



**Consolidated Financial Statements**

**Years Ended**

**December 31, 2019 and 2018**

(Expressed in Canadian Dollars)

## INDEPENDENT AUDITOR'S REPORT

**To the Shareholders of Hillcrest Petroleum Ltd.**

**Report on the Audit of the Consolidated Financial Statements**

### **Opinion**

We have audited the consolidated financial statements of Hillcrest Petroleum Ltd., which comprise the consolidated statement of financial position as at December 31, 2019 and the consolidated statements of loss and comprehensive loss, changes in shareholders' deficiency and cash flows for the year then ended, and notes to the consolidated financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the financial position of Hillcrest Petroleum Ltd. as at December 31, 2019 and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards ("IFRS").

### **Basis for Opinion**

We conducted our audit 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 Consolidated Financial Statements section of our report. We are independent of Hillcrest Petroleum Ltd. in accordance with the ethical requirements that are relevant to our audit of the financial statements in Canada, and we have fulfilled our 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.

### **Material Uncertainty Related to Going Concern**

We draw attention to Note 1 in the consolidated financial statements, which indicates that Hillcrest Petroleum Ltd. incurred a net loss of \$1,201,929 during the year ended December 31, 2019 and has accumulated losses of \$13,073,487 since inception. As stated in Note 1, these events or conditions, along with other matters as set forth in Note 1, indicate that a material uncertainty exists that may cast significant doubt on Hillcrest Petroleum Ltd.'s ability to continue as a going concern. Our opinion is not modified in respect of this matter.

### **Other Information**

Management is responsible for the other information. The other information comprises the information included in "Management's Discussion and Analysis" but does not include the consolidated financial statements and our auditor's report thereon.

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

In connection with our audit of the consolidated financial statements, our responsibility is to read the other information, and in doing so, consider whether the other information is materially inconsistent with the consolidated financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated. If, based on the work we have performed, 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 Consolidated Financial Statements**

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

In preparing the consolidated financial statements, management is responsible for assessing Hillcrest Petroleum Ltd.'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 Hillcrest Petroleum Ltd. or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing Hillcrest Petroleum Ltd.'s financial reporting process.

## **Auditor's Responsibilities for the Audit of the Consolidated Financial Statements**

Our objectives are to obtain reasonable assurance about whether the consolidated 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 consolidated 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 consolidated 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 Hillcrest Petroleum Ltd.'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 Hillcrest Petroleum Ltd.'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 consolidated 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 Hillcrest Petroleum Ltd. to cease to continue as a going concern.
- Evaluate the overall presentation, structure, and content of the consolidated financial statements, including the disclosures, and whether the consolidated 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 audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

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.

### **Other Matter**

The financial statements of Hillcrest Petroleum Ltd. for the year ended December 31, 2018 were audited by another auditor which expressed an unmodified opinion on those financial statements in its report to the shareholders dated April 30, 2019.

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



### **Chartered Professional Accountants**

Vancouver, BC, Canada  
June 15, 2020

**HILLCREST PETROLEUM LTD.****Consolidated Statements of Financial Position**

(Expressed in Canadian dollars)

	December 31, 2019	December 31, 2018
	(\$)	(\$)
<b>ASSETS</b>		
Current assets		
Cash	41,749	21,348
Receivables	87,919	38,505
Prepaid expenses	37,627	90,689
Right-of-use asset (Notes 3(n) and 19)	12,532	-
Total current assets	179,827	150,542
Non-current assets		
Exploration and evaluation assets (Note 4)	-	964,881
Property and equipment (Note 5)	684,071	-
<b>TOTAL ASSETS</b>	<b>863,898</b>	<b>1,115,423</b>
<b>LIABILITIES</b>		
Current liabilities		
Accounts payable and accrued liabilities (Note 6)	1,411,071	1,452,044
Loans (Notes 7, 8 and 10)	1,234,542	1,012,241
Embedded derivative liabilities (Notes 7 and 9)	91,439	52,500
Lease liability (Notes 3(n) and 19)	11,265	-
Current portion of convertible debentures (Note 9)	76,657	-
Current portion of decommissioning liability (Note 11)	-	34,564
Total current liabilities	2,824,974	2,551,349
Convertible debentures (Note 9)	39,763	690,646
Other liability (Note 9)	116,000	116,000
Decommissioning liability (Note 11)	373,187	429,920
<b>TOTAL LIABILITIES</b>	<b>3,353,924</b>	<b>3,787,915</b>
<b>SHAREHOLDERS' DEFICIENCY</b>		
Share capital (Note 12)	8,980,016	7,681,347
Contributed surplus (Note 12)	1,357,361	1,350,917
Reserves (Note 12)	246,084	167,473
Deficit	(13,073,487)	(11,872,229)
	(2,490,026)	(2,672,492)
<b>TOTAL LIABILITIES &amp; SHAREHOLDERS' DEFICIENCY</b>	<b>863,898</b>	<b>1,115,423</b>

Nature of operations and going concern (Note 1)

Commitments (Note 13)

Subsequent events (Note 20)

On behalf of the Board of Directors:

"Michael Krzus"

Director

"Thomas Milne"

Director

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

**HILLCREST PETROLEUM LTD.****Consolidated Statements of Loss and Comprehensive Loss**

(Expressed in Canadian dollars)

	Year Ended December 31, 2019	Year Ended December 31, 2018
	(\$)	(\$)
<b>Revenue and costs</b>		
Oil sales	1,042,327	52,263
Royalties	(279,327)	(4,484)
Operating costs	(673,914)	(261,667)
Depletion and depreciation (Note 5)	(169,403)	-
	(80,317)	(213,888)
<b>General and administrative expenses</b>		
Management and consulting fees (Note 10)	534,223	390,085
Office and general	522,653	624,117
Share-based payments (Note 12)	6,444	46,556
	1,063,320	1,060,758
<b>Loss from operations</b>	(1,143,637)	(1,274,646)
Change in fair value of loan and convertible debenture conversion liabilities (Notes 7 and 9)	(11,280)	21,200
Financing expenses (Notes 7, 8 and 19)	(332,990)	(404,117)
Impairment of oil and gas properties (Note 5)	-	(202,525)
Foreign exchange gain	3,916	(6,447)
Gain on disposal of equipment	46,212	-
<b>Loss for the year before other item</b>	(1,437,779)	(1,866,535)
<b>Other item</b>		
Forgiveness of debt (Note 10(d))	235,850	-
<b>Net loss</b>	(1,201,929)	(1,866,535)
<b>Item that may be subsequently reclassified to net loss</b>		
Exchange differences on translating foreign operations	(3,389)	(3,158)
<b>Comprehensive loss for the year</b>	(1,205,318)	(1,869,693)
<b>Basic and diluted loss per share</b>	(0.01)	(0.02)
<b>Weighted average common shares outstanding:</b>		
Basic	91,461,993	85,000,297
Diluted	91,461,993	85,000,297

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

**HILLCREST PETROLEUM LTD.**

**Consolidated Statements of Changes in Shareholders' Deficiency**

(Expressed in Canadian dollars)

	Share Capital		Reserves				Shareholders' Deficiency
	Number of Shares	Amount	Contributed Surplus	Warrants	Foreign Currency Translation	Deficit	
		(\$)	(\$)	(\$)	(\$)	(\$)	(\$)
<b>Balance at December 31, 2017</b>	74,876,226	7,029,436	1,345,420	47,550	123,081	(10,005,694)	(1,460,207)
Proceeds from private placement	9,992,000	499,600	-	-	-	-	499,600
Share issuance costs	-	(17,248)	-	-	-	-	(17,248)
Exercise of stock options	725,000	84,559	(41,059)	-	-	-	43,500
Shares issued to settle debts	1,700,000	85,000	-	-	-	-	85,000
Vesting of stock options	-	-	46,556	-	-	-	46,556
Comprehensive loss for the period	-	-	-	-	(3,158)	(1,866,535)	(1,869,693)
<b>Balance at December 31, 2018</b>	87,293,226	7,681,347	1,350,917	47,550	119,923	(11,872,229)	(2,672,492)
Impact on adopting IFRS 16 (Notes 3(n) and 19)	-	-	-	-	-	671	671
<b>Restated opening balances under IFRS 16</b>	87,293,226	7,681,347	1,350,917	47,550	119,923	(11,871,558)	(2,671,821)
Proceeds from private placements	24,844,446	823,333	-	-	-	-	823,333
Value of warrants issued pursuant to private placements		(78,000)	-	78,000	-	-	-
Conversion of convertible debentures	11,541,627	577,081	-	-	-	-	577,081
Share issuance costs	-	(23,745)	-	4,000	-	-	(19,745)
Vesting of stock options	-	-	6,444	-	-	-	6,444
Comprehensive loss for the period	-	-	-	-	(3,389)	(1,201,929)	(1,205,318)
<b>Balance at December 31, 2019</b>	123,679,299	8,980,016	1,357,361	129,550	116,534	(13,073,487)	(2,490,026)

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

**HILLCREST PETROLEUM LTD.****Consolidated Statements of Cash Flows**

(Expressed in Canadian dollars)

	<b>Year Ended December 31, 2019</b>	<b>Year Ended December 31, 2018</b>
	<b>(\$)</b>	<b>(\$)</b>
Net loss for the period	(1,201,929)	(1,866,535)
Adjusted for items not involving cash:		
Accretion expense	60,580	59,725
Accrued interest expense	263,934	131,687
Financing cost of retained profit interest	-	116,000
Change in fair value of loan conversion liability	11,280	(21,200)
Depletion and depreciation	169,403	-
Impairment of oil and gas properties	-	202,525
Bad debt expense	(143,203)	-
Share-based payments	6,444	46,556
Gain on disposal of equipment	(46,212)	-
Unrealized foreign exchange loss	(3,389)	(3,189)
Changes in non-cash working capital:		
Prepaid expenses	78,062	111,533
Receivables	68,789	(22,831)
Accounts payable and accrued liabilities	254,137	679,559
<b>Cash flows used in operating activities</b>	<b>(482,104)</b>	<b>(566,170)</b>
Proceeds from disposal of oil and gas property interest	170,000	-
Property and equipment expenditures	(101,132)	(483,635)
<b>Cash flows provided by (used in) investing activities</b>	<b>68,868</b>	<b>(483,635)</b>
Proceeds from private placements	823,333	445,600
Proceeds from loans	60,000	282,000
Proceeds from convertible debentures	55,000	625,000
Proceeds from exercise of stock options	-	43,500
Share issuance costs	(2,146)	(17,249)
Repayment of lease liability	(23,732)	-
Repayment of loan principal and interest	(327,711)	(366,915)
Repayment of convertible debenture principal and interest	(151,107)	-
<b>Cash flows provided by financing activities</b>	<b>433,637</b>	<b>1,011,936</b>
<b>Change in cash</b>	<b>20,401</b>	<b>(37,869)</b>
<b>Effect of exchange rate changes on cash denominated in a foreign currency</b>	<b>-</b>	<b>31</b>
<b>Cash, beginning of the period</b>	<b>21,348</b>	<b>59,186</b>
<b>Cash, end of the period</b>	<b>41,749</b>	<b>21,348</b>

Supplemental cash flow information (Note 17)

## Hillcrest Petroleum Ltd.

Notes to the Consolidated Financial Statements

Years Ended December 31, 2019 and 2018

(Expressed in Canadian dollars)

---

### 1. NATURE OF OPERATIONS AND GOING CONCERN

Hillcrest Petroleum Ltd. (the "Company") was incorporated on May 2, 2006 under the Business Corporations Act of British Columbia, and is in the business of acquiring, exploring and developing exploration interests in oil and gas projects located in North America. The Company's registered office is Suite 1300 - 1030 West Georgia Street, Vancouver, BC, V6E 2Y3. The Company's shares are listed for trading on the TSX Venture Exchange ("TSXV") under the symbol "HRH" and on the OTC pink sheets under the symbol "HLRTF".

The Company is subject to several categories of risk associated with the exploration and development of oil and gas resources. Oil and gas exploration and production is a speculative business, and involves a high degree of risk. Among the factors that have a direct bearing on the Company's prospects are uncertainties inherent in estimating oil and gas reserves, future hydrocarbon production, and cash flows, particularly with respect to wells that have not been fully tested and with wells having limited production histories; access to additional capital; changes in the price of oil and gas; availability and cost of services and equipment; and the presence of competitors with greater financial resources and capacity.

These consolidated financial statements have been prepared on the basis of a going concern, which contemplates the realization of assets and the discharge of liabilities in the normal course of business for the foreseeable future. The Company recorded a net loss of \$1,201,929 (2018: \$1,866,535), an accumulated deficit of \$13,073,487 (2018 - \$11,872,229) and had a working capital deficiency of \$2,645,147 (2018 - \$2,400,807) as at and for the year ended December 31, 2019. The Company is currently in default on the Bridge Loan (December 31, 2019 - \$403,433), 1055328 BC Ltd. Loan (December 31, 2019 - \$123,871), ASI Loan (December 31, 2019 - \$138,550), Credit Line (December 31, 2019 - \$95,859) and the Ballakilley Loan (December 31, 2019 - \$206,771), but continues to accrue interest in accordance with the terms of the agreements (Note 7). The Company's ability to meet its obligations as they fall due and to continue to operate as a going concern is dependent on the continued financial support of its creditors and its shareholders and ultimately, the attainment of profitable operations. There is no certainty that the Company will continue to produce revenue due to the inherent production risks associated with the oil and natural gas industry. In the past, the Company has relied on sales of equity securities, debt instruments and asset sales to meet its cash requirements. There can be no assurance that funding from this or other sources will be sufficient in the future to satisfy operational requirements and cash commitments. Even if the Company is able to obtain new financing, it may not be on commercially reasonable terms or terms that are acceptable to it. Failure to obtain such financing on a timely basis could cause the Company to reduce or terminate its operations.

Due to the conditions and events as noted above, there is material uncertainty casting significant doubt on the Company's ability to continue as a going concern. These consolidated financial statements do not include any adjustments to the recoverability and classification of recorded asset amounts and classification of liabilities that might be necessary should the Company be unable to continue as a going concern. These adjustments could be material.

### 2. BASIS OF PREPARATION

#### (a) Statement of Compliance

The Company prepares its consolidated financial statements in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board.

These consolidated financial statements were approved by the Audit Committee and the Board of Directors of the Company on June 15, 2020.

#### (b) Statement of Compliance

The consolidated financial statements have been prepared on a historical cost basis, with the exception of the embedded derivatives in the Ballakilley loan and the convertible debentures which are recognised at fair value (Notes 7 and 9), using the accrual basis of accounting, except for cash flow information.



## Hillcrest Petroleum Ltd.

Notes to the Consolidated Financial Statements

Years Ended December 31, 2019 and 2018

(Expressed in Canadian dollars)

---

### 2. BASIS OF PREPARATION (continued)

#### (c) Basis of Consolidation

These consolidated financial statements include the accounts of the parent company, Hillcrest Petroleum Ltd., and its wholly-owned subsidiaries. Intercompany balances and transactions, and any unrealized income and expenses arising from intercompany transactions, are eliminated in preparing the consolidated financial statements.

<u>Name of Subsidiary</u>	<u>Jurisdiction of Incorporation</u>	<u>Principal Activity</u>
Hillcrest Exploration Ltd. ("HEL")	USA	Oil and Gas exploration
1084580 BC Ltd.	Canada	Oil and Gas exploration
2044573 Alberta Ltd.	Canada	Oil and Gas exploration
102031850 Saskatchewan Ltd.	Canada	Oil and Gas exploration
Hillcrest Resources (Arizona) Ltd. ("HARL")	USA	Dormant

#### (d) Functional and Presentation Currency

These consolidated financial statements are presented in Canadian dollars. The functional currency of the parent, 1084580 BC Ltd., 2044573 Alberta Ltd., 102031850 Saskatchewan Ltd. and HARL is the Canadian dollar. The functional currency of HEL is the United States dollar.

#### (e) Use of Estimates and Judgments

The preparation of these consolidated financial statements requires management to make certain estimates, judgments and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and reported amounts of expenses during the period. Actual results could differ from these estimates.

These consolidated financial statements include estimates which, by their nature, are uncertain. The impacts of such estimates are pervasive throughout the consolidated financial statements, and may require accounting adjustments based on future occurrences. Revisions to accounting estimates are recognized in the period in which the estimate is revised and future periods if the revision affects both current and future periods. These estimates are based on historical experience, current and future economic conditions and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

Significant assumptions about the future and other sources of estimation uncertainty that management has made at the reporting date that could result in a material adjustment to the carrying amounts of assets and liabilities, in the event that actual results differ from assumptions made, relate to, but are not limited to, the following:

##### Depletion and Depreciation

The amounts recorded for depletion and depreciation of oil and natural gas properties and the amounts used in impairment testing are based on independent estimates of proved and probable reserves, well production rates, realized and forecast oil and natural gas prices, future development costs and other relevant assumptions. By their nature, these estimates are subject to measurement uncertainty. Accordingly, the impact on the consolidated financial statements for future periods may be material.

## Hillcrest Petroleum Ltd.

Notes to the Consolidated Financial Statements

Years Ended December 31, 2019 and 2018

(Expressed in Canadian dollars)

---

### 2. BASIS OF PREPARATION (continued)

#### (e) Use of Estimates and Judgments (continued)

##### Decommissioning provisions

Restoration costs will be incurred by the Company at the end of the operating life of the Company's oil properties. The Company estimates abandonment and reclamation costs based on a combination of publicly available industry benchmarks and internal site-specific information. For producing wells and facilities, the expected timing of settlement is estimated based on the period to abandonment for each field, as per an independent report. The ultimate restoration liability is uncertain and can vary in response to many factors including changes to relevant legal requirements, the emergence of new restoration techniques, experience at other production sites, or changes in the risk-free discount rate. The expected timing and amount of expenditure can also change in response to changes in reserves or changes in laws and regulations or their interpretation. As a result, there could be significant adjustments to the provisions established which would affect future financial results.

##### Income taxes

The calculation of income taxes requires judgment in applying tax laws and regulations, estimating the timing of the reversals of temporary differences, and estimating the reliability of deferred tax assets. These estimates impact current and deferred income tax assets and liabilities, and current and deferred income tax expense (recovery).

Significant judgments that management has made at the end of the reporting period are as follows:

##### Carrying value and the recoverability of exploration and evaluation assets

Management has determined that exploration, evaluation and related costs incurred which were capitalized may have future economic benefits and may be economically recoverable. Management uses several criteria in its assessments of economic recoverability and probability of future economic benefits including geologic and other technical information, history of conversion of mineral deposits with similar characteristics to its own properties to proven and probable mineral reserves, scoping and feasibility studies, accessible facilities and existing permits.

##### Fair value of stock options and other share-based payments

Management assesses the fair value of stock options and other share-based payments granted in accordance with the accounting policy stated in Note 3 to the consolidated financial statements. The fair value of the options granted is measured using the Black-Scholes model, taking into account the terms and conditions upon which the options are granted. Changes in assumptions concerning volatilities, interest rates and expected life could have significant impact on the fair valuation attributed to the Company's stock options.

##### Going concern

In order to assess whether it is appropriate for the Company to be reported as a going concern, the Directors apply judgment, having undertaken appropriate inquiries and having considered the business activities and the Company's principal risks. Management estimates future cash flows, including the timing of future capital expenditures and equity funding.

##### Fair value of embedded derivatives and other liability

Management assesses its financial instruments in order to identify whether or not non-derivative instruments might contain an embedded derivative component. If such a derivative component is identified, then it must be separated from the non-derivative host contract and recorded at fair value. The fair value of the embedded derivative is measured using the Black-Scholes model, taking into account the terms and conditions upon which the derivative is granted. Changes in assumptions concerning volatilities, interest rates and expected life could have significant impact on the fair valuation attributed to the embedded derivative. Fair value of the other liability is measured using a market-based approach.

## Hillcrest Petroleum Ltd.

Notes to the Consolidated Financial Statements  
Years Ended December 31, 2019 and 2018  
(Expressed in Canadian dollars)

---

### 2. BASIS OF PREPARATION (continued)

#### (e) Use of Estimates and Judgments (continued)

##### Carrying value and the recoverability of property and equipment

The Company reviews its equipment for indicators of impairment whenever there is a change in events or circumstances that indicate an asset may be impaired and at each reporting period. Reviews are undertaken to evaluate the carrying value of the property and equipment considering, among other factors: the carrying value of each type of asset and the changes in circumstances that affect the carrying value of the Company's property and equipment. If such indication exists, a formal estimate of recoverable amount is performed and an impairment loss is recognized to the extent 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 ("VIU") and its fair value less costs to dispose ("FVLCD"). The FVLCD is the amount obtainable from the sale of an asset or CGU in an arm's length transaction between knowledgeable, and willing parties, less the costs of disposal or in the case of lack of comparable transactions, based upon discounted cash after tax cash flow. VIU is determined by estimating the pre-tax present value of the future net cash flows expected to be derived from the continued use of the asset of CGU.

##### Determination of cash generating units

Management must make judgments as to which oil and gas properties can be aggregated into a cash generating unit ("CGU"). The Company's oil and gas assets are aggregated into CGUs for the purpose of calculating impairment and depletion. Factors considered by management include, but are not limited to, the product produced (i.e. oil versus gas), the common infrastructure shared by individual properties, proximity of properties to each other, and planned development activities.

##### Right-of-Use Asset/Lease Liability

The incremental rate of borrowing used in the measurement of the lease liability was based on the interest rate of the Credit Line. See Notes 3 (n) and 19.

### 3. SIGNIFICANT ACCOUNTING POLICIES

#### (a) Foreign Currency Translation

##### Functional and presentation currency

The financial results of foreign operations that have a functional currency different from the Company's presentation currency are translated into the presentation currency. Income and expenditure transactions of foreign operations are translated at the average rate of exchange for the quarter except for significant individual transactions which are translated at the rate of exchange in effect at the transaction date. All assets and liabilities are translated at the rate of exchange ruling at the reporting date. Differences arising on translation are recognized as other comprehensive income.

When the settlement of a monetary receivable from or payable to a foreign operation is neither planned nor likely in the foreseeable future, foreign exchange gains and losses arising from such a monetary item are considered to form part of the net investment in a foreign operation and are recognized in other comprehensive income. On disposal of part or all of the operations, the proportionate share of the related cumulative gains and losses previously recognized in the comprehensive income are included in determining the profit or loss on disposal of that operation. The consolidated financial statements are presented in Canadian dollars, which is the Company's functional and presentation currency, while the United States dollar is the functional currency of several of the Company's subsidiaries.

##### Transactions and balances

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions, and from the translation of monetary assets and liabilities denominated in foreign currencies, are recognised in net income (loss), except for the Company's net investment in its foreign subsidiaries which are recognised in other comprehensive income.

## Hillcrest Petroleum Ltd.

Notes to the Consolidated Financial Statements

Years Ended December 31, 2019 and 2018

(Expressed in Canadian dollars)

---

### 3. SIGNIFICANT ACCOUNTING POLICIES (continued)

#### (a) Exploration and Evaluation

Exploration and evaluation (“E&E”) costs are capitalized for projects after the Company has acquired the legal right to explore but prior to their technical feasibility and commercial viability being confirmed, generally determined as the establishment of proved or probable reserves. These costs may include costs of license acquisition, technical services and studies, seismic acquisition, exploration drilling and testing, directly attributable overhead and administration expenses, including remuneration of production personnel and supervisory management, the projected costs of retiring the assets, and any activities in relation to evaluating the technical feasibility and commercial viability of extracting mineral resources.

Once technical feasibility and commercial viability are confirmed the E&E asset is then reclassified to property and equipment and tested for impairment. For purposes of impairment testing, E&E assets are allocated to the appropriate cash-generating units based on geographic proximity. Expired lease costs are expensed as part of depletion and depreciation expense as they occur and costs incurred prior to the legal right to explore are charged to net income (loss).

#### (b) Property and Equipment

##### Cost and valuation

All costs directly associated with the development of oil and gas interests are capitalized on a CGU basis as oil and gas interests and are measured at cost less accumulated depletion and net of impairment losses. These costs include expenditures for areas where technical feasibility and commercial viability have been determined. These costs include property acquisitions with proved and/or probable reserves, development drilling, completion, gathering and infrastructure, decommissioning liabilities and transfers of exploration and evaluation assets.

Equipment includes computer equipment which is recorded at cost on initial acquisition. Cost includes the purchase price and the directly attributable costs of acquisition required to bring an asset to the location and condition necessary for the asset to be capable of operating in the manner intended by management. Subsequent expenditure relating to an item of equipment is capitalized when it is probable that future economic benefits from the use of the assets will be increased. All other subsequent expenditure is recognized as repairs and maintenance expenses during the period in which they are incurred.

##### Depletion and depreciation

The provision for depletion for oil and natural gas assets is calculated based on each asset’s production for the period divided by the Company’s estimated total proved and probable oil and natural gas reserve volumes before royalties for that asset, taking into account estimated future development costs. Production and reserves of natural gas and associated liquids are converted at the energy equivalent ratio of six thousand cubic feet of natural gas to one barrel of oil. Changes in estimates used in prior periods, such as proven and probable reserves, that affect the unit-of-production calculations do not give rise to prior period adjustments and are dealt with on a prospective basis.

Equipment is depreciated on a declining balance basis over the estimated useful life of the asset at the rate of 33% to 55% per annum. Where components of an asset have a different useful life and cost that is significant to the total cost of the asset, depreciation is calculated on each separate component. Depreciation methods, useful lives and residual values are reviewed at the end of each reporting date, and adjusted on a prospective basis if appropriate.

## Hillcrest Petroleum Ltd.

Notes to the Consolidated Financial Statements

Years Ended December 31, 2019 and 2018

(Expressed in Canadian dollars)

---

### 3. SIGNIFICANT ACCOUNTING POLICIES (continued)

#### (c) Decommissioning and Restoration Costs

The Company recognizes liabilities for statutory, contractual, constructive or legal obligations associated with the retirement of long-term assets, when those obligations result from the acquisition, construction, development or normal operation of the assets. The net present value of future restoration cost estimates arising from the decommissioning of well sites is capitalized to oil and gas properties along with a corresponding increase in the restoration provision in the period incurred. The Company uses a risk-free discount rate that reflects the time value of money to calculate the net present value of the decommissioning provisions. The restoration asset will be depreciated on the same basis as other oil and gas properties.

The Company's estimates of restoration costs could change as a result of changes in regulatory requirements, discount rates and assumptions regarding the amount and timing of the future expenditures. These changes are recorded directly to oil and gas properties with a corresponding entry to the restoration provision, except when the related oil and gas property is closed. Changes in estimates of restoration costs for closed oil and gas properties are recorded in the income statement. The Company's estimates are reviewed annually for changes in regulatory requirements, discount rates, effects of inflation and changes in estimates.

The restoration provisions are accreted to full value over time through charges to finance expenses on the consolidated statement of loss and comprehensive loss.

The net present value of restoration costs arising from subsequent site damage that is incurred on an ongoing basis during production are charged to profit or loss in the period incurred. The costs of restoration projects that were included in the provision are recorded against the provision as incurred.

#### (d) Impairment of Non-Financial Assets

At each reporting period the carrying amounts of the Company's non-financial assets, are reviewed for indicators of impairment. If indicators exist, the recoverable amount of the asset is estimated. Exploration and evaluation assets are assessed for impairment when they are reclassified to property and equipment and if facts and circumstances suggest that the carrying amount exceeds the recoverable amount.

For purposes of assessing impairment, exploration and evaluation assets and property and equipment are grouped into CGUs defined as the smallest identifiable group of assets that generate cash inflows that are largely independent of the cash inflows of other assets or groups of assets. The Company has used geographical proximity, geological similarities, analysis of shared infrastructure, commodity type, assessment of exposure to market risks and materiality to define its CGUs.

If the carrying amount exceeds the recoverable amount, the asset or CGU is recorded at its recoverable amount with the reduction recognized in net income (loss) as an impairment expense. The recoverable amount is the greater of the value in use or fair value less costs of disposal ("FVLCD"). Fair value is the amount the asset could be sold for in an arm's length transaction. The value in use is the present value of the estimated future cash flows of the asset from its continued use. The fair value less costs of disposal considers the continued development of a property and market transactions in a valuation model. The Company uses the present value of the cash generating unit's estimated future cash flows from both proved and probable reserves in its fair value model. These calculations are corroborated by valuation multiples, quoted share prices for publicly traded entities or other available fair value indicators.

Impairments are reversed in subsequent periods when there has been an increase in the recoverable amount of a previously impaired asset or CGU and these reversals are recognized in net income (loss). The recovery is limited to the original carrying amount less depletion and depreciation that would have been recorded had the asset not been impaired.

## Hillcrest Petroleum Ltd.

Notes to the Consolidated Financial Statements

Years Ended December 31, 2019 and 2018

(Expressed in Canadian dollars)

### 3. SIGNIFICANT ACCOUNTING POLICIES (continued)

#### (e) Impairment of Financial Assets

At each reporting date, the Company assesses whether there is any objective evidence that a financial asset or a group of financial assets is impaired. A financial asset or group of financial assets is deemed to be impaired if, and only if, there is objective evidence of impairment as a result of one or more events that has occurred after initial recognition of the asset and that event has an impact on the estimated future cash flows of the financial asset or group of financial assets.

#### (f) Financial Instruments

Effective January 1, 2018, Hillcrest retrospectively adopted IFRS 9. The standard supersedes earlier versions of IFRS 9 and completes the IASB's project to replace IAS 39 Financial Instruments: Recognition and Measurement ("IAS 39"). There were no adjustments to the amounts recognized in Hillcrest's consolidated financial statements for the year ended December 31, 2019 and December 31, 2018. The adoption of IFRS 9 has resulted in changes to the classification of some of the Company's financial assets but did not change the classification of the Company's financial liabilities. There is no difference in the measurement of these instruments under IFRS 9.

Financial assets and financial liabilities are recognized when the Company becomes a party to the contractual provisions of the financial instrument.

Financial assets and financial liabilities are initially measured at fair value. Transaction costs that are directly attributable to the acquisition or issue of financial assets and financial liabilities (other than financial assets and financial liabilities classified at fair value through profit or loss) are added to, or deducted from, the fair value of the financial assets or financial liabilities, as appropriate, on initial recognition. Transaction costs directly attributable to the acquisition of financial assets or financial liabilities classified at fair value through profit or loss are recognized immediately in profit or loss.

The following table summarizes the classification categories for Hillcrest's financial assets and liabilities.

<b>Financial Assets</b>	<b>IAS 39</b>	<b>IFRS 9</b>
Cash	Held-for-trading (FVTPL)	Amortized costs
Accounts receivable	Loans and receivables (Amortized cost)	Amortized costs
<b>Financial Liabilities</b>	<b>IAS 39</b>	<b>IFRS 9</b>
Accounts payable and accrued liabilities	Other financial liabilities (Amortized cost)	Amortized costs
Embedded derivative liability	Held-for-trading (FVTPL)	FVTPL
Lease liability	N/A	Amortized costs
Loans and convertible debentures	Other financial liabilities (Amortized cost)	Amortized costs

#### (g) Provisions

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

#### (h) Basic and Diluted Earnings (Loss) Per Share

Earnings (loss) per share are calculated using the weighted-average number of common shares outstanding during the year. In calculating diluted earnings (loss) per share, the Company considers the potential exercise of outstanding share purchase options and warrants to the extent each option, warrant or contingent issuance was dilutive. Potentially dilutive securities were excluded in the computation of diluted loss per share as their inclusion would be anti-dilutive.

## Hillcrest Petroleum Ltd.

Notes to the Consolidated Financial Statements

Years Ended December 31, 2019 and 2018

(Expressed in Canadian dollars)

---

### 3. SIGNIFICANT ACCOUNTING POLICIES (continued)

#### (i) Convertible Debentures

The convertible debenture is a compound financial instrument as it contains a host debt component and an equity conversion feature. Accordingly, each part of the instrument is examined separately. The host debt component is classified as a financial liability in its entirety since a contractual obligation exists to deliver cash that the Company cannot avoid if the conversion right is not exercised. Furthermore, on a stand-alone basis there is no feature in the host debt component that is similar to equity.

The conversion feature is then assessed on a stand-alone basis. There is no contractual obligation to pay cash that the issuer cannot avoid on the conversion feature. The equity conversion feature can only be settled through the issue of common shares. However, the feature does not qualify as equity as it does not satisfy the "fixed for fixed" requirement. Consequently, the conversion feature is classified as a derivative liability.

Therefore, the embedded derivative liability and other liability is determined first and the residual value is assigned to the host debt component. The embedded derivative is fair valued with the initial carrying amount of the host contract being the residual. Any transaction costs are split on a pro-rata basis between the derivative and the debt. The embedded derivative liability and other liability is treated as FVTPL and is re-measured at each reporting period with any changes in fair value going through the income statement. The debt component is accounted for at amortized cost.

#### (j) Revenue Recognition

Effective January 1, 2018, the Company adopted IFRS 15, Revenue from Contracts with Customers ("IFRS 15"). The Company adopted IFRS 15 using the modified retrospective approach. The Company elected to use the following practical expedient: IFRS 15 was only applied retrospectively to contracts which were not completed as at January 1, 2018. The Company generates revenue solely from the sale of crude oil in Canada therefore has not added enhanced disclosure upon adoption of the new standard.

Hillcrest principally generates revenue from the sale of crude oil. Revenue associated with the sale of oil is recognized when control is transferred from Hillcrest to its customers. Hillcrest's oil sale contracts represent a series of distinct transactions. Hillcrest considers its performance obligations to be satisfied and control to be transferred when all of the following conditions are satisfied:

- Hillcrest has transferred title and physical possession of the commodity to the buyer;
- Hillcrest has transferred the significant risks and rewards of ownership of the commodity to the buyer; and
- Hillcrest has the present right to payment.

Revenue represents Hillcrest's share of oil sales net of royalty obligations to governments and other mineral interest owners. Hillcrest sells its production pursuant to variable priced contracts. The transaction price for variable priced contracts is based on the commodity price, adjusted for quality, location or other factors, whereby each component of the pricing formula can be either fixed or variable, depending on the contract terms. Revenue is recognized when a unit of production is delivered to the contract counterparty. The amount of revenue recognized is based on the agreed upon transaction price, whereby any variability in revenue is related specifically to the Company's efforts to deliver production. Therefore, the resulting revenue is allocated to the production delivered in the period during which the variability occurs. As a result, none of Hillcrest's variable revenue is considered to be constrained.

Payment terms for Hillcrest's oil sales contracts are on the 25th of the month following delivery. Hillcrest does not have any contracts where the period between the transfer of the promised goods or services to the customer and payment by the customer exceeds one year and therefore Hillcrest does not adjust its revenue transactions for the time value of money.

## Hillcrest Petroleum Ltd.

Notes to the Consolidated Financial Statements

Years Ended December 31, 2019 and 2018

(Expressed in Canadian dollars)

---

### 3. SIGNIFICANT ACCOUNTING POLICIES (continued)

#### (k) Share-based Payments

The grant date fair value of share-based payment awards granted to employees is recognized as an employee expense, with a corresponding increase in equity, over the period that the employees unconditionally become entitled to the awards. The amount recognized as an expense is adjusted to reflect the number of awards for which the related service and non-market vesting conditions are expected to be met, such that the amount ultimately recognized as an expense is based on the number of awards that do meet the related service and non-market performance conditions at the vesting date. For share-based payment awards with non-vesting conditions, the grant date fair value of the share-based payment is measured to reflect such conditions and there is no true-up for differences between expected and actual outcomes.

Where equity instruments are granted to parties other than employees, they are recorded by reference to the fair value of the services received. If the fair value of the services received cannot be reliably estimated, the Company measures the services received by reference to the fair value of the equity instruments granted, measured at the date the counterparty renders the services.

All equity-settled share-based payments are reflected in contributed surplus, until exercised. Upon exercise, shares are issued from treasury and the amount reflected in contributed surplus is credited to share capital, adjusted for any consideration paid.

#### (l) Joint Venture Activities and Joint Controlled Operations

Joint control is defined as the contractually agreed sharing of control over an economic activity, and exists only when the strategic, financial and operating decisions essential to the relevant activities require the unanimous consent of the parties sharing control. When the Company enters into agreements that provide for specific percentage interests in exploration properties, a portion of the Company's exploration activities is conducted jointly with others, without establishment of a corporation, partnership or other entity.

Under IFRS 11 "Joint Arrangements", this type of joint control of exploration assets and joint exploration and/or development activities is considered as a joint operation, which is defined as a joint arrangement whereby the parties that have joint control of the arrangement have rights to the assets, and obligations for the liabilities, relating to the arrangement. In these financial statements, the Company recognizes the following in relation to its interests in joint operations:

- its assets, including its share of any assets held jointly;
- its liabilities, including its share of any liabilities incurred jointly;
- its revenue from the sale of its share of the output of the joint operation; and
- its expenses, including its share of any expenses incurred jointly.

#### (m) Taxes

Income tax expense comprises current and deferred tax. Current tax and deferred tax are recognized in profit or loss except to the extent that it relates to a business combination, or items recognized directly in equity or in other comprehensive income.

##### Current income tax

Current tax is the expected tax payable or receivable on the taxable income or loss 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 income tax

Deferred tax is recognized in respect of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes.



## Hillcrest Petroleum Ltd.

Notes to the Consolidated Financial Statements

Years Ended December 31, 2019 and 2018

(Expressed in Canadian dollars)

---

### 3. SIGNIFICANT ACCOUNTING POLICIES (continued)

#### (m) Taxes (continued)

Deferred tax is not recognized for the following temporary differences:

- liabilities arising from initial recognition of goodwill for which amortization is not deductible for tax purposes;
- liabilities arising from the initial recognition of an asset/liability other than in a business combination which, at the time of the transaction, does not affect either the accounting or the taxable profit; and
- liabilities arising from undistributed profits from investments where the entity is able to control the timing of the reversal of the difference and it is probable that the reversal will not occur in the foreseeable future.

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

#### Sales tax

Revenues, expenses and assets are recognized net of the amount of sales tax except:

- Where the sales tax incurred on a purchase of assets or services is not recoverable from the taxation authority, in which case, the sales tax is recognized as part of the cost of acquisition of the asset or as part of the expense item as applicable; and
- Receivables and payables that are stated with the amount of sales tax included. The net amount of sales tax recoverable from, or payable to, the taxation authority is included as part of receivables or payables in the statement of financial position.

#### (n) Adoption of IFRS 16 Leases

The Company has adopted the requirements of IFRS 16 Leases ("IFRS 16") as of January 1, 2019. IFRS 16 introduces a single lessee accounting model and requires a lessee to recognize right-of-use assets and liabilities for leases. The Company elected to apply IFRS 16 using a modified retrospective approach; therefore, the comparative information has not been restated and continues to be reported under IAS 17, Leases. The details of the new accounting policy and the impact of the policy change are described below.

At inception of a contract, the Company must assess whether a contract is, or contains, a lease. A contract is, or contains, a lease if the contract conveys the right to control the use of an identified asset over a period of time in exchange for consideration. The Company must assess whether the contract involves the use of an identified asset, whether it has the right to obtain substantially all of the economic benefits from the use of the asset during the term of the contract and if it has the right to direct the use of the asset.

As a lessee, the Company recognizes a right-of-use asset and a lease liability at the commencement date of the lease.

## Hillcrest Petroleum Ltd.

Notes to the Consolidated Financial Statements  
Years Ended December 31, 2019 and 2018  
(Expressed in Canadian dollars)

### 3. SIGNIFICANT ACCOUNTING POLICIES (continued)

#### (n) Adoption of IFRS 16 Leases (continued)

##### *Right-of-use asset*

The right-of-use asset is initially measured at cost, which is comprised of the initial amount of the lease liability adjusted for any lease payments made and any initial direct costs incurred at or before the commencement date, plus any decommissioning and restoration costs, less any lease incentives received.

The right-of-use asset is subsequently amortized from the commencement date to the earlier of the end of the lease term, or the end of the useful life of the asset. In addition, the right-of-use asset may be reduced due to impairment losses, if any, and adjusted for certain re-measurements of the lease liability.

##### *Lease liability*

A lease liability is initially measured at the present value of the lease payments that are not paid at the commencement date discounted by the interest rate implicit in the lease or, if that rate cannot be readily determined, the incremental borrowing rate. The lease liability is subsequently measured at amortized cost using the effective interest method.

Lease payments included in the measurement of the lease liability comprise: fixed payments; variable lease payments that depend on an index or a rate; amounts expected to be payable under any residual value guarantee; the exercise price under any purchase option that the Company would be reasonably certain to exercise; lease payments in any optional renewal period if the Company is reasonably certain to exercise an extension option; and penalties for any early termination of a lease unless the Company is reasonably certain not to terminate early. The Company has elected to exclude non-lease components related to premises leases in the determination of the lease liability.

The Company has elected not to recognize right-of-use assets and lease liabilities for short-term leases that have a lease term of twelve months or less and leases of low-value assets. The lease payments associated with these leases are charged directly to income on a straight-line basis over the lease term.

The reconciliation of the lease liability as at January 1, 2019 is as follows:

	<u>\$</u>
Future aggregate minimum lease payments	36,173
Effect of discounting at the incremental rate of borrowing	<u>(1,176)</u>
Lease liability as at January 1, 2019	<u>34,997</u>

See Note 19.

### 4. EXPLORATION AND EVALUATION ASSETS

	<u>Flaxcombe</u>	<u>West Hazel</u>	<u>Total</u>
	(\$)	(\$)	(\$)
Balance at January 1, 2018	38,264	-	38,264
Additions	114,163	595,181	709,344
ARO	50,098	369,700	419,798
Reclassification	<u>(202,525)</u>	-	<u>(202,525)</u>
Balance at December 31, 2018	-	964,881	964,881
Additions	-	101,132	101,132
Disposals	-	(170,000)	(170,000)
Reclassification	-	<u>(896,013)</u>	<u>(896,013)</u>
Balance at December 31, 2019	<u>-</u>	<u>-</u>	<u>-</u>

## Hillcrest Petroleum Ltd.

Notes to the Consolidated Financial Statements

Years Ended December 31, 2019 and 2018

(Expressed in Canadian dollars)

---

### 4. EXPLORATION AND EVALUATION ASSETS (continued)

#### Flaxcombe Project, Saskatchewan

On December 14, 2017, the Company entered into a farm-in agreement with Westcore Energy Ltd. (“Westcore”) to workover two previously shut-in oil wells (16-13 and 7-13) in the Flaxcombe area of southwestern Saskatchewan. The Company was required to incur 100% of the workover costs in exchange for a 50% working interest in the wells. In accordance with an approved budget, the Company incurred \$152,427 to complete the workovers. Both wells were completed and reactivated in the first quarter of 2018, and as a result were reclassified to property and equipment.

#### West Hazel Project, Saskatchewan

On October 4, 2017, the Company entered into a joint venture agreement with Charterhouse Co. (“Charterhouse”), a private Alberta corporation, to workover four previously shut-in oil wells in southeastern Saskatchewan. The Company was required to incur 100% of the workover costs in exchange for a 75% working interest in the wells before of recovery of all reactivation costs incurred (“Payout”) and a 50% working interest after Payout.

If after the work program obligations have been completed for the West Hazel project (the “WH Property”), but prior to Payout for the WH Property, average total daily oil production from the WH Property over any calendar month, is less than 200 barrels per day and the Company’s working interest revenue from the WH Property is insufficient to cover the minimum financing costs related to that work program, then the Company may, at its sole discretion, retain net Charterhouse’s working interest revenue from the WH Property sufficient to meet the minimum financing cost for that month. Any retained Charterhouse revenue would be credited in Payout account calculations.

From the joint venture agreement date through February 2019, the Company completed \$878,040 in required workover costs to earn the 75% pre-Payout working interest. In February 2019, the Company sold 17% of its interest in the West Hazel project for cash proceeds of \$170,000, reducing its pre-Payout interest to 62.25% and its post-Payout interest to 41.5%. In addition, the Company completed the reactivation of three wells, and as a result the West Hazel project costs were reclassified to property and equipment.

## Hillcrest Petroleum Ltd.

Notes to the Consolidated Financial Statements  
Years Ended December 31, 2019 and 2018  
(Expressed in Canadian dollars)

### 5. PROPERTY AND EQUIPMENT

	<b>Computers</b>	<b>Oil and Gas Interests</b>	<b>Total</b>
	<b>(\$)</b>	<b>(\$)</b>	<b>(\$)</b>
<b>Cost</b>			
At January 1, 2018	16,028	1,713,407	1,729,435
Additions	-	202,525	202,525
At December 31, 2018	16,028	1,915,932	1,931,960
Reclassification from exploration and evaluation assets	-	896,013	896,013
Revaluation of decommissioning liabilities	-	(65,675)	(65,675)
<b>At December 31, 2019</b>	<b>16,028</b>	<b>2,746,270</b>	<b>2,762,298</b>
<b>Accumulated depletion and depreciation</b>			
At January 1, 2018	16,028	1,221,864	1,237,892
Depletion and depreciation for the year	-	-	-
At December 31, 2018	16,028	1,221,864	1,237,892
Depletion and depreciation for the year	-	146,267	146,267
<b>At December 31, 2019</b>	<b>16,028</b>	<b>1,368,131</b>	<b>1,384,159</b>
<b>Impairment</b>			
At January 1, 2018	-	491,543	491,543
Additions	-	202,525	202,525
<b>At December 31, 2018 and December 31, 2019</b>	<b>-</b>	<b>694,068</b>	<b>694,068</b>
<b>Carrying amounts:</b>			
At December 31, 2018	-	-	-
<b>At December 31, 2019</b>	<b>-</b>	<b>684,071</b>	<b>684,071</b>

#### West Hazel, Saskatchewan

In February 2019, three wells under the West Hazel farm-in agreement (see Note 4) were reactivated, and as a result the Company reclassified the associated costs from exploration and evaluation assets to property and equipment on the consolidated statement of financial position. The Company is the joint venture operator with its working interest of 62.25%. The owners of the other working interests are:

- 2042870 Alberta Ltd. (Charterhouse subsidiary): 25%;
- KFG Resources Ltd: 11.25%; and
- Geronimo Corp.: 1.5%

#### Flaxcombe, Saskatchewan

In January 2018, Well 16-13 and Well 07-13 under the Westcore farm-in agreement (see Note 4) were reactivated, and as a result the Company reclassified the associated costs from exploration and evaluation assets to property and equipment on the consolidated statement of financial position.

## Hillcrest Petroleum Ltd.

Notes to the Consolidated Financial Statements  
Years Ended December 31, 2019 and 2018  
(Expressed in Canadian dollars)

---

### 5. PROPERTY AND EQUIPMENT (continued)

#### Impairment

The Company's oil production assets were assessed for impairment against the proved and probable reserves within the Company's producing wells. The valuation determined that the pre-tax net present value of oil and gas reserves at a discount rate of 10% is \$4.525 million.

Proved reserves are the estimated quantities of oil and gas which geological and engineering data demonstrate with reasonable certainty to be recoverable in future years from known reservoirs under existing economic and operating conditions. Probable reserves are defined as those which have a better than 50% chance of being technically and economically recoverable.

At December 31, 2019, the Company's estimated total Proven and Probable Reserves were 282.4 Mboe. Assumptions for the fair value calculation included heavy oil prices ranging from \$54 – 63 bbl (2020 – 2026) and an inflation rate of 2%.

During the year ended December 31, 2019, the Company reviewed the carrying value of its oil and gas interests and determined there were no indicators of impairment with respect to the performance and operating costs of the West Hazel wells. For the year ended December 31, 2019, the Company recorded an impairment charge of \$Nil (2018: \$202,525).

The impairment charge for the year ended December 31, 2018 relates to the entire carrying value of the Flaxcombe property CGU, on the consolidated statement of income (loss) and comprehensive income (loss) after management determined the Flaxcombe assets to not be technically or economically viable.

### 6. ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

	December 31, 2019	December 31, 2018
	(\$)	(\$)
Trade payables	885,655	900,553
Related party payables (Note 10)	69,431	318,478
Accrued liabilities	443,941	233,013
GST payable	12,044	-
	<u>1,411,071</u>	<u>1,452,044</u>

### 7. SECURED LOANS

#### ASI Loan

As at December 31, 2019, the Company has \$138,550 (December 31, 2018 - \$138,550) outstanding on a senior secured loan facility that bears interest at a rate of 20% per annum and is currently payable on demand. As part of the consideration for the loan facility, the lenders and the arranging agent receive an aggregate 10% overriding royalty interest in the Company's proceeds from all oil, gas and other hydrocarbons produced from any new wells developed on the Company's Hartburg Properties using any portion of the proceeds from the loan. The Company has fully impaired these Hartburg assets and they are no longer producing.

During year ended December 31, 2019, the Company repaid \$Nil (2018 - \$Nil) in loan principal and incurred \$27,710 (2018 - \$27,710) in interest expense.

#### Bridge Loan

On August 10, 2016, the Company borrowed \$300,000 under a loan agreement (the "Bridge Loan") bearing interest at 1% per month, compounded monthly, and maturing on August 9, 2017. The Company also issued 1,500,000 common shares with a value of \$75,000 as payment of arrangement fees and syndication fees incurred in connection with the Bridge Loan. The cash received under the Bridge Loan has been allocated between the fair value of the loan liability and the value of the 1,500,000 common shares. The value ascribed to the common shares as at the loan date was \$75,000, and the residual

## Hillcrest Petroleum Ltd.

Notes to the Consolidated Financial Statements  
Years Ended December 31, 2019 and 2018  
(Expressed in Canadian dollars)

---

### 7. SECURED LOANS (continued)

amount has been allocated to the loan liability.

During the year ended December 31, 2019, the Company incurred \$45,406 (2018 - \$41,083) in interest expense and paid \$Nil (2018 - \$36,000) in accrued interest. At December 31, 2019 a total of \$403,433 (December 31, 2018 - \$358,027) in loan principal and accrued interest remained outstanding.

The loan is in default, but the Company continues to accrue interest in accordance with the agreement.

#### Ballakilley Loan

On June 15, 2017, the Company borrowed \$140,950 under a convertible loan agreement (the "Ballakilley Loan") bearing interest at 20% per annum, payable semi-annually, and maturing on May 31, 2019. The Ballakilley Loan is convertible into common shares of the Company at a price of \$0.07 per share, subject to a reduction if the Company completes a private placement or issues options or warrants at a lower price, at the option of the lender. The cash received under the Ballakilley Loan was allocated between the fair value of the loan liability and the value of the loan conversion feature which is considered an embedded derivative. The value ascribed to the loan liability as at the loan date was \$35,650, and the residual amount has been allocated to the loan conversion feature.

During the year ended December 31, 2019, the Company incurred \$36,221 (2018 - \$29,600) in interest expense and \$36,820 (2018 - \$52,028) in accretion of the loan liability. At December 31, 2019 a total of \$206,771 (December 31, 2018 - \$170,550) in loan principal and accrued interest remained outstanding. Additionally, on the basis of the private placement completed by the Company in December 2019 at \$0.03 per share, the loan conversion feature has been revalued to \$84,000 (2018 - \$52,500), and the Company has recorded a loss of \$31,500 (2018 - gain of \$21,200) on the consolidated statement of loss and comprehensive loss.

The loan is in default, but the Company continues to accrue interest in accordance with the agreement.

#### Project Financing

In February 2017, the Company entered into an arrangement with a third party to provide potential debt financing of up to \$2,500,000. The Company incurred standby charges at a rate of 7% per annum for the availability of this potential debt financing for the acquisition and development of oil projects located in Canada. Upon making a draw down under the facility additional fees would be incurred resulting in an effective borrowing rate of 20% per annum. The Company did not borrow any funds but has incurred standby charges totalling \$13,531 during the year ended December 31, 2019 (2018 - \$71,515). The arrangement is still currently in place but there are no funds currently incurring standby charges as at December 31, 2019. At December 31, 2019, a total of \$154,154 (2018 - \$260,623) in standby charges and interest on standby charges remained outstanding.

#### 1055328 BC Ltd. Loan

On October 6, 2017, the Company borrowed \$63,000 under a secured loan that bears 12% interest per annum and is repayable on or before October 6, 2018. On June 6, 2018, the Company borrowed an additional \$37,000 under the same terms.

During the year ended December 31, 2019 the Company incurred \$12,000 (2018 - \$10,832) in interest expense. At December 31, 2019, a total of \$123,871 (2018 - \$111,871) in loan principal and accrued interest remained outstanding.

The loan is in default, but the Company continues to accrue interest in accordance with the agreement.

### 8. UNSECURED LOANS

Significant unsecured loans are as follows:

#### Credit Line

On December 10, 2015, the Company obtained access to an unsecured line of credit bearing interest at an annual rate calculated semi-annually which is equal to the lending rate of the Canadian Imperial Bank of Commerce ("CIBC"). The credit

## Hillcrest Petroleum Ltd.

Notes to the Consolidated Financial Statements

Years Ended December 31, 2019 and 2018

(Expressed in Canadian dollars)

---

### 8. UNSECURED LOANS (continued)

line has a term of 30 months, and it has a maximum capacity of \$400,000 that requires monthly repayments equal to the lesser of i) \$15,000 and ii) the aggregate principal and interest outstanding. In addition, the Company issued 1,000,000 common shares as consideration to the lender. The Company borrowed \$390,000 under the credit line, and the cash received has been allocated between the fair value of the loan liability and the fair value of the 1,000,000 common shares. The fair value of the common shares as at the loan date was \$30,000, and the residual amount has been allocated to the loan liability.

During the year ended December 31, 2019, the Company incurred \$10,156 (2018 - \$19,437) in interest expense, including \$Nil (2018 - \$5,452) in accretion of the loan liability. At December 31, 2019, a total of \$95,859 (2018 - \$266,478) in loan principal and accrued interest remained outstanding.

#### Proactive Advance

On December 16, 2019, the Company received \$60,000 from Proactive Investors. This advance bears interest at 4% per annum and is intended to be applied towards a future private placement.

During the year ended December 31, 2019, the Company incurred \$99 (2018 - \$Nil) in interest expense. At December 31, 2019, a total of \$60,099 (2018 - \$Nil) in advance principal and interest remained outstanding.

### 9. CONVERTIBLE DEBENTURES

During the year ended December 31, 2019, the Company borrowed a total of \$55,000 under convertible debenture agreements (the "2019 Convertible Debentures") bearing interest at 15% per annum, payable quarterly, and maturing two years from the dates of advance.

The cash received under the 2019 Convertible Debentures has been allocated between the fair value of the loan liability and the conversion feature. The value ascribed to the loan liability as at the loan date was \$27,341, and the value ascribed to the conversion feature was \$27,659. Additionally, the loan conversion feature was revalued to \$7,439 at December 31, 2019 (2018 - \$Nil), and the Company has recorded a gain of \$20,220 (2018 - \$Nil) on the consolidated statement of loss and comprehensive loss.

During the year ended December 31, 2018, the Company borrowed a total of \$695,000 under convertible debenture agreements (the "2018 Convertible Debentures") bearing interest at 15% per annum, payable quarterly, and maturing two years from the dates of advance. A total of \$600,000 of the Convertible Debentures were issued to the CEO of the Company.

The cash received under the 2018 Convertible Debentures has been allocated between the fair value of the loan liability and the conversion feature. The value ascribed to the loan liability, net of transaction costs of \$5,731, as at the loan date was \$689,269, and the conversion feature was determined to have no value. In addition, the 20% retained profit interest which was attached to the Convertible Debentures and takes effect upon full loan repayment, and is applicable only to specific zones of the four original reactivation wells, was determined to have a fair value of \$116,000 which was recorded as financing expense during the year ended December 31, 2018.

The Convertible Debentures are secured by the West Hazel property and are convertible into common shares of the Company at a price equal to market price of the common shares of the Company in the first twelve months or the greater of \$0.10 and market price thereafter. In addition, should the West Hazel property be sold prior to the first anniversary of the advance date of the Convertible Debentures, then the Company will pay an amount equal to one full year of interest, the loan principal and 15% of any profit realized on the sale above the original reactivation costs. Should the West Hazel property be sold subsequent to the first anniversary of the advance date and prior to maturity of the Convertible Debentures, then the Company will pay an amount equal to the loan principal and 15% of any profit realized on the sale above the original reactivation costs.

During the year ended December 31, 2019, debenture holders converted \$577,081 (2018 - \$Nil) of debenture principal and interest payable via the issuance of 11,541,627 common shares, including \$557,081 payable to the CEO of the Company via the issuance of 11,141,627 common shares, and the Company repaid \$43,833 of debenture principal and \$107,274 of debenture interest. During the year ended December 31, 2019, the Company incurred \$126,622 (2018 - \$13,996) in interest and accretion expense. At December 31, 2019 a total of \$131,656 (December 31, 2018 - \$690,646) in loan principal and accrued interest remained outstanding.

## Hillcrest Petroleum Ltd.

Notes to the Consolidated Financial Statements

Years Ended December 31, 2019 and 2018

(Expressed in Canadian dollars)

### 10. RELATED PARTY TRANSACTIONS

The following summarizes the Company's related party transactions during the years ended December 31, 2019 and 2018. Key management personnel included the Chief Executive Officer ("CEO"), Chief Financial Officer ("CFO"), and directors and officers and companies controlled or significantly influenced by them:

#### Key management compensation

	<u>2019</u>	<u>2018</u>
	(\$)	(\$)
Management and consulting fees paid or accrued to directors, officers or corporations controlled by directors and officers of the Company*	271,350	365,850
Share-based payments paid to certain directors and officers of the Company in connection with the extension of the expiry dates of share purchase warrants and amendment of exercise prices of share purchase options	5,700	35,400
	<u>277,050</u>	<u>401,250</u>

\*For the year ended December 31, 2019, \$289,406 in gross management and consulting were billed by or accrued to related parties, with \$18,056 of management and consulting fees allocated to other West Hazel joint venture partners.

- a) As at December 31, 2019, a total of \$69,431 (December 31, 2018 - \$318,478) was included in accounts payable and accrued liabilities owing to the directors and officers or corporations controlled by directors and officers of the Company for unpaid consulting fees and reimbursable expenses. These liabilities are non-interest bearing and payable on demand.
- b) As at December 31, 2019, a total of \$Nil (December 31, 2018 - \$600,000) was included in convertible debentures owing to the CEO. A total of \$Nil (December 31, 2018 - \$57,353) was paid in advance for future interest payments and was recorded as prepaids on the consolidated statement of financial position (see Note 9).
- c) As at December 31, 2019, the Company owed a total of \$51,805 (December 31, 2018 - \$45,055) in loan principal and interest to the Chairman of the Company pursuant to a December 27, 2018 loan agreement where the Company borrowed \$45,000 from the Chairman. The loan bears interest at 15% and is repayable on demand.
- d) During the year ended December 31, 2019, related parties forgave a net amount of \$235,850 (2018 - \$Nil) in unpaid management and consulting fees accrued in prior years.

### 11. DECOMMISSIONING LIABILITY

The decommissioning liability relates to the expected present value of costs of plugging and abandoning the oil and gas held by Hillcrest. The provision for decommissioning is estimated after taking account of inflation, years to abandonment and an appropriate discount rate. As at December 31, 2019, the oil and gas properties had estimated abandonment dates between 2024 and 2028.

Actual decommissioning costs will ultimately depend upon future market prices for the decommissioning work required, which will reflect market conditions at the relevant time. Furthermore, the timing of decommissioning is likely to depend on when the fields cease to produce at economically viable rates. This in turn will depend upon future oil and gas prices, which are inherently uncertain.



**Hillcrest Petroleum Ltd.**

Notes to the Consolidated Financial Statements  
 Years Ended December 31, 2019 and 2018  
 (Expressed in Canadian dollars)

**11. DECOMMISSIONING LIABILITY** (continued)

The movement in the provision for the decommissioning liability was as follows:

	<b>Hartburg, Texas</b>	<b>West Hazel, Saskatchewan</b>	<b>Flaxcombe, Saskatchewan</b>	<b>Total</b>
	<b>(\$)</b>	<b>(\$)</b>		<b>(\$)</b>
Balance, January 1, 2018	42,844	-	-	42,844
Accretion	850	-	992	1,842
Additions	-	369,700	50,098	419,798
Balance, December 31, 2018	43,694	369,700	51,090	464,484
Change in estimate	-	(65,675)	-	(65,675)
Accretion	867	7,320	1,012	9,199
Disposal	(35,249)	-	-	(35,249)
Foreign exchange movement	428	-	-	428
Balance, December 31, 2019	9,740	311,345	52,102	373,187
Current portion	-	-	-	-
Non-current portion	9,740	311,345	52,102	373,187
	9,740	311,345	52,102	373,187

The total undiscounted amount of estimated cash flows required to settle the provision for decommissioning liability for the Hartburg Project was \$10,957 (US\$8,436) (December 31, 2018 - \$46,358 (US\$35,976)) as at December 31, 2019. The provision has been estimated using a risk-free discount rate of 1.98% (December 31, 2018 - 1.93%) and an inflation rate of 2.00% (December 31, 2018 - 2.00%).

The total undiscounted amount of estimated cash flows required to settle the provision for decommissioning liability for the Flaxcombe Project was \$60,950 (December 31, 2018 - \$60,950) at December 31, 2019. The provision has been estimated using a risk-free discount rate of 1.98% (December 31, 2018 - 1.93%) and an inflation rate of 2.00% (December 31, 2018 - 2.00%).

The total undiscounted amount of estimated cash flows required to settle the provision for decommissioning liability for the West Hazel Project was \$338,391 (December 31, 2018 - \$415,854) at December 31, 2019. The provision has been estimated using a risk-free discount rate of 1.68% (December 31, 2018 - 1.93%) and an inflation rate of 2.00% (December 31, 2018 - 2.00%).

## Hillcrest Petroleum Ltd.

Notes to the Consolidated Financial Statements

Years Ended December 31, 2019 and 2018

(Expressed in Canadian dollars)

---

### 12. SHARE CAPITAL

#### Authorized

Unlimited number of common shares without par value

#### Issued and outstanding

##### Year Ended December 31, 2019

- a) The Company completed a non-brokered private placement wherein it issued an aggregate of 3,900,000 units at \$0.05 per unit for gross proceeds of \$195,000. Each unit is comprised of one common share and one-half of one common share purchase warrant. Each whole warrant entitled the holder to acquire an additional common share at \$0.10 for two years from the date of closing of the placement. In September 2019, these exercise price of these warrants was repriced to \$0.05 per share. The Company used the residual method to determine the value of the warrants issued as part of the private placement. It was determined that the warrants issued as part of the private placement had a value of \$78,000.

The Company incurred \$2,146 in cash share issuance costs and issued 272,000 finder's warrants valued at \$1,891 and exercisable on the same terms as the private placement warrants in connection with the private placement. \$15,000 of the proceeds from this private placement remained unreceived as at December 31, 2019 and were written off from accounts receivable during the year ended December 31, 2019.

- b) The Company issued 400,000 common shares in connection with the conversion of a \$20,000 portion of the outstanding Convertible Debentures at \$0.05 per share.
- c) The Company issued 11,141,627 common shares in connection with the conversion of a \$557,081 portion of the outstanding Convertible Debentures at \$0.05 per share.
- d) The Company completed a non-brokered private placement wherein it issued an aggregate of 20,944,446 units at \$0.03 per unit for gross proceeds of \$628,333. Each unit is comprised of one common share and one common share purchase warrant. Each whole warrant entitles the holder to acquire an additional common share at \$0.05 for one year from the date of closing of the placement. The Company used the residual method to determine the value of the warrants issued as part of the private placement. It was determined that the warrants issued as part of the private placement had a value of \$Nil.

The Company incurred \$17,600 in cash share issuance costs and issued 586,666 finder's warrants valued at \$2,109 and exercisable on the same terms as the private placement warrants in connection with the private placement. Each finder's warrant entitles the holder to acquire an additional common share at \$0.05 for one year from the date of closing of the placement.

- e) The Company repriced a total of 6,140,600 existing share purchase warrants to \$0.05 per warrant, including:
- 3,636,887 share purchase warrants expiring February 27, 2020 from \$0.10 per warrant;
  - 553,713 share purchase warrants expiring March 23, 2020 from \$0.10 per warrant; and
  - 1,950,000 share purchase warrants expiring May 10, 2021 from \$0.10 per warrant.
- f) The Company repriced a total of 2,600,000 existing stock options to \$0.05 per option, including:
- 1,950,000 stock options expiring February 21, 2022 from \$0.07 per option;
  - 300,000 stock options expiring May 1, 2022 from \$0.06 per option; and
  - 350,000 stock options expiring June 13, 2022 from \$0.065 per option.

## Hillcrest Petroleum Ltd.

Notes to the Consolidated Financial Statements

Years Ended December 31, 2019 and 2018

(Expressed in Canadian dollars)

---

### 12. SHARE CAPITAL (continued)

#### Year Ended December 31, 2018

- a) The Company issued 1,700,000 common shares to settle \$85,000 in outstanding debts.
- b) The Company completed a non-brokered private placement in two tranches wherein it issued an aggregate of 9,992,000 units at \$0.05 per unit for gross proceeds of \$499,600. Each unit is comprised of one common share and one-half of one common share purchase warrant. Each whole warrant entitles the holder to acquire an additional common share at \$0.10 for two years from the date of closing of the placement. The Company used the residual method to determine the value of the warrants issued as part of the private placement. It was determined that the warrants issued as part of the private placement do not have any value. The Company incurred \$17,248 in share issuance costs in connection with this private placement.
- c) The Company issued 725,000 common shares due to the exercise of stock options at \$0.06 per share for gross proceeds of \$43,500. The fair value of the options was determined to be \$41,059, and accordingly the amount has been transferred from contributed surplus to share capital.

#### **Share Purchase Warrants**

#### Year Ended December 31, 2019

- a) The Company issued 1,950,000 share purchase warrants in connection with a non-brokered private placement. Each warrant originally entitled the holder to acquire a common share of the Company at \$0.10 per share until May 10, 2021. In September 2019, the exercise price of these warrants was repriced to \$0.05 per share. Pursuant to the same private placement, the Company also issued 272,000 finder's share purchase warrants exercisable on the same terms as the private placement warrants.
- b) The Company issued 20,944,446 share purchase warrants in connection with a non-brokered private placement. Each warrant entitles the holder to acquire a common share of the Company at \$0.05 per share until December 4, 2020. Pursuant to the same private placement, the Company also issued 586,666 finder's share purchase warrants exercisable on the same terms as the private placement warrants.

#### Year Ended December 31, 2018

- c) The Company issued 4,396,000 share purchase warrants in connection with the first tranche of a non-brokered private placement. Each warrant entitles the holder to acquire a common share of the Company at \$0.10 per share until February 27, 2020.
- d) The Company issued 600,000 share purchase warrants in connection with the second tranche a non-brokered private placement. Each warrant entitles the holder to acquire a common share of the Company at \$0.10 per share until March 23, 2020.

## Hillcrest Petroleum Ltd.

Notes to the Consolidated Financial Statements  
Years Ended December 31, 2019 and 2018  
(Expressed in Canadian dollars)

### 12. SHARE CAPITAL (continued)

The continuity of the Company's share purchase warrants is as follows:

	Number of Warrants	Weighted Average Exercise Price (\$)
Balance, January 1, 2018	11,897,429	0.08
Issued	4,996,000	0.10
Expired	(3,650,000)	0.08
Balance, December 31, 2018	13,243,429	0.09
Issued	23,753,112	0.05
Repriced – original prices	(6,140,600)	0.10
Repriced – amended prices	6,140,600	0.05
Expired	(7,247,429)	0.09
Balance, December 31, 2019	29,749,112	0.05

The following table summarizes the share purchase warrants outstanding as at December 31, 2019:

Number of Warrants	Weighted Average Exercise Price (\$)	Expiry Date	Weighted Average Remaining Contractual Life (yrs)
1,950,000	0.05	May 10, 2021	1.36
272,000*	0.10	May 10, 2021	1.36
20,944,446	0.05	December 4, 2020	0.93
586,666*	0.05	December 4, 2020	0.93
500,000	0.07	August 17, 2020	0.63
500,000	0.10	August 17, 2020	0.63
46,287	0.10	March 23, 2020	0.23
553,713	0.05	March 23, 2020	0.23
759,113	0.10	February 27, 2020	0.16
3,636,887	0.05	February 27, 2020	0.16
29,749,112	0.05		0.82

\*Finder's warrants

### Stock Options

Effective November 4, 2010, the Company adopted a stock option plan to grant stock options to its directors, officers, employees and consultants. In accordance with the policies of the TSXV, the aggregate number of securities reserved for issuance under the plan, at any point in time, will be 10% of the number of common shares of the Company issued and outstanding at the time the option is granted, less any common share reserved for issuance under share options granted under share compensation arrangements other than the plan. The exercise price of option grants will be determined by the Board of Directors, but will not be less than the closing market price of the common shares on the Exchange at the time of grant. All unexercised options granted under the plan will expire no later than five years from the date of grant.

The Company granted an aggregate of 950,000 stock options during the year ended December 31, 2018. The options vest over different time periods, and the Company expensed \$41,598 as share-based compensation. The Company expensed an additional \$744 during the year ended December 31, 2019 in connection with the 2018 option grants.

## Hillcrest Petroleum Ltd.

Notes to the Consolidated Financial Statements  
Years Ended December 31, 2019 and 2018  
(Expressed in Canadian dollars)

---

### 12. SHARE CAPITAL (continued)

The options granted were valued using the Black-Scholes option pricing model under the following weighted average assumptions:

	<b>2018</b>
Risk-free interest rate	2.11%
Expected life of options	3.7 years
Volatility	149%
Expected Dividend yield	Nil
Forfeiture rate	Nil
Weighted average fair value	\$0.05

During the year ended December 31, 2019, the Company expensed \$5,700 as share-based compensation for the incremental value of repricing 2,600,000 stock options with prices originally ranging from \$0.06 to \$0.07 per option to amended prices of \$0.05 per option. The incremental value was determined using the Black-Scholes option pricing model under the following weighted average assumptions:

	<b>2019</b>
Risk-free interest rate	1.62%
Expected life of options	2.43-2.73 years
Volatility	83-87%
Expected Dividend yield	Nil
Forfeiture rate	Nil
Weighted average fair value	\$0.002

The continuity of the Company's stock options is as follows:

	<b>Number of Options</b>	<b>Weighted Average Exercise Price (\$)</b>
Balance, January 1, 2018	6,400,000	0.07
Issued	950,000	0.06
Exercised	(725,000)	0.06
Expired	(1,700,000)	0.06
Balance, December 31, 2018	4,925,000	0.07
Repriced – original prices	(2,600,000)	0.07
Repriced – amended prices	2,600,000	0.05
Cancelled	(275,000)	0.07
Balance, December 31, 2019	4,650,000	0.06

## Hillcrest Petroleum Ltd.

Notes to the Consolidated Financial Statements  
Years Ended December 31, 2019 and 2018  
(Expressed in Canadian dollars)

---

### 12. SHARE CAPITAL (continued)

The following table summarizes the stock options outstanding and exercisable as at December 31, 2019:

Number of Options Outstanding	Number of Options Exercisable	Weighted Average Exercise Price (\$)	Expiry Date	Weighted Average Remaining Contractual Life (yrs)
300,000	300,000	0.05	April 3, 2021	1.26
1,750,000	1,750,000	0.07	February 21, 2022	2.15
1,950,000	1,950,000	0.05	February 21, 2022	2.15
300,000	300,000	0.05	May 1, 2022	2.33
350,000	350,000	0.05	June 13, 2022	2.45
4,650,000	4,650,000	0.06		2.12

### 13. COMMITMENTS

The Company had the following commitments as at December 31, 2019:

- The Company entered into an office rental agreement in Vancouver, British Columbia with a term of 36 months, terminating on June 15, 2020. The remaining base rent payable under the lease is \$13,436 up until the lease expires. In addition to the base rent of \$2,067 per month, the Company's share of operating costs is estimated at approximately \$1,598 per month.
- HEL entered into an office rental agreement with a term of 72 months, terminating on February 28, 2023. The landlord issued a notice of termination to the Company effective January 31, 2019 and has sent a demand for payment of \$43,961 (US\$32,245) representing unpaid rental charges under the rental agreement. The Company has recognized the full liability as at December 31, 2019.

See Note 20.

### 14. GEOGRAPHICAL SEGMENTED INFORMATION

The Company is engaged in one business activity, being the acquisition, exploration, development and production of oil and gas reserves in Canada and the United States. For the year ended December 31, 2019, all revenues were derived from operations in Canada and all non-current assets were located in Canada (2018 - all revenues were derived from operations in Canada and all non-current assets were located in Canada).

### 15. CAPITAL MANAGEMENT

The Company manages its capital structure and makes adjustments to it, based on the funds available to the Company, in order to support the acquisition, exploration and development of oil and gas properties. The Board of Directors does not establish quantitative return on capital criteria for management, but rather relies on the expertise of the Company's management to sustain future development of the business.

The Company is primarily dependent on external financing to fund its activities. In order to carry out the planned exploration and development and pay for administrative costs, the Company will spend its existing working capital and raise additional funds as needed using best efforts. The Company will continue to assess new properties and seek to acquire an interest in additional properties if it feels there is sufficient economic potential and if it has adequate available or committed financial resources to complete such acquisitions.

Management reviews its capital management approach on an ongoing basis and believes that this approach, given the size of the Company, is reasonable.

## Hillcrest Petroleum Ltd.

Notes to the Consolidated Financial Statements  
Years Ended December 31, 2019 and 2018  
(Expressed in Canadian dollars)

---

### 15. CAPITAL MANAGEMENT (continued)

There were no changes in the Company's approach to capital management during the year ended December 31, 2019. The Company is not subject to externally imposed capital requirements.

### 16. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT

#### Financial Risk Management

The Company's financial instruments that are measured at fair value on a recurring basis in periods subsequent to initial recognition and the fair value hierarchy used to measure them are presented in the table below. The Company classifies its other financial assets and other financial liabilities measured at fair value using a fair value hierarchy that reflects the significance of the inputs used in making the measurements.

The fair value hierarchy has the following levels:

- Level 1: Quoted prices (unadjusted) in active markets for identical assets or liabilities;
- Level 2: Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices); and
- Level 3: Inputs for the asset or liability that is not based on observable market data (unobservable inputs).

The Board of Directors has overall responsibility for the establishment and oversight of the Company's risk management framework. The Company's financial instruments consist of cash, receivables, accounts payable and accrued liabilities and loans.

The fair value of cash, receivables and accounts payable and accrued liabilities approximate their book values because of the short-term nature of these instruments. The carrying amounts of the loans approximate fair value as the applicable interest rates, which were negotiated between the Company and arm's length third parties, are similar to market interest rates which would be available to the Company at the balance sheet date. The fair value of the convertible debentures has been determined after deducting transaction costs and allocating the portion of the proceeds applicable to the retained profit interest.

#### Financial Instrument Risk Exposure

The Company is exposed in varying degrees to a variety of financial instrument related risks. The Board approves and monitors the risk management processes.

#### Credit risk

The Company's credit risk is primarily attributable to cash and accounts receivable. The Company's maximum exposure to credit risk at the end of the reporting period is the carrying value of these assets. Substantially all of the Company's customers are in the oil and natural gas industry and are subject to normal industry credit risks. The remaining customers are related to the recovery of shared office rent and share subscription proceeds. The Company has minimal collection risk related to these receivables and expects to collect the outstanding receivables in the normal course of operations. At December 31, 2019, the maximum credit exposure is the carrying amount of Receivables of \$87,919 (December 31, 2018 - \$38,505).

The Company has no significant concentration of credit risk arising from operations. Cash is held with reputable financial institutions, from which management believes the risk of loss to be remote.

#### Market risk

Market risk is the risk of loss that may arise from changes in market factors such as interest rates, foreign exchange rates, and commodity and equity prices. The Company's primary commodity is heavy oil which is closely tied to the price of Western Canadian Select.

#### Interest rate risk

The Company is exposed to interest rate risk. The Company has an unsecured loan associated with a CIBC line of credit which has a variable interest rate, recalculated quarterly. A 1% change in market interest rates would result in an increase/decrease of \$1,948 on the Company's net loss.

## Hillcrest Petroleum Ltd.

Notes to the Consolidated Financial Statements  
Years Ended December 31, 2019 and 2018  
(Expressed in Canadian dollars)

---

### 16. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT (continued)

#### Liquidity risk

The Company's approach to managing liquidity risk is to ensure that it will have sufficient liquid capital to meet its current liabilities as they come due. At December 31, 2019, the Company had a working capital deficiency of \$2,645,147 (December 31, 2018 - \$2,400,807). The Company finances its operations through a combination of cash, loans, equity and convertible debentures. The Company's ability to continue as a going concern is dependent upon the ongoing support from its lenders and its ability to fund the repayment of its debt by generating positive cash flows from operations, securing funding from additional debt, equity financing, disposing of assets or making other arrangements. Refer to Note 1 for further discussion.

The Company's financial liabilities had contractual maturities as follows:

	<u>2019</u>	<u>2018</u>
	(\$)	(\$)
Less than 1 year	2,824,974	2,616,800
Between 1 – 2 years	39,763	594,686
Between 2 – 5 years	-	-
	<u>2,864,737</u>	<u>3,211,486</u>

#### Foreign currency risk

Foreign currency exchange rate risk is the risk that the fair value of financial instruments or future cash flows will fluctuate as a result of changes in foreign exchange rates. The Company operates in Canada and the United States. All of the Company's oil sales are denominated in Canadian dollars. As a result, the Company has minimal exposure to foreign exchange risk.

### 17. SUPPLEMENTAL CASH FLOW INFORMATION

	<u>2019</u>	<u>2018</u>
	(\$)	(\$)
<b>Non-cash investing and financing activities:</b>		
Recognition of the estimated asset retirement obligation for the Flaxcombe and West Hazel properties	-	419,798
Change in estimate of asset retirement obligation for the West Hazel property	65,675	-
Common shares issued upon the conversion of convertible debentures	577,081	-
Common shares issued to settle outstanding liabilities	-	85,000
Exploration and evaluation assets reclassified to property and equipment	896,013	152,427
<b>Interest paid during the year</b>	263,714	60,705
<b>Income taxes paid during the year</b>	<u>-</u>	<u>-</u>

Also see Note 19.



**Hillcrest Petroleum Ltd.**

Notes to the Consolidated Financial Statements

Years Ended December 31, 2019 and 2018

(Expressed in Canadian dollars)

**18. INCOME TAXES****a) Provision for Income Taxes**

A reconciliation of the combined income taxes at statutory rates and the Company's effective income tax expense is as follows:

	<b>2019</b>	<b>2018</b>
	<b>(\$)</b>	<b>(\$)</b>
Income (loss) for the year	(1,201,929)	(1,866,535)
Expected income tax expense (recovery) at 27%	(325,000)	(504,000)
Non-deductible items	-	(3,000)
Difference due to overseas tax rates and foreign exchange	(46,000)	13,000
Change in unrecognized deductible temporary differences	371,000	494,000
Income tax expense	-	-

**b) Deferred Income Taxes**

The components of the Company's deferred income tax asset balances are as follows:

	<b>2019</b>	<b>2018</b>
	<b>(\$)</b>	<b>(\$)</b>
Non-capital losses carry-forwards	2,759,000	2,433,000
Property and equipment	364,000	547,000
Share issuance costs	9,000	5,000
Other	57,000	84,000
	<b>3,189,000</b>	<b>3,069,000</b>

Tax attributes are subject to review, and potential adjustment, by tax authorities.

**c) Unrecognized Deductible Temporary Differences and Unused Tax Losses**

The Company's unrecognized deductible temporary differences and unused tax losses consist of the following:

	<b>2019</b>	<b>2018</b>
	<b>(\$)</b>	<b>(\$)</b>
Non-capital losses carry-forwards	10,249,000	9,200,000
Property and equipment	1,348,000	2,015,000
Share issuance costs	32,000	17,000
Other	211,000	211,000

## Hillcrest Petroleum Ltd.

Notes to the Consolidated Financial Statements  
Years Ended December 31, 2019 and 2018  
(Expressed in Canadian dollars)

---

### 19. RIGHT-OF-USE ASSET/LEASE LIABILITY

On June 15, 2017, the Company entered into an office rental agreement in Vancouver, British Columbia with a term of 36 months, terminating on June 15, 2020. Pursuant to this agreement, the Company has a commitment to lease office space at a base rent rate of \$24,804 per annum, plus common costs and taxes.

#### a) Right-of-use asset

As at December 31, 2019, the right-of-use asset recorded for the Company's office premises was as follows:

	<b>2019</b>
	<b>\$</b>
As at December 31, 2018	-
IFRS 16 adoption	35,668
Amortization	<u>(23,136)</u>
As at December 31, 2019	<u><u>12,532</u></u>

#### b) Lease liability

Minimum lease payments in respect of lease liabilities and the effect of discounting as at December 31, 2019 are as follows:

	<b>2019</b>
	<b>\$</b>
Undiscounted minimum lease payments:	
Less than one year	11,369
Effect of discounting	<u>(104)</u>
Present value of minimum lease payments	<u><u>11,265</u></u>

#### c) Lease liability continuity

The net change in the Company's lease liability during the year ended December 31, 2019 was as follows:

	<b>2019</b>
	<b>\$</b>
As at December 31, 2018	-
IFRS 16 adoption	34,997
Principal payments	<u>(23,732)</u>
As at December 31, 2019	<u><u>11,265</u></u>

Interest of \$1,072 for the year ended December 31, 2019 (2018 - \$nil) is included in financing expenses.

See Note 3(n).

## Hillcrest Petroleum Ltd.

Notes to the Consolidated Financial Statements

Years Ended December 31, 2019 and 2018

(Expressed in Canadian dollars)

---

### 20. SUBSEQUENT EVENTS

Subsequent to December 31, 2019:

- a) The Company issued 900,000 common shares in connection with the conversion of a portion of the outstanding Convertible Debentures at \$0.05 per share.
- b) A total of 4,396,000 share purchase warrants exercisable at \$0.05 expired unexercised on February 27, 2020.
- c) A total of 600,000 share purchase warrants exercisable at \$0.10 expired unexercised on March 23, 2020.
- d) The Company entered into a non-binding memorandum of intent with Oropass Ltd. ("Oropass") to form and invest in a joint venture with Oropass on a 50% basis each to license and market certain intellectual property in the United States ("USA Licensing Rights MOI"). Under the USA Licensing Rights MOI, the Company paid \$10,000 of an initial \$15,000 deposit payable, with Oropass paying the other \$5,000, to a third party that originally licensed the intellectual property to Oropass. Formation of a joint venture is subject to the Company securing \$500,000 of joint venture seed funding and entry of the Company and Oropass into a joint venture shareholders' agreement.
- e) The Company entered into a non-binding memorandum of intent with Oropass to form and invest in a joint venture with Oropass on a 50% basis each to license and market certain intellectual property in the European Union ("EU Licensing Rights MOI"). Under the EU Licensing Rights MOI, the Company paid an initial \$10,000 deposit payable to a third party that originally licensed the intellectual property to Oropass. Formation of a joint venture is subject to the Company securing joint venture seed funding, the submission of European Union patent applications on or before August 1, 2020 and entry of the Company and Oropass into a joint venture shareholders' agreement.
- f) On May 6, 2020, the Company extended its existing office rental agreement in Vancouver, British Columbia, originally set to terminate June 15, 2020, to November 30, 2020. Under the extension agreement, the Company will pay base rent of \$2,385 per month, plus common costs and taxes, from June to November 2020.
- g) The outbreak of the novel strain of coronavirus ("COVID-19") has resulted in governments enacting emergency measures to combat the spread of the virus. These measures, which include the implementation of travel bans, self-imposed quarantine periods and social distancing, have caused an economic slowdown and material disruption to business. Government has reacted with interventions intended to stabilize economic conditions. The duration and impact of the COVID-19 outbreak is unknown at this time. It is not possible to reliably estimate the length and severity of these developments and the impact on the financial performance and financial position of the Company in future periods.