Sahara Energy Ltd.

Financial Statements

For the years ended December 31, 2018 and 2017

Independent Auditor's Report

To the Shareholders of Sahara Energy Ltd.:

Opinion

We have audited the financial statements of Sahara Energy Ltd. (the "Company"), which comprise the statements of financial position as at December 31, 2018 and December 31, 2017, and the statements of loss and comprehensive loss, changes in equity and cash flows for the years then ended, and notes to the financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2018 and December 31, 2017, and its financial performance and its cash flows for the years then ended in accordance with International Financial Reporting Standards.

Basis for Opinion

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

Other Information

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

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

In connection with our audits of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audits or otherwise appears to be materially misstated. We obtained Management's Discussion and Analysis prior to the date of this auditor's report. If, based on the work we have performed on this other information, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

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

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

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

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

Auditor's Responsibilities for the Audit of the Financial Statements

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

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

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

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

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

The engagement partner on the audit resulting in this independent auditor's report is James Fuerderer.

MNP LLP

Calgary, Alberta
April 26, 2019

Chartered Professional Accountants

MNP

Sahara Energy Ltd.
Statements of Financial Position
As at December 31
(in Canadian dollars)

		2018		2017
Assets				
Current assets				
Cash and cash equivalents (Note 5)	$	777,027	$	812,084
Term deposits (Note 5)		8,724,951		9,338,149
Trade and other receivables (Note 13(b))		10,497		84,660
Inventory		31,720		-
Prepaid expenses and deposits		699,167		677,338
		10,243,362		10,912,231
Property, plant and equipment (Note 6)		3,458,966		3,489,094
Total Assets	$	13,702,328	$	14,401,325
Liabilities and Shareholders' Equity				
Current liabilities				
Trade and other payables	$	455,192	$	468,647
Decommissioning obligation (Note 7)		449,890		466,040
Total Liabilities		905,082		934,687
Shareholders' Equity				
Share capital (Note 8)		20,465,084		20,465,084
Contributed surplus		1,244,119		1,244,119
Accumulated deficit		(8,911,957)		(8,242,565)
Total Shareholders' Equity		12,797,246		13,466,638
Total Liabilities and Shareholders' Equity	$	13,702,328	$	14,401,325

Commitment (Note 12)

Approved on behalf of the Board:

(Signed) "*Fan (Rose) Gong*", Director

(Signed) "*Gary Chang*", Director

See the accompanying notes to these financial statements.

Sahara Energy Ltd.
Statements of Loss and Comprehensive Loss
For the years ended December 31
(in Canadian dollars)

		2018		2017
Revenue				
Oil sales (Note 9)	$	162,970	$	51,062
Royalties		(4,637)		(1,467)
		158,333		49,595
Expenses				
Production and operating		176,304		128,294
General and administrative		653,620		618,501
Depletion and depreciation (Note 6)		54,314		34,075
Accretion (Note 7)		9,410		8,924
Bad debt expense (Note 13(b))		39,630		-
		933,278		789,794
Loss from operating activities		(774,945)		(740,199)
Interest income		105,553		112,186
Net loss and comprehensive loss	$	(669,392)	$	(628,013)
Net loss per share - basic	$	(0.00)	$	(0.00)
Basic weighted average number of common shares outstanding		289,684,072		289,684,072

See the accompanying notes to these financial statements.

Sahara Energy Ltd.
Statements of Changes in Equity
For the years ended December 31
(in Canadian dollars)

		2018		2017
Share capital				
289,684,072 common shares issued and outstanding				
Balance, beginning and end of year	$	20,465,084	$	20,465,084
Contributed surplus				
Balance, beginning and end of year		1,244,119		1,244,119
Accumulated deficit				
Balance, beginning of year		(8,242,565)		(7,614,552)
Net loss		(669,392)		(628,013)
Balance, end of year		(8,911,957)		(8,242,565)
Total Shareholders' Equity	$	12,797,246	$	13,466,638

See the accompanying notes to these financial statements.

Sahara Energy Ltd.
Statements of Cash Flows
For the years ended December 31
(in Canadian dollars)

	2018	2017
Operating activities		
Net loss	$ (669,392)	$ (628,013)
Add back (deduct) non-cash items:		
Depletion and depreciation (Note 6)	54,314	34,075
Decommissioning obligation accretion (Note 7)	9,410	8,924
Abandonment expenditures (Note 7)	(49,000)	(16,579)
Change in non-cash working capital		
Trade and other receivables	74,163	21,593
Inventory	(31,720)	-
Prepaid expenses and deposits	(21,829)	(1,699)
Trade and other payables	(13,455)	(6,541)
Cash flows used in operating activities	(647,509)	(588,240)
Investing activities		
Term deposit redemption (purchase)	613,198	(92,474)
Development and production asset expenditures (Note 6)	(746)	(970)
Cash flows provided by (used in) investing activities	612,452	(93,444)
Change in cash and cash equivalents	(35,057)	(681,684)
Cash and cash equivalents, beginning of year	812,084	1,493,768
Cash and cash equivalents, end of year	$ 777,027	$ 812,084

See the accompanying notes to these financial statements.

1. Nature of operations

Sahara Energy Ltd. (the "Company") was incorporated under the Business Corporations Act (Alberta) and is listed on the TSX Venture Exchange ("the Exchange"). The Company is a junior resource exploration company engaged in the acquisition, exploration and development of petroleum and natural gas reserves in Western Canada. The Company's registered address is 610, 700 – 4th Avenue SW, Calgary, Alberta.

As at December 31, 2018, JF Investment (Hong Kong) Co., Limited ("JF Investment") owned and controlled 69% of the Company's issued and outstanding shares.

2. Basis of preparation

(a) Statement of compliance

These financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB") and the interpretations of the International Financial Reporting Interpretations Committee in effect at January 1, 2018.

These financial statements were authorized for issue by the Board of Directors on April 26, 2019.

(b) Basis of measurement

The financial statements have been prepared on the historical cost basis except for certain financial assets and liabilities which are measured at fair value.

The methods used to measure fair values are discussed in Note 4.

(c) Functional and presentation currency

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

(d) Use of judgments and estimates

The preparation of financial statements in conformity with IFRS requires management to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amount of assets, liabilities, income and expenses. Actual results may differ materially from estimated amounts.

Estimates and their underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the year in which the estimates are revised and for any future years affected.

<u>Critical judgments in applying accounting policies</u>

The following are critical judgments that management has made in the process of applying accounting policies and that have the most significant effect on the amounts recognized in the financial statements.

Cash-generating units

The Company's assets are aggregated into a single cash-generating unit ("CGU") for the purpose of calculating impairment. CGUs are based on an assessment of a unit's ability to generate independent cash inflows. The determination of the Company's CGU was based on management's judgment in regards to shared infrastructure, geographical proximity, exposure to market risk and materiality.

Joint arrangements

Judgment is required to determine when the Company has joint control over an arrangement. In establishing joint control, the Company considers whether unanimous consent is required to direct the activities that significantly affect the returns of the arrangement, such as the capital and operating activities of the arrangement.

Once joint control has been established, judgment is also required to classify as a joint arrangement. The type of joint arrangement is determined through analysis of the rights and obligations arising from the arrangement by considering its structure, legal form, and terms agreed upon by the parties sharing control. An arrangement where the controlling parties have rights to the assets and revenues and obligations for the liabilities and expenses is classified as a joint operation.

Impairment indicators

Judgments are required to assess when impairment indicators exist and impairment testing is required. In determining the recoverable amount of assets, in the absence of quoted market prices, impairment tests are based on estimates of reserves, production rates, future oil and natural gas prices, future costs, discount rates, market value of land and other relevant assumptions.

Provisions

Judgments are required to assess the existence of obligations requiring a probable outflow of funds to settle the obligation and the requirement to recognize a related provision.

Deferred taxes

Judgments are made by management to determine the likelihood of whether deferred income tax assets at the end of the reporting period will be realized from future taxable earnings.

Contingencies

Judgments are made by management to determine the existence of contingencies and the outcome of future events.

<u>Key Sources of Estimation Uncertainty</u>

The following are key estimates and their assumptions made by management affecting the measurement of balances and transactions in these financial statements.

Recoverability of asset carrying values

The recoverability of development and production asset carrying values are assessed at the CGU level. Determination of what constitutes a CGU is subject to management judgments. The asset composition of a CGU can directly impact the recoverability of the assets included therein. The key estimates used in the determination of cash flows from oil and natural gas reserves include the following:

- Reserves – Assumptions that are valid at the time of reserve estimation may change significantly when new information becomes available. Changes in forward price estimates, production costs or recovery rates may change the economic status of reserves and may ultimately result in reserves being restated.
- Oil and natural gas prices – Forward price estimates are used in the cash flow model. Commodity prices can fluctuate for a variety of reasons including supply and demand fundamentals, inventory levels, exchange rates, weather, and economic and geopolitical factors.
- Discount rate – The discount rate used to calculate the net present value of cash flows is based on estimates of an approximate industry peer group weighted average cost of capital. Changes in the general economic environment could result in significant changes to this estimate.

Depletion and depreciation

Amounts recorded for depletion and depreciation and amounts used for impairment calculations are based on estimates of total proved and probable oil and natural gas reserves and future development capital. By their nature, the estimates of reserves, including the estimates of future prices, costs and future cash flows, are subject to measurement uncertainty. Accordingly, the impact to the financial statements in future periods could be material.

Decommissioning obligation

The amount recorded for the decommissioning obligation and the related accretion expense requires the use of estimates with respect to the amount and timing of decommissioning expenditures. Actual costs and cash outflows can differ from estimates because of changes in laws and regulations, public expectations, market conditions, discovery and analysis of site conditions and changes in technology. Other provisions are recognized in the period when it becomes probable that there will be a future cash outflow.

Deferred taxes

Tax interpretations, regulations and legislation in the various jurisdictions in which the Company operates are subject to change. As such income taxes are subject to measurement uncertainty. Deferred income tax assets are assessed by management at the end of the reporting period to determine the likelihood that they will be realized from future taxable earnings.

Contingencies

By their nature, contingencies will only be resolved when one or more future events occur or fail to occur. Management must make estimates of amounts related to the outcome of future events.

3. Significant accounting policies

The accounting policies set out below have been applied consistently to all periods presented in these financial statements.

(a) Financial instruments

As of January 1, 2018, the Company classifies its financial instruments in the following measurement categories:

- subsequently measured at fair value (either through profit or loss ("FVPTL") or other comprehensive income ("FVOCI"); and
- subsequently measured at amortized cost.

The classification depends on the Company's business model for managing the financial instruments and the contractual terms of the cash flows. There was no change in the categorization of the Company's financial instruments upon the adoption of IFRS 9 Financial Instruments ("IFRS 9").

Non-derivative financial instruments

Non-derivative financial instruments comprise cash and cash equivalents, term deposits, trade and other receivables and trade and other payables. Non-derivative financial instruments are recognized initially at fair value plus, for instruments not at FVTPL, any directly attributable transaction costs. Transaction costs of financial assets measured at FVPL are expensed in profit or loss. Subsequent to initial recognition, non-derivative financial instruments are measured as described below:

- Financial assets at FVTPL

  Financial assets at FVTPL are measured at fair value, and changes therein are recognized in profit or loss. A financial asset is classified at FVPL unless it is measured at amortized cost or classified as FVOCI. However an entity may make an irrevocable election at initial recognition for particular investments in equity instruments that would otherwise be measured at FVPL to present subsequent changes in FVOCI with no reclassification of realized gains or losses to profit or loss upon derecognition of the equity instruments.

- Financial liabilities at FVTPL

  A financial liability is initially classified as measured at amortized cost or FVTPL. A financial liability is classified as measured at FVTPL if it is held-for-trading, a derivative, or designated as FVTPL on initial recognition. The classification of a financial liability is irrevocable.

  Financial liabilities at FVTPL (other than financial liabilities designated at FVTPL) are measured at fair value with changes in fair value, along with any interest expense, recognized in net earnings. Other financial liabilities are initially measured at fair value less directly attributable transaction costs and are subsequently measured at amortized cost using the effective interest method. Interest expense and foreign exchange gains and losses are recognized in net earnings. Any gain or loss on derecognition is also recognized in net earnings.

  A financial liability is derecognized when the obligation is discharged, cancelled or expired. When an existing financial liability is replaced by another from the same counterparty with substantially different terms, or the terms of an existing liability are substantially modified, it is treated as a derecognition of the original liability and the recognition of a new liability. When the terms of an existing financial liability are altered, but the changes are considered non-substantial, it is accounted for as a modification to the existing financial liability. Where a liability is substantially modified it is considered to be extinguished and a gain or loss is recognized in net earnings based on the difference between the carrying amount of the liability derecognized and the fair value of the revised liability. Where a liability is modified in a non-substantial way, the amortized cost of the liability is remeasured based on the new cash flows and a gain or loss is recorded in net earnings.

- Financial assets at FVOCI

  Financial assets at FVOCI are measured at fair value, and changes therein are recognized in other comprehensive income. A financial asset is classified as FVOCI if it is held within a business model whose objective is achieved by both collecting contractual cash flows and selling financial assets and the contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

- Financial instruments at amortized cost

  The Company classifies cash and cash equivalents, term deposits, trade and other receivables and trade and other payables as financial instruments at amortized cost. These financial instruments are measured at amortized cost using the effective interest method, less any impairment losses. Any gain or loss arising on de-recognition is recognized directly in profit or loss. Impairment losses are presented as separate line item in the statement of profit or loss.

Derivative financial instruments

The Company has not entered into any financial derivative contracts.

(b) Impairment of financial instruments

As of January 1, 2018, the Company assesses, on a forward looking basis, the expected credit losses associated with financial instruments carried at amortized cost. The impairment methodology applied depends on whether there has been a significant increase in credit risk. For trade and other receivables, the Company applied the simplified approach permitted by IFRS 9.

The Company retrospectively adopted IFRS 9 on January 1, 2018, but has elected not to restate comparative information. As a result, the comparative information provided continues to be accounted for in accordance with the Company's previous accounting policy:

A financial asset is assessed at each reporting date to determine whether there is any objective evidence that it is impaired. A financial asset is considered to be impaired if objective evidence indicates that one or more events have had a negative effect on the estimated future cash flows of that asset. An impairment loss in respect of a financial asset measured at amortized cost is calculated as the difference between its carrying amount and the present value of the estimated future cash flows discounted at the original effective interest rate. Individually significant financial assets are tested for impairment on an individual basis. The remaining financial assets are assessed collectively in groups that share similar credit risk characteristics. All impairment losses are recognized in the statement of loss and comprehensive loss. An impairment loss is reversed if the reversal can be related objectively to an event occurring after the impairment loss was recognized. For financial assets measured at amortized cost, the reversal is recognized in the statement of loss and comprehensive loss.

(c) Share capital

Common shares are classified as equity. Incremental costs directly attributable to the issuance of common shares are recognized as a reduction of equity.

(d) Jointly controlled operations and jointly controlled assets

The Company's petroleum and natural gas exploration activities are conducted jointly with others. These financial statements reflect only the Company's proportionate interest in such activities. Joint control exists for contractual arrangements governing the Company's assets whereby the Company has less than 100 per cent working interest, all of the partners have control of the arrangement collectively, and spending on the project requires unanimous consent of all parties that collectively control the arrangement and share the associated risks. The Company does not have any joint arrangements structured through joint venture arrangements.

(e) Property, plant and equipment and exploration and evaluation assets

(i) Recognition and measurement

Exploration and evaluation expenditures

Pre-license costs are recognized in the statement of loss and comprehensive loss as incurred. Exploration and evaluation costs, including the costs of acquiring undeveloped land and drilling costs are initially capitalized until the drilling of the well is complete and the results have been evaluated. The costs are accumulated in cost centres pending determination of technical feasibility and commercial viability. The technical feasibility and commercial viability is considered to be determinable when proved and/or probable reserves are determined to exist. If proved and/or probable reserves are found, the drilling costs and associated undeveloped land are transferred to property, plant and equipment. Any impairment recognized during a period, is charged as additional depletion and depreciation expense.

Exploration and evaluation assets are assessed for impairment if (i) sufficient data exists to determine technical feasibility and commercial viability, and (ii) facts and circumstances suggest that the carrying amount exceeds the recoverable amount. For purposes of impairment testing, exploration and evaluation assets are allocated to CGUs.

Development and production costs

Property, plant and equipment, which includes oil and gas development and production assets, are initially measured at cost and subsequently carried at cost less accumulated depletion and depreciation and accumulated impairment losses.

The cost of development and production assets includes; transfers from exploration and evaluation assets, which generally include the cost to drill the well and the cost of the associated land upon determination of technical feasibility and commercial viability; the cost to complete and tie-in the wells; facility costs; the cost of recognizing provisions for future restoration and decommissioning; geological and geophysical costs; and directly attributable overheads.

Development and production assets are grouped into CGUs for impairment testing.

When significant parts of an item of property and equipment, including petroleum and natural gas properties, have different useful lives, they are accounted for as separate items (major components). Gains and losses on disposal of an item of property, plant and equipment, including oil and natural gas interests, are determined by comparing the proceeds from disposal with the carrying amount of property, plant and equipment and are recognized in the statement of loss and comprehensive loss.

(ii) Subsequent costs

Costs incurred subsequent to the determination of technical feasibility and commercial viability and the costs of replacing parts of property, plant and equipment are recognized as oil and natural gas interests only when they increase the future economic benefits embodied in the specific asset to which they relate. All other expenditures are recognized in the statement of loss and comprehensive loss as incurred. Such capitalized oil and natural gas interests generally represent costs incurred in developing proved and/or probable reserves and bringing in or enhancing production from such reserves, and are accumulated on a field or geotechnical area basis. The carrying amount of any replaced or sold component is derecognized. The costs of periodic servicing of property, plant and equipment are recognized in operating expenses as incurred.

(iii) Depletion and depreciation

The net carrying value of development and production assets is depleted using the unit of production method by reference to the ratio of production in the period to the related proved plus probable reserves, taking into account estimated future development costs necessary to bring those reserves into production and the estimated salvage value of the assets at the end of their useful lives. Future development costs are estimated taking into account the level of development required to produce the reserves.

Proved plus probable reserves are estimated annually by independent qualified reserve evaluators, in accordance with Canadian Securities Administration National Instrument 51-101, and represent the estimated quantities of crude oil, natural gas and natural gas liquids which geological, geophysical and engineering data demonstrate with a specified degree of certainty to be recoverable in future years from known reservoirs and which are considered commercially producible.

For depletion purposes, relative volumes of petroleum and natural gas production and reserves are converted at the energy equivalent conversion rate of six thousand cubic feet of natural gas to one barrel of crude oil.

Depreciation of furniture and equipment is based on estimated useful lives and is calculated using the declining balance method at rates ranging from 20% - 45%. Depreciation methods, useful lives and residual values are reviewed at each reporting date.

(f) Impairment of non-financial assets

The carrying amounts of the Company's non-financial assets, other than exploration and evaluation assets and deferred tax assets, are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists, then the asset's recoverable amount is estimated. Exploration and evaluation assets are assessed for impairment when they are transferred to property, plant and equipment, and also if facts and circumstances suggest that the carrying amount exceeds the recoverable amount.

The recoverable amount of an asset or a CGU is the greater of its value in use and its fair value less costs of disposal.

Fair value less costs of disposal is determined as the amount that would be obtained from the sale of a CGU in an arm's length transaction between knowledgeable and willing parties. The fair value less costs of disposal of oil and gas assets is generally determined as the net present value of the estimated future cash flows expected to arise from the continued use of the CGU, including any expansion prospects, and its eventual disposal, using assumptions that an independent market participant may take into account. These cash flows are discounted by an appropriate discount rate which would be applied by such a market participant to arrive at a net present value of the CGU.

Value in use is determined as the net present value of the estimated future cash flows expected to arise from the continued use of the asset in its present form and its eventual disposal. Value in use is determined by applying assumptions specific to the Company's continued use and can only take into account approved future development costs. Estimates of future cash flows used in the evaluation of impairment of assets are made using management's forecasts of commodity prices and expected production volumes. The latter takes into account assessments of field reservoir performance and includes expectations about proved and unproved volumes, which are risk-weighted utilizing geological, production, recovery and economic projections.

An impairment loss is recognized if the carrying amount of a CGU exceeds its estimated recoverable amount. Impairment losses are recognized in depletion and depreciation expense in the statement of loss and comprehensive loss. Impairment losses recognized in respect of CGU's are allocated first to reduce the carrying amount of any goodwill allocated to the CGU and then to reduce the carrying amounts of the other assets in the CGU on a pro rata basis.

Impairment losses recognized in prior years are assessed at each reporting date, if facts and circumstances indicate that the loss has decreased or no longer exists. An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount.

An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depletion and depreciation, if no impairment loss had been recognized.

(g) Decommissioning obligation

The Company's activities give rise to dismantling, decommissioning and site disturbance remediation activities. Provision is made for the estimated cost of site restoration and capitalized in the relevant asset category.

The Company's decommissioning obligation is measured at the present value of management's best estimate of expenditure required to settle the present obligation at the balance sheet date at a risk-free rate. Subsequent to the initial measurement, the obligation is adjusted at the end of each period to reflect the passage of time, revisions to the amount of the original estimate, changes in the discount rate or risk-free rate and changes in the estimated future cash flows underlying the obligation. The increase in the provision due to the passage of time is recognized as finance costs whereas increases/decreases due to changes in the estimated future cash flows and other assumptions are capitalized. Actual costs incurred upon settlement of the decommissioning obligation are charged against the provision to the extent the provision was established.

(h) Revenue recognition

The Company recognizes revenue from the sale of oil when control of the product transfers to the buyer and collection is reasonably assured. This is generally at the point in time when the customer obtains legal title to the product which is when it is physically transferred to the pipeline or other transportation method agreed upon. Sales of oil are based on variable pricing based on benchmark commodity prices and other variable factors including quality, location and other factors.

(i) Finance income and expenses

Finance expense comprises interest expense on borrowings, accretion of the discount on the decommissioning obligation and impairment losses recognized on financial assets. Interest income is recognized as it accrues in the statement of loss and comprehensive loss, using the effective interest method.

(j) Taxes

Tax expense comprises current and deferred tax. Tax expense is recognized in the statement of loss and comprehensive loss except to the extent that it relates to items recognized directly in equity, in which case it is recognized in equity.

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

Deferred tax is recognized using the liability method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is not recognized on the initial recognition of assets or liabilities in a transaction that is not a business combination. In addition, deferred tax is not recognized for taxable temporary differences arising on the initial recognition of goodwill. Deferred tax is measured at the tax rates that are expected to be applied to temporary differences when they reverse, based on the laws that have been enacted or substantively enacted by the reporting date. Deferred tax assets and liabilities are offset if there is a legally enforceable right to offset, and they relate to income taxes levied by the same tax authority on the same taxable entity, or on different tax entities, but they intend to settle current tax liabilities and assets on a net basis or their tax assets and liabilities will be realized simultaneously.

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

(in Canadian dollars)

(k) Per share amounts

Basic per share amounts are calculated by dividing the income attributable to common shareholders of the Company by the weighted average number of common shares outstanding during the period. Diluted per share amounts are determined by adjusting the income (loss) attributable to common shareholders and the weighted average number of common shares outstanding for the effects of dilutive instruments such as warrants and stock options granted. Anti-dilutive instruments are not included in the determination of diluted per share amounts.

(l) Changes in accounting standards

Adoption of IFRS 9 Financial Instruments

On January 1, 2018, the Company retrospectively adopted IFRS 9 which replaces IAS 39 Financial Instruments: Recognition and Measurement ("IAS 29") and includes new requirements for the classification and measurement of financial assets, a new credit loss impairment model and new model to be used for hedge accounting for risk management contracts. The Company does not currently have any risk management contracts. The adoption of IFRS 9 did not have a material impact on the Company's financial statements and management applied the provision matrix practical expedient as part of the adoption of the standard.

The additional disclosures required by IFRS 9 are detailed in Note 13(b).

IFRS 9 contains three principal classification categories for financial assets: measured at amortized cost, FVOCI, and FVTPL. The previous IAS 39 categories of held to maturity, loans and receivables and available for sale are eliminated. IFRS 9 bases the classification of financial assets on the contractual cash flow characteristics and the Company's business model for managing the financial asset. Additionally, embedded derivatives are not separated if the host contract is a financial asset within the scope of IFRS 9. Instead, the entire hybrid contract is assessed for classification and measurement. IFRS 9 largely retains the existing requirements in IAS 39 for the classification of financial liabilities. The differences between the two standards did not impact the Company at the time of transition.

The following table shows the original measurement categories under IAS 39 and the new measurement categories under IFRS 9 for each class of the Company's financial assets and financial liabilities as at January 1, 2018.

	Measurement Category (1) (2)	
Financial instrument	IAS 39	IFRS 9
Cash and cash equivalents	Loans and receivables	Amortized cost
Term deposits	Loans and receivables	Amortized cost
Trade and other receivables	Loans and receivables	Amortized cost
Trade and other payables	Amortized cost	Amortized cost

(1) There were no adjustments to the carrying amounts of financial instruments as a result of the classification change from IAS 39 to IFRS 9.
(2) The Company has no contract assets or debt investments measured at FVOCI.

Adoption of IFRS 15 Revenue from Contracts with Customers

On January 1, 2018, the Company adopted IFRS 15 Revenue from Contracts with Customers ("IFRS 15") using the modified retrospective method of adoption. The adoption of IFRS 15 did not have a material impact on the Company's financial statements and as a result, the Company did not apply any practical expedients as part of the adoption of IFRS 15. The additional disclosures required by IFRS 15 are detailed in Note 9.

For the comparative year, prior to the adoption of IFRS 15, the Company's revenue accounting policy was:

Revenue from the sale of crude oil and natural gas is recorded when the significant risks and rewards of ownership of the product is transferred to the buyer which is usually when legal title passes to the external party. This is generally at the time volumes are delivered to customers at contractual delivery points and rates.

(m) New and amended standards not yet adopted

The Company has reviewed new and amended accounting pronouncements that have been issued but are not yet effective and determined that the following may have an impact on the Company:

IFRS 16 Leases

In January 2016, the IASB issued IFRS 16 Leases ("IFRS 16") which replaces the previous leases standard, IAS 17 Leases. IFRS 16 eliminates the classification of leases as either operating leases or finance leases as is required by IAS 17 and, instead, introduces a single lessee accounting model.

IFRS 16 will result in almost all leases being recognized in the statement of financial position, as the distinction between operating and finance leases is removed. Under IFRS 16, an asset (the right-to-use the leased item) and a financial liability are recognized. On initial adoption, the Company anticipates that it will elect to use the following practical expedients permitted under the standard:

- Apply a single discount rate to a portfolio of leases with similar characteristics;
- Account for leases with a remaining term of less than 12 months as at January 1, 2019 as short-term leases;
- Account for lease payments as an expense and not recognize a right-of-use asset if the underlying asset is of low dollar value; and
- The use of hindsight in determining the lease term where the contract contains terms to extend or terminate the lease.

IFRS 16 is effective for periods beginning on or after January 1, 2019. The Company is currently evaluating the impact of IFRS 16 and the extent of the impact on its financial statements has not been determined.

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. Fair values have been determined for measurement and/or disclosure purposes based on the following methods. When applicable, further information about the assumptions made in determining fair values is disclosed in the notes specific to that asset or liability.

(a) Property, plant and equipment and exploration and evaluation assets

The market value of property, plant and equipment and exploration and evaluation assets is the estimated amount for which the assets could be exchanged on the acquisition date between a willing buyer and a willing seller in an arm's length transaction after proper marketing wherein the parties had each acted knowledgeably, prudently and without compulsion. The market value of oil and natural gas interests (included in property, plant and equipment) and intangible exploration assets is estimated with reference to the discounted cash flows expected to be derived from oil and natural gas production based on externally prepared reserve reports. The risk-adjusted discount rate is specific to the asset with reference to general market conditions.

The market value of other items of property, plant and equipment is based on the quoted market prices for similar items.

(in Canadian dollars)

(b) Cash and cash equivalents, term deposits, trade and other receivables, deposits and trade and other payables

The fair value of cash and cash equivalents, term deposits, trade and other receivables, deposits and trade and other payables is estimated as the present value of future cash flows, discounted at the market rate of interest at the reporting date. At December 31, 2018 and 2017, the fair value of these balances approximated their carrying value due to their short term to maturity.

(c) Fair value measurement information

The Company classifies the fair value of certain financial instruments according to the following hierarchy based on the amount of observable inputs used to value the instrument.

- 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. Cash and cash equivalents and term deposits are a Level 1 fair value measurement.
- Level 2 – Pricing inputs are other than quoted prices in active markets included in Level 1. Prices are either directly or indirectly observable as of the reporting date. 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.

5. Cash and cash equivalents and term deposits

	2018	2017
Cash and cash equivalents		
Cash in bank	$ 777,027	$ 378,556
Term deposits with maturities of three months or less	–	433,528
	$ 777,027	$ 812,084
Term deposits		
Term deposits with maturities over three months	$ 8,724,951	$ 9,338,149

(in Canadian dollars)

6. Property, plant and equipment

	Furniture and equipment	Development and production assets	Total
Cost			
As at December 31, 2016	$ 217,798	$ 4,711,497	$ 4,929,295
Additions	–	970	970
Decommissioning revisions	–	(16,929)	(16,929)
As at December 31, 2017	217,798	4,695,538	4,913,336
Additions	–	746	746
Decommissioning revisions	–	23,440	23,440
As at December 31, 2018	$ 217,798	$ 4,719,724	$ 4,937,522
Accumulated depletion and depreciation			
As at December 31, 2016	$ 138,201	$ 1,251,966	$ 1,390,167
Depletion and depreciation	22,501	11,574	34,075
As at December 31, 2017	160,702	1,263,540	1,424,242
Depletion and depreciation	15,881	38,433	54,314
As at December 31, 2018	$ 176,583	$ 1,301,973	$ 1,478,556
Net carrying amount			
As at December 31, 2017	$ 57,096	$ 3,431,998	$ 3,489,094
As at December 31, 2018	$ 41,215	$ 3,417,751	$ 3,458,966

Depletion and depreciation:

The calculation of 2018 depletion and depreciation expense included an estimated $4.4 million (2017 – $4.5 million) for future development costs associated with proved plus probable reserves. The Company has not capitalized any directly attributable general and administrative expenses to development and production assets.

Impairment:

At December 31, 2018 and 2017, the Company identified certain business risks related to its CGU such as a decline in forward commodity prices. As a result, the Company tested its petroleum and natural gas CGU for impairment at December 31, 2018 and 2017 based on the net present value of cash flows from oil and natural gas reserves as estimated by the Company's independent reserves evaluator at a discount rate of 15%. As at December 31, 2018 and 2017, the estimate of the 'fair value less costs of disposal' of the Company's petroleum and natural gas assets was sufficiently in excess of the carrying value of the CGU and therefore the Company did not recognize any impairment.

A 1% increase in the assumed discount rate would not result in impairment in 2018 or 2017; a 5% decrease in the forward commodity price estimates would not result in any impairment in 2018 (2017 – $195,000 of impairment).

(in Canadian dollars)

The December 31, 2018 and 2017 impairment test used the following commodity price estimates:

	December 31, 2018		December 31, 2017	
	AB Synthetic Crude (Light) Cdn$/bbl	Western Canada Select (Heavy) Cdn$/bbl	AB Synthetic Crude (Light) Cdn$/bbl	Western Canada Select (Heavy) Cdn$/bbl
2018	n/a	n/a	71.41	52.84
2019	75.35	50.48	76.79	56.82
2020	74.47	55.86	80.10	59.28
2021	77.56	58.17	83.12	61.51
2022	80.76	60.57	84.14	62.27
2023	81.44	61.08	87.08	64.44
2024	82.14	61.61	90.03	66.62
2025	83.96	62.97	92.97	68.80
2026	85.83	64.37	95.91	70.97
Escalation rate thereafter	+ 2% per year	+ 2% per year	+ 2% per year	+ 2% per year

7. Decommissioning obligation

As at December 31, 2018, the Company has estimated the total undiscounted inflation-adjusted amount of cash flows required to settle its decommissioning liabilities to be $569,855 (2017 – $626,623). This amount will be substantially incurred over the next 11 years (2017 – 13 years). The Company calculated the decommissioning liabilities using an average risk-free discount rate of 2.07% (2017 – 2.10%) per annum and an inflation rate of 2% (2017 – 2%) per annum.

	2018	2017
Balance, beginning of year	$ 466,040	$ 490,624
Accretion	9,410	8,924
Revisions	23,440	(16,929)
Expenditures	(49,000)	(16,579)
Balance, end of year	$ 449,890	$ 466,040

8. Share capital

a) Authorized

Unlimited number of common voting shares with no par value
Unlimited number of preferred non-voting shares with no par value

b) Issued and outstanding common shares

	Number of shares	Amount
Balance, December 31, 2016, 2017 and 2018	289,684,072	$ 20,465,084

9. Oil sales

The Company sells its production pursuant to fixed and variable price contracts with varying length terms up to 1 year. Under the contracts, the Company is required to deliver a fixed or variable volume of light-medium oil to the contract counterparty. The transaction price is based on the commodity price, adjusted for quality, location or other factors.

All of the Company's oil sales revenue is from the sale of heavy and light-medium oil from non-operated properties. Oil sales were earned from two working interest partners (the property operators) during the

(in Canadian dollars)

2018 (2017 – a single working interest partner and property operator) representing 100% of revenue for the years ended December 31, 2018 and 2017 and $nil of accounts receivable at December 31, 2018 (December 31, 2017 – $1,520).

Composition of oil sales revenue:

	2018	2017
Light-medium oil	$ 47,668	$ 51,062
Heavy oil	115,302	–
	$ 162,970	$ 51,062

10. Taxes

The provision for deferred taxes differs from the amount computed by applying the combined federal and provincial tax rates to the loss before taxes. The difference results from the following:

	2018	2017
Loss before income taxes	$ (669,392)	$ (628,013)
Combined federal and provincial statutory income tax rate	27.10%	27.10%
Expected income tax reduction	$ (181,405)	$ (170,191)
Effect of unrecognized deferred tax assets	181,405	170,191
	$ –	$ –

The following table summarizes the components of deferred tax:

	2018	2017
Deferred tax assets		
Non-capital loss carryforwards	$ 277,216	$ 228,382
Deferred tax liabilities		
Property, plant and equipment	(277,216)	(228,382)
	$ –	$ –

Deferred tax assets result from temporary differences that arise due to the differences between the income tax values and the carrying amount of assets and liabilities. Deferred tax assets have not been recognized for the following deductible temporary differences as it is not probable that future taxable profit will be available against which the Company can utilize the benefits:

	2018	2017
Non-capital loss carryforwards	$ 12,960,209	$ 12,427,555
Share issue costs	–	21,072
Reorganization costs	82,900	89,140
Decommissioning obligation	449,890	466,040
Other	175,631	175,631
	$ 13,668,630	$ 13,179,438

As at December 31, 2018, the Company has approximately $2.7 million (2017 – $2.9 million) of tax pools available for deduction against future taxable income. The Company also has non-capital tax losses of approximately $15 million (2017 – $14.3 million) available for deduction against future taxable income that begin to expire in 2028.

11. Supplemental disclosures

a) Employee compensation cost

The statement of loss and comprehensive loss is prepared primarily by nature of expense. During 2018, the Company incurred $164,995 (2017 – $212,017) of employee compensation cost which is included in general and administrative expenses.

b) Key management compensation

The Company considers its directors and executives to be key management personnel. As at December 31, 2018, key management personnel included 10 individuals (2017 – 10 individuals).

Key management personnel compensation is comprised of the following:

		2018		2017
Salaries and wages	$	105,796	$	105,434
Short-term employee benefits		10,054		11,266
	$	115,850	$	116,700

12. Commitment

The Company is committed to lease rental payments and a proportionate share of operating costs pursuant to the terms of an office lease agreement in the amount of $15,762 per month from January 1, 2019 to August 31, 2019.

13. Financial instruments

The Company holds various financial instruments as at December 31, 2018. The nature of these instruments and its operations expose the Company to market risk, credit risk and liquidity risks. The Company manages its exposure to these risks by operating in a manner that minimizes this exposure. While management monitors and administers these risks, the Board of Directors has the overall responsibility for the establishment and oversight of the Company's risk management framework.

(a) Market risk

Market risks are generally those risks that are outside of the control of the Company. These are: commodity prices, foreign exchange rates and interest rates. The objective of the Company is to mitigate exposure to these risks, while maximizing returns to the Company.

(i) Commodity price risk
Due to the volatility of commodity prices, the Company is exposed to adverse consequences in the event of declining prices. The Company did not enter into any oil price contracts to protect its cash flow on future sales in 2018 or 2017. A 5% change in the average commodity price earned by the Company would change oil sales revenue and net loss and comprehensive loss by approximately $8,150 (2017 – $2,550).

(ii) Foreign currency exchange risk
Although all of the Company's oil sales are denominated in Canadian dollars, the underlying market

(in Canadian dollars)

prices for oil are impacted by the exchange rate between Canada and the United States. As at December 31, 2018 and 2017, the Company had no forward foreign exchange contracts in place.

(iii) Interest rate risk

The Company does not have any debt subject to floating rates and is therefore not exposed to fluctuations in the market rate of interest.

(b) Credit risk

Substantially all of the Company's trade and other receivables are with customers and joint venture partners in the petroleum and gas industry and are subject to normal industry credit risks. The Company generally extends unsecured credit to these customers and, therefore, the collection of accounts receivable may be affected by changes in economic or other conditions. Management believes the risk is mitigated by entering into transactions with long-standing, reputable counterparties and partners. Wherever possible, the Company requires cash calls from its partners on capital projects before they commence. Receivables related to the sale of the Company's petroleum and natural gas production are from major marketing companies who have excellent credit ratings. These revenues are normally collected on the 25th day of the month following delivery.

The maximum exposure to credit risk at is as follows:

		2018		2017
Cash and cash equivalents	$	777,027	$	812,084
Term deposits		8,724,951		9,338,149
Trade and other receivables		10,497		84,660
	$	9,512,475	$	10,234,893

Composition of trade and other receivables:

		2018		2017
Production revenue receivable	$	–	$	1,520
Joint venture partner and cash call receivables		–		73,237
Goods and Services Tax and other receivables		10,497		9,903
	$	10,497	$	84,660

During 2018, the Company recognized $39,630 of bad debt expense for the write-off of uncollectible trade and other receivables. As at December 31, 2018, all of the Company's trade and other receivables are all less than 60 days old (December 31, 2017 – all less than 60 days old except for $73,985 which are greater than 60 days old).

(c) Liquidity risk

Liquidity risk would occur if the Company is not able to meet its financial obligations as they come due. Historically, the Company has suffered substantial operating losses. As at December 31, 2018, the Company has a working capital surplus of $9,788,170 (2017 – $10,443,584). The Company's goal continues to be prudent capital spending while improving its credit reputation amongst its suppliers.

The Company has sufficient cash resources to ensure its financial obligations, comprised of trade and other payables of $455,192, are met on a current basis.

14. Capital disclosures

The Company considers its capital structure to include working capital and shareholders' equity. The Company will adjust its capital structure to manage its current and projected debt through the issuance of shares and/or adjusting its capital spending. The Company monitors its capital based on the current and projected ratios of net debt to cash flow. The Company's objectives in managing its capital structure are to create and maintain flexibility so that the Company can continue to meet its financial obligations; and finance its growth either through internally generated projects, joint venture relationships or asset/corporate acquisitions.

	2018	2017
Working capital	$ 9,788,170	$ 10,443,584
Shareholders' equity	$ 12,797,246	$ 13,466,638

The Company does not have any externally imposed capital requirements as at December 31, 2018.