)(3)
Corporate Director

(1) Chair of the Board
(2) Member of the Audit Committee
(3) Member of the Reserves Committee
(4) Member of the Corporate, Governance & Compensation Committee
(5) Member of the Listing Committee

**AUDITORS**

KPMG LLP

**LEGAL COUNSEL**

Cassels Brock & Blackwell LLP
Osler, Hoskin & Harcourt LLP
Norton Rose Fulbright Canada LLP

**INDEPENDENT ENGINEERS**

GLJ Petroleum Consultants Ltd.

**TRANSFER AGENT**

Computershare Trust Company of Canada

**OFFICERS**

Pat Carlson
President and Chief Executive Officer

Jakub Brogowski
Chief Financial Officer

Glen Nevokshonoff
Chief Operating Officer

Tim Alberts
Vice President, Production

Mike Carlson
Vice President, Completions

Sue Kuethe
Vice President, Land

Mike Hantzsch
Vice President, Midstream and Marketing

Morteza Nobakht
Vice President Development

Farid Shirkavand
Vice President, Drilling

Lisa Wong
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**ABBREVIATIONS**

bbls ……………………………barrels
bbls/d ……………………………barrels per day
bcf ……………………………billion cubic feet
boe ……………………………barrels of oil equivalent (6 mcf:1 bbl)
boe/d ……………………………barrels of oil equivalent per day
gj……………………………gigajoules
mbbls ……………………………thousand barrels
mcf ……………………………thousand cubic feet
mcf/d ……………………………thousand cubic feet per day
mmboe ……………………………million barrels of oil equivalent
mmbtu/d……………………………million british thermal units
mmcf ……………………………million cubic feet
mmcf/d ……………………………million cubic feet per day
NGL ……………………………natural gas liquids