Petro Viking Energy Inc.
Consolidated Financial Statements
December 31, 2013 and 2012

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Auditors' Report

To the Shareholders of Petro Viking Energy Inc.:

We have audited the accompanying consolidated financial statements of Petro Viking Energy Inc. and its subsidiary (the "Company"), which comprise the consolidated statements of financial position as at December 31, 2013 and 2012 and the consolidated statements of operations, loss and comprehensive loss, changes in shareholders' equity and cash flows for the years then ended, and a summary of significant accounting policies and other explanatory information.

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

Auditor's Responsibility
Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements 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 entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained in our audits is sufficient and appropriate to provide a basis for our audit opinion.

Opinion
In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of Petro Viking Energy Inc. and its subsidiary as at December 31, 2013 and 2012 and their financial performance and their cash flows for the years then ended in accordance with International Financial Reporting Standards.

Emphasis of Matter – Going Concern
Without qualifying our opinion, we draw attention to Note 1 in the consolidated financial statements which indicates the existence of a material uncertainty which may cast significant doubt about the ability of Petro Viking Energy Inc. to continue as a going concern.

MNP LLP
Chartered Accountants

Calgary, Alberta
April 30, 2014

		December 31, 2013		December 31, 2012
Assets				
Current				
Cash and cash equivalents	$	152,041	$	368,468
Accounts receivable *(note 4)*		702,969		494,924
Prepaid expenses and deposits		42,155		19,538
Total current assets		897,165		882,930
Property and equipment *(note 6)*		1,250,065		1,731,686
Total assets	**$**	**2,147,230**	**$**	**2,614,616**
Liabilities				
Current				
Accounts payable and accrued liabilities *(note 7)*	$	1,023,212	$	584,836
Debentures *(note 9)*		640,000		640,000
Notes payable *(note 8)*		300,000		-
Total current liabilities		1,963,212		1,224,836
Decommissioning liabilities *(note 10)*		4,173,189		3,778,928
Total liabilities		6,136,401		5,003,764
Shareholders' Deficiency				
Share capital *(note 11)*		4,525,521		4,525,521
Warrants *(note 13)*		-		870,773
Contributed surplus		1,617,760		746,987
Deficit		(10,132,452)		(8,532,429)
Total shareholders' deficiency		(3,989,171)		(2,389,148)
Total liabilities and shareholders' deficiency	**$**	**2,147,230**	**$**	**2,614,616**

Going concern *(note 1)*

Contingency *(note 25)*

Subsequent events *(note 26)*

Approved on behalf of the Board of Directors

"Irvin Eisler" (signed) — **Irvin Eisler**

"Lars Glimhagen" (signed) — **Lars Glimhagen**

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

	Year ended December 31, 2013	Year ended December 31, 2012
Revenue		
Petroleum and natural gas sales *(note 14)*	$ 896,732	$ 1,160,548
Other Income *(note 15)*	2,300	95,070
Total revenue	899,032	1,255,618
Expenses		
Operating and production	724,197	1,198,527
General and administrative *(note 17)*	641,151	1,495,725
Share-based compensation *(note 12)*	-	163,175
Depletion, depreciation and impairment *(notes 5 and 6)*	983,120	1,067,720
Financing costs *(note 16)*	150,587	101,819
Total expenses	2,499,055	4,026,966
Net loss and comprehensive loss before income taxes	**$ (1,600,023)**	**$ (2,771,348)**
Deferred tax recovery *(note 23)*	-	-
Net loss and comprehensive loss	**$ (1,600,023)**	**$ (2,771,348)**
Net loss per share *(note 18)*		
Basic	$ (0.05)	$ (0.09)
Diluted	$ (0.05)	$ (0.09)
Weighted average number of shares *(note 18)*		
Basic	30,259,707	30,099,756
Diluted	30,259,707	30,099,756

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

	Year ended December 31, 2013	Year ended December 31, 2012
Share capital *(note 11)*		
Balance, beginning of year	$ 4,525,521	$ 4,367,233
Issued	-	112,000
Option value transferred to share capital from contributed surplus	-	46,288
Balance, end of year	4,525,521	4,525,521
Warrants *(note 13)*		
Balance, beginning of year	870,773	870,773
Expired share purchase warrants	(870,773)	-
Balance, end of year	-	870,773
Contributed surplus		
Balance, beginning of year	746,987	630,100
Share-based compensation related to:		
Options granted to directors, officers and consultants	-	163,175
Option value transferred from contributed surplus to share capital	-	(46,288)
Expired warrants	870,773	-
Balance, end of year	1,617,760	746,987
Deficit		
Balance, beginning of year	(8,532,429)	(5,761,081)
Net loss and comprehensive loss	(1,600,023)	(2,771,348)
Balance, end of year	(10,132,452)	(8,532,429)
Shareholders' Deficiency	**$ (3,989,171)**	**$ (2,389,148)**

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

	Year ended December 31, 2013	Year ended December 31, 2012
Operating		
Net loss and comprehensive loss for the year	$ (1,600,023)	$ (2,771,348)
Add back (deduct) non-cash items:		
Share-based compensation *(note 12)*	-	163,175
Depletion, depreciation and impairment	983,120	1,067,720
Accretion on decommissioning liabilities *(note 16)*	57,475	45,490
Gain on sale of asset *(note 6)*	-	(83,000)
Cash settlement of decommissioning liabilities *(note 10)*	(26,065)	(43,245)
Changes in non-cash working capital *(note 19)*	141,808	224,690
Cash flows used in operating activities	(443,685)	(1,396,518)
Financing		
Issue of equity instruments *(note 11)*	-	112,000
Changes in non-cash working capital *(note 19)*	-	-
Issue of notes payable *(note 8)*	300,000	-
Cash flows provided by financing activities	300,000	112,000
Investing		
Expenditures on property and equipment	(138,648)	(129,077)
Expenditures on exploration and evaluation *(note 5)*	-	(93,750)
Sale of non-current asset *(note 6)*	-	83,000
Sale of short-term investment	-	650,242
Changes in non-cash working capital *(note 19)*	65,906	(997,551)
Cash flows used in investing activities	(72,742)	(487,136)
Change in cash	(216,427)	(1,771,654)
Cash, beginning of the year	368,468	2,140,122
Cash, end of the year	**$ 152,041**	**$ 368,468**
Supplemental cash flow information		
Interest received	2,300	12,070
Interest paid	15,689	56,329
Non-cash transactions		
Option value transferred from contributed surplus to share capital	-	46,288
Expired warrants	$ 870,773	$ -

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

1. Corporate information and going concern

Petro Viking Energy Inc. ("Petro Viking" or the "Company") is incorporated under the laws of the province of Alberta with shares listed on the TSX Venture Exchange, and is engaged in petroleum and natural gas exploration and development activities in western Canada. The records office and principal address is located at 500 – 5940 Macleod Trail SW, Calgary, Alberta T2H 2G4.

These consolidated financial statements include the accounts of the Company and its wholly owned subsidiary, Petro Viking Management Corp. ("PVMC"), after the elimination of intercompany transactions and balances.

The business of exploring for oil and gas involves a high degree of risk and there can be no assurance that planned exploration and development programs will result in profitable reserves that are economically recoverable. The recovery of amounts capitalized for resource properties and related costs in the consolidated statement of financial position is dependent upon the existence of economically recoverable reserves, the ability of the Company to arrange appropriate financing to complete development of its properties and upon future profitable production or proceeds from their disposition. Changes in future conditions could require material write-downs of the carrying values of its properties.

The consolidated financial statements have been prepared using International Financial Reporting Standards applicable to a going concern, which assumes continuity of operations and realization of assets and settlement of liabilities in the normal course of business. In assessing whether or not there are material uncertainties that may lend doubt as to the ability of the Company to continue as a going concern, management takes into account all available information about the future, which is at least but is not limited to twelve months from the end of the reporting period. Management is aware of the material uncertainties that could cast significant doubt upon the Company's ability to continue as a going concern. As at December 31, 2013, the Company reported a net loss of $1,600,023 and a negative working capital of $1,066,047. Included in the current year's loss is an impairment loss of $736,000 as a reflection of a decrease in the carrying values of its oil and gas assets. As a result the Company will need to raise additional financing within the next twelve months in order to meet its liabilities as they come due and to continue with its business activities.

2. Basis of presentation

These consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB") and the interpretations of the International Financial Reporting Interpretation Committee (IFRIC") in effect at the closing date of December 31, 2013.

The consolidated financial statements were authorized by the Board of Directors for issue on April 30, 2014.

3. Summary of significant accounting policies

a) Basis of measurement

The consolidated financial statements have been prepared under the historical cost method, except for certain equity instruments and financial instruments measured at fair value.

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

b) Basis of consolidation

(i) Subsidiaries

Subsidiaries are entities controlled by the Company. Control exists when the Company has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. In assessing control, potential voting rights that currently are exercisable are taken into account. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases.

(ii) Joint operations

A portion of the Company's petroleum and natural gas exploration and production activities are conducted jointly with others, and, accordingly, these financial statements reflect only the Company's proportionate interest in such activities.

(iii) Transactions eliminated on consolidation

Intercompany balances and transactions, and any unrealized income and expenses arising from intercompany transactions, are eliminated in preparing the consolidated financial statements.

c) Cash and cash equivalents

Cash and cash equivalents are comprised of cash in banks and all short-term investments that are highly liquid in nature, cashable, and have an original maturity date of three months or less.

d) Exploration and Evaluation Expenditures

Pre-license costs are expensed as incurred. Exploration and evaluation expenditures directly attributable to the exploration for petroleum and natural gas reserves are capitalized as exploration and evaluation assets on an area basis. These costs include, but are not limited to: lease acquisition either directly or by business combination, lease rentals on undeveloped properties, acquisition of rights to explore, geological, and geophysical costs, exploratory drilling of both productive and unproductive wells and overhead charges. No depletion or amortization is charged during the exploration and evaluation phase.

Exploration and evaluation expenditures are capitalized until reserves are evaluated and determined to be commercially viable and technically feasible. If reserves are not identified, these costs are expensed. The balance of exploration and evaluation expenditures is carried forward as an exploration and evaluation asset in the statement of financial position where the mineral rights are current and it is considered probable that costs will be recovered through the future development or sale of the property.

If it is determined that a commercial discovery of reserves will not be achieved, the capitalized exploration and evaluation assets are written down to their recoverable amounts. Where commercial discovery of reserves has been made, the exploration and evaluation assets are tested for impairment and transferred to property and equipment as petroleum and natural gas properties.

3. Summary of significant accounting policies *(continued from previous page)*

e) Property and equipment

(i) Property and equipment

Property and equipment (P&E) are carried at cost, less accumulated depletion, depreciation and impairment losses. The cost of an item of P&E consists of the purchase price, any costs directly attributable to bringing the asset into the location and condition necessary for its intended use, a discounted current estimate of the decommissioning costs and borrowing costs for qualifying assets. All costs incurred to identify and evaluate assets are expensed as incurred.

Petroleum and natural gas capitalized costs are depleted using the unit-of-production method. Depletion is calculated using the ratio of production in the year to the remaining total proved and probable reserves before royalties, taking into account future development costs prior to inflation necessary to bring those reserves into production. These estimates are evaluated and reported on by independent reserve engineers annually. Proven and probable reserves are estimated using independent reserve engineer reports.

Where an item of P&E comprises major components with different useful lives, the components are accounted for as separate items of P&E. The expected useful lives of P&E, residual values and methods of depreciation are reviewed at each reporting period and, if necessary, changes are accounted for prospectively.

Changes in estimates such as quantities of proved and probable reserves that affect unit-of-production calculations are applied on a prospective basis.

An item of P&E is derecognized upon disposal or is impaired when no future economic benefits are expected to arise from the continued use of the asset. Any gain or loss on disposal of the asset, determined as the difference between the net proceeds and the carrying amount of the asset, is recognized in the statement of operations, loss and comprehensive loss in the period incurred.

The carrying amounts of property and equipment are reviewed for impairment when indicators of such impairment exist. If indicators exist, the assets are tested for impairment under IAS 36.

(ii) Impairment of non-financial assets

At each financial reporting date, the carrying amounts of property and equipment are reviewed to determine whether there is any indication that those assets are impaired. If such indication exists, an estimate of the recoverable amount of the asset is calculated.

Individual assets are grouped together for impairment assessment purposes into the smallest group of assets that generates cash inflows from continuing use that are largely independent of the cash inflows of other assets or groups of assets (the cash generating unit or CGU). The carrying amount of P&E assets within a CGU are compared to the recoverable amount of the CGU.

A CGU's recoverable amount is the higher of its fair value less costs to sell and its value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money to the Company and the risks specific to the asset. In determining fair value less cost to sell, recent market transactions are taken into account, if available. If no transactions can be identified, an appropriate valuation model is used.

Where the carrying amount of a CGU exceeds its recoverable amount, the CGU is considered impaired and is written down to its recoverable amount. The impairment loss is charged to the statement of operations, loss and comprehensive loss. A previously recognized impairment loss is reversed or partially reversed only if there has been a change in the assumptions used to determine the assets recoverable amount since the last impairment loss was recognized. If that is the case, the carrying amount of the asset is increased to its recoverable amount. The new carrying amount cannot exceed the carrying amount that would have been determined, net of depletion and depreciation, had no impairment loss been recognized for the asset in prior periods.

3. Summary of significant accounting policies *(continued from previous page)*

e) Property and equipment *(continued from previous page)*

(iii) Decommissioning liabilities

The Company recognizes a decommissioning liability in the period it arises with a corresponding increase to the carrying amount of the related asset. Measurement occurs when a legal or constructive obligation arises. Provisions are measured at the present value of the expenditures expected to be required to settle the obligation discounted using the pre-tax risk-free rate, updated at each reporting date. The increase in the provision due to the passage of time (accretion) is recognized as a financing cost whereas increases or decreases due to changes in the estimated cost to decommission the asset are capitalized as P&E. Actual costs incurred upon settlement of the decommissioning liability reduce the liability to the extent the provision was established. The related decommissioning asset is depreciated or depleted on the same basis as the P&E to which it relates.

(iv) Maintenance and turnarounds

Expenditures associated with activities that improve the productive capacity or extend the life of an asset are capitalized. These costs are included in P&E when incurred and charged to depletion and depreciation over the estimated useful life. Any remaining carrying amounts of any replaced or sold components are derecognized. Maintenance and repairs, other than major turnaround costs, are expensed as incurred.

f) Provisions

Provisions are recognized when the Company has a present obligation as a result of a past event, it is probable that an outflow of resources will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation. The provisions are measured at Management's best estimate of the expenditure required to settle the obligation at the balance sheet date, and are discounted to present value where the effect of time is material.

g) Share capital

Common shares issued for non-monetary consideration are recorded at their fair market value based upon the trading price of the Company's shares on the TSX Venture Exchange. Share issue costs incurred on the issue of the Company's shares are charged directly to share capital.

h) Flow-through shares

Expenditure deductions for income tax purposes related to exploratory activities funded by flow-through equity instruments are renounced to investors in accordance with income tax legislation. The difference between the value ascribed to flow-through shares issued and the value that would have been received for common shares at the date of issuance of the flow-through shares is initially recognized as a liability on the Statement of Financial Position. The liability is reversed when tax benefits are renounced and a deferred tax liability is recognized at that time. Income tax expense is the difference between the amount of the deferred tax liability and the liability recognized on issuance.

i) Revenue recognition

Revenue is recognized from oil sales when the oil is delivered to the buyer and from gas sales when the gas passes through the pipeline at the delivery point. Interest income is recorded as earned.

j) Transportation

The Company is contractually obligated to pay to transport on the Company's share of oil and gas products sold to the nearest market terminal. These costs are presented in the statement of operations, loss and comprehensive loss within operating and production expense.

3. Summary of significant accounting policies *(continued from previous page)*

k) Income taxes

Income tax expense represents the sum of current tax expense and deferred tax expense. Current tax expense is based on the taxable profits for the year. Income tax is recognized in the statement of operations, loss and comprehensive loss except to the extent that it relates to items recognized directly in equity, in which case it is recognized in equity.

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

Deferred tax assets and liabilities are recognized based on differences in the financial statement carrying amount for assets and liabilities and the associated tax balance. Deferred tax liabilities are generally recognized for all taxable temporary differences. Deferred tax assets are generally recognized for all deductible temporary differences, unused tax credits carried forward and unused tax losses to the extent that it is probable that there will be taxable profits against which deductible temporary differences can be utilized.

Deferred taxes are measured based on enacted or substantively enacted tax rates for the period in which the temporary differences are expected to be realized or settled, and are presented as non-current.

Deferred tax assets and liabilities are offset when there is a legally enforceable right to offset current tax assets against current tax liabilities, when they relate to income taxes levied by the same taxation authority and when the Company intends to settle its current tax assets and liabilities on a net basis.

l) Share-based compensation plans

When options to purchase shares are granted to employees, directors, officers and consultants, the fair value of the options on the date of the grant, using the Black-Scholes option pricing model, is recognized as a compensation expense, with a corresponding increase in contributed surplus, over the period during which the related options vest. An estimated forfeiture rate is applied to the options granted before applying the Black-Scholes pricing model except for options which vest immediately on issuance for which no forfeiture is required. When options to purchase shares are granted to non-employees in return for goods or services, the fair value of the options granted is recognized as an expense, with a corresponding increase in contributed surplus, in the period in which the goods or services are received or are expected to be received. The consideration received on the exercise of share options is credited to share capital. When options are exercised, previously recorded compensation is transferred from contributed surplus to share capital to fully reflect the consideration for the shares issued.

m) Share purchase warrants

The Company's share purchase warrants ("warrants") are classified as equity. The warrants are initially measure using the Black-Scholes model, which is based on significant assumptions such as volatility, dividend yield and expected term.

n) Loss per share

Basic earnings per share ("EPS") is calculated by dividing the net loss for the year attributable to equity owners of the Company by the weighted average number of common shares outstanding during the period. Diluted EPS is calculated by adjusting the weighted average number of common shares outstanding for dilutive instruments. The Company's potentially dilutive instruments are comprised of stock options granted and warrants issued.

3. Summary of significant accounting policies *(continued from previous page)*

o) Financial instruments

Financial assets and liabilities are recognized when the Company becomes a party to the contractual provisions of the instrument. Financial assets are derecognized when the rights to receive cash flows from the assets have expired or have been transferred and the Company has transferred substantially all the risks and rewards of ownership.

Financial assets and liabilities are offset and the net amount reported in the statement of financial position when there is a legally enforceable right to offset the recognized amounts and there is an intention to settle on a net basis, or realize the asset and settle the liability simultaneously.

At initial recognition, the Company classifies its financial instruments in the following categories depending on the purpose for which the instrument were acquired.

Financial assets

i. Fair value through profit or loss

A financial asset can be classified as fair value through profit or loss only if it is designated at fair value through profit or loss or held-for-trading. The Company's financial assets at fair value through profit or loss are held for trading financial assets. The Company's cash is classified as fair value through profit or loss. Transaction costs related to the acquisition of financial assets that are classified as held for trading are expensed in net income as incurred

ii. Held-to-maturity

These assets are non-derivative financial assets with fixed or determinable payments and fixed maturities that the Company has the positive intention and ability to hold until maturity. These assets are measured at amortized cost using the effective interest method. If there is objective evidence that the investment is impaired, impairment losses are included in profit or loss. The Company does not have any financial assets in this category.

iii. Loans and receivables

These assets are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. These assets are measured at amortized cost using the effective interest method. Any gains or losses on the realization of receivables are included in profit or loss. The Company's accounts receivable are classified as loans and receivables.

Impairment of financial assets

All financial assets except for those at fair value through profit or loss are subject to review for impairment at each reporting date. Financial assets are impaired when there is any objective evidence that a financial asset or a group of financial assets are impaired. Impairment losses on financial assets carried at amortized cost are reversed in subsequent periods if the amount of the loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognized.

3. Summary of significant accounting policies *(continued from previous page)*

o) Financial instruments *(continued from previous page)*

Financial liabilities

i. Fair value through profit or loss

These liabilities are comprised of derivatives or liabilities acquired or incurred principally for the purpose of selling or repurchasing in the near term. They are measured at fair value with changes in fair value included in profit or loss. The Company does not have any financial liabilities in this category.

ii. Other financial liabilities

They are measured at amortized cost using the effective interest method. Any gains or losses in the realization of other financial liabilities are included in profit or loss. The Company's accounts payable and accrued liabilities, notes payable and debentures are classified as other financial liabilities.

p) Borrowing costs and discounts on issuance of new debt

Borrowing costs that are directly related to the issuance of new debt are recorded net of the associated debt and recognized into income using the effective interest rate method over the life of the debt. Discounts, where proceeds received are less than the par value of the debt, are recorded as a reduction to long-term debt. These discounts are being amortized using the effective interest method and included in borrowing costs.

q) Business combinations

Business combinations are accounted for using the acquisition method of accounting. The acquired net identifiable assets are measured at their fair value at the date of acquisition. Any excess of the purchase price over the fair value of the identifiable net assets acquired is recognized as goodwill. Any deficiency of the purchase price below the fair value of the identifiable net assets acquired is recognized as a gain in the consolidated statement of operations, loss and comprehensive loss. Associated transactions costs and costs incurred to identify and evaluate business acquisitions are expensed when incurred.

r) Business combinations under common control

Business combinations under common control are accounted for prospectively from the date the Company obtains the ownership interest using the predecessor values method, whereby, assets and liabilities are recognized upon consolidation at their carrying amount recorded in the books of the acquired company.

s) Related party transactions

Related party transaction amounts are recorded at the transaction amounts determined by contractual or other agreement between the parties; except for business combinations under common control which are accounted for as described above.

3. Summary of significant accounting policies *(continued from previous page)*

t) Significant accounting judgments and estimates

The preparation of the financial statements in accordance with IFRS requires management to make judgments, estimates and assumptions that affect reported amounts and presentation of assets, liabilities, revenues, expenses and disclosures of contingencies and commitments. Such estimates primarily relate to unsettled transactions and events at the statement of financial position date which are based on information available to management at each financial statement date. Actual results could differ from those estimated.

Judgments, estimates and assumptions are continuously evaluated and are based on management's experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

Reserves

Reserves and resources are used in the unit of production calculation for depletion and depreciation as well as impairment analysis. The quantity of reserves is subject to a number of estimates and projections including assessment of engineering data, projected future rates of production, commodity prices, regulatory changes, foreign exchange rates, operating costs and sustaining capital expenditures. These estimates and projections are uncertain as the Company does not have a long commercial production history to assist in the development of these forward-looking estimates. However, all reserve and associated financial information is evaluated and reported on by a firm of qualified independent reserve evaluators in accordance with the standards prescribed by applicable securities regulators.

The calculation of future cash flows based on these reserves is dependent on a number of estimates including: production volumes, facility performance, commodity prices, and royalties, operating costs, sustaining capital, foreign exchange and tax rates. The price used in our assessment of future cash flows is based on the Company's independent evaluator's estimate of future prices and evaluated for reasonability by the Company against other available information. The Company believes these prices are reasonable estimates for a long-term outlook.

Impairment

The Company assesses its P&E for possible impairment if there are events or changes in circumstances that indicate the carrying values of the assets may not be recoverable. Such indicators include changes in the Company's business plans, changes in commodity prices, evidence of physical damage and significant downward revisions to estimated recoverable volumes or increases in estimated future development expenditures.

The assessment for impairment for P&E assets involves comparing the carrying value of the CGU with the higher of value in use calculations and fair value less costs to sell. Determination as to whether and how much an asset is impaired involves management estimates on highly uncertain matters such as future commodity prices, the effects of inflation on operating expenses, discount rates, production profiles and the outlook for regional supply-and-demand conditions for crude oil. Impairment is recognized in earnings in the period in which carrying amount exceeded the recoverable amount.

Depletion and depreciation

Depletion of resource assets is measured over the life of proved and probable reserves on a unit-of-production basis and commences when the facilities are substantially complete and after commercial production has begun. Reserve estimates and the associated future capital can have a significant impact on earnings, as these are key components to the calculation of depletion. A downward revision in the reserve estimate or an upward revision to future capital would result in increased depletion, reduced earnings and reduced carrying value of petroleum and natural gas property assets.

3. Summary of significant accounting policies *(continued from previous page)*

t) Significant accounting judgments and estimates *(continued from previous page)*

Decommissioning liabilities

The Company measures decommissioning liabilities at each financial statement date. The estimate is based on the Company's share of costs to reclaim the resource assets and certain facilities as well as other resource assets associated with future expansions. To determine the future value of the liability, estimates of the amount, timing and inflation of the associated abandonment costs are made. The present value of the cost is recorded as decommissioning liability using a risk-free discount rate. Due to the long-term nature of current and future project developments, abandonment costs will be incurred many years in the future. As a result of these factors, different estimates could be used for such abandonment costs and the associated timing. Assumptions of higher future abandonment costs, regulatory changes, higher inflation, lower risk-free rates or an assumption of earlier or specified timing of abandonment would cause the decommissioning liability and corresponding asset to increase. These changes would also cause future accretion expenses to increase and future earnings to decrease.

Deferred taxes

Deferred tax assets and liabilities are recognized for the estimated future tax consequences attributable to differences between the financial statement carrying amount and the tax basis of assets and liabilities. An estimate is required for both the timing and corresponding tax rate for this reversal. Should these estimates change, it may impact the measurement of asset or liability as well as deferred tax recovery or expense recognized to earnings. The Company only recognizes deferred tax assets arising from unused tax losses to the extent that the Company has sufficient taxable temporary differences or it is probable that sufficient taxable profit will be available against which the unused tax losses can be utilized.

Contingencies

By their nature, contingencies will only be resolved when one or more of the future events occur or fail to occur. The assessment of contingencies inherently involves the exercise of significant judgment and estimates of the outcome of future events.

Share-based payments

The recognition of amounts in relation to share-based compensation requires estimates related to valuation of stock options at the time of issuance. By their nature, estimates are subject to measurement uncertainty and the effect of changes in such estimates on the financial statements for current and future periods could be significant.

3. Summary of significant accounting policies *(continued from previous page)*

u) Recent Accounting pronouncements:

On January 1, 2013, the Company adopted the following new standards and amendments which became effective for annual periods on or after January 1, 2013:

- IFRS 10, “Consolidated Financial Statements,” supersedes IAS 27 “Consolidated and Separate Financial Statements” and SIC-12 “Consolidation – Special Purpose Entities”. This standard provides a single model to be applied in control analysis for all investees including special purpose entities. The adoption of this standard had no impact on the amounts recorded in the Company’s financial statements.
- IFRS 11, “Joint Arrangements,” whereby joint arrangements are classified as either joint operations or joint ventures, each with their own accounting treatment. All joint arrangements are required to be reassessed on transition to IFRS 11 to determine their type to apply the appropriate accounting. The adoption of this standard had no impact on the amounts recorded in the Company’s financial statements.
- IFRS 12, “Disclosure of Interest in Other Entities,” combines the disclosure requirements for entities that have interest in subsidiaries, joint arrangements, and associates as well as unconsolidated structured entities. The adoption of this standard had no impact on the Company’s financial statements.
- IFRS 13, “Fair Value Measurement,” establishes a framework for measuring fair value and sets out disclosure requirements for fair value measurements. This standard defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The adoption of this standard had no impact on the Company’s financial statements except for the expanded disclosure on fair value measurement.
- IFRS 7, "Financial Instruments: Disclosures" was amended to develop common disclosure requirements for financial assets and financial liabilities that are offset in the financial statements, or that are subject to enforceable master netting arrangements or similar agreements. The adoption of this amendment had no impact on the Company’s financial statements.
- The Company has adopted the amendments to IAS 1, Presentation of Financial Statements, effective January 1, 2013. These amendments required the Company to group other comprehensive income items by those that will be reclassified subsequently to profit or loss and those that will not be reclassified. These changes did not result in any adjustments to net and other comprehensive income or loss.

3. Summary of significant accounting policies *(continued from previous page)*

v) Accounting standards issued but not yet applied

- In May 2013, the IASB issued amendments to IAS 36 "Impairment of Assets" which reduces the circumstances in which the recoverable amount of CGUs is required to be disclosed and clarify the disclosures required when an impairment loss has been recognized or reversed in the period. The amendments are required to be adopted retrospectively for fiscal years beginning January 1, 2014, with earlier adoption permitted. These amendments will be applied by the Company on January 1, 2014 and the adoption will only impact the Company's disclosures in the notes to the financial statements in periods when an impairment loss or impairment reversal is recognized.
- In May 2013, the IASB issued IFRIC 21 "Levies," which was developed by the IFRS Interpretations Committee ("IFRIC"). IFRIC 21 clarifies that an entity recognizes a liability for a levy when the activity that triggers payment, as identified by the relevant legislation, occurs. The interpretation also clarifies that no liability should be recognized before the specified minimum threshold to trigger that levy is reached. IFRIC 21 is required to be adopted retrospectively for fiscal years beginning January 1, 2014, with earlier adoption permitted. IFRIC 21 will be applied by the Company on January 1, 2014 and the adoption may have an impact on the Company's accounting for production and similar taxes, which do not meet the definition of an income tax in IAS 12 "Income Taxes." The Company is currently assessing and quantifying the effect on its financial statements.
- The IASB has undertaken a three-phase project to replace IAS 39 "Financial Instruments: Recognition and Measurement" with IFRS 9 "Financial Instruments." In November 2009, the IASB issued the first phase of IFRS 9, which details the classification and measurement requirements for financial assets. Requirements for financial liabilities were added to the standard in October 2010. The new standard replaces the current multiple classification and measurement models for financial assets and liabilities with a single model that has only two classification categories: amortized cost and fair value.
- In November 2013, the IASB issued the third phase of IFRS 9 which details the new general hedge accounting model. Hedge accounting remains optional and the new model is intended to allow reporters to better reflect risk management activities in the financial statements and provide more opportunities to apply hedge accounting. the Company does not employ hedge accounting for its risk management contracts currently in place. In July 2013, the IASB deferred the mandatory effective date of IFRS 9 and has left this date open pending the finalization of the impairment and classification and measurement requirements. IFRS 9 is still available for early adoption. The full impact of the standard on the Company's financial statements will not be known until the project is complete.

4. Accounts receivable

		2013		2012
Significant components of Accounts Receivable				
Accounts receivable - trade and joint venture	$	697,195	$	483,927
GST and HST Receivable		5,774		10,997
	$	**702,969**	**$**	**494,924**

The Company did not provide for any doubtful accounts at December 31, 2013 (2012 - $5,000). During the year, $12,533 (2012 - $7,041) of receivables was written off to general and administrative expenses in the Company's consolidated statements of operations, loss and comprehensive loss.

As at December 31, 2013, the Company had one individual receivable (2012 – two receivables) that accounted for more than 55% (2012 – 76%) of the outstanding accounts receivable balance totaling $389,725 (2012 - $273,402 and $52,961) from a joint venture partner. The Company is currently negotiating the assumption of the joint venture partner's working interest in the related assets (note 26).

As at December 31, 2013, the Company considers its receivables to be aged as follows:

	2013		2012
Not past due	119,117	$	334,435
Past due by less than 90 days	58,925		81,282
Past due by more than 90 days	524,927		79,207
Total	**702,969**	**$**	**494,924**

5. Exploration and evaluation assets

		2013		2012
Balance, beginning of year	$	-	$	-
Additions		-		93,750
Impairments		-		(93,750)
Balance, end of year	**$**	**-**	$	-

At December 31, 2012, the Company had determined that it will not develop the exploration and evaluation assets and has recorded impairment of the entire amount of $93,750.

6. Property and equipment

Oil and Natural Gas Interests

	2013	2012
Cost or deemed cost		
Balance, beginning of year	$ 7,233,932	$ 7,126,449
Additions	138,648	129,077
Decommissioning liability revision	362,851	(21,594)
Balance, end of year	$ 7,735,431	$ 7,233,932
Depletion, depreciation and impairment losses		
Balance, beginning of year	$ (5,502,246)	$ (4,528,276)
Addition	(983,120)	(973,970)
Balance, end of year	$ (6,485,366)	$ (5,502,246)
Net book amount	**$ 1,250,065**	$ 1,731,686

(i) The Company disposed an asset in the Kaybob area during the year ended December 31, 2012. The carrying value of the assets was $Nil and the assets were sold for a cash consideration of $83,000. The Company has recorded a gain on sale of property and equipment of $83,000, which has been disclosed in other income in the Company's Consolidated Statements of Operations, Loss and Comprehensive Loss for the year ended December 31, 2012.

(ii) There were no costs that were excluded from the depletion calculation for the year. Future development costs at December 31, 2013 and December 31, 2012 was $nil.

(iii) The Company recorded an impairment expense of $736,000 (2012 - $777,000), included in depletion expense, for the year. The recoverable amount of the CGU was based on the higher of the value in use and the fair value less costs to sell. The estimate of fair value less costs to sell (3%) was determined using a discount rate of 12% and forecasted cash flows, with escalating prices and future development costs, as obtained from an independent reserves engineer for the Company's proved plus probable reserves. The CGU's that were impaired are as follow:

	Impairment	Primary Product
Ronalane	$ 152,000	Oil
Kaybob	149,000	Gas
Retlaw	115,000	Gas
Carson Creek	100,000	Gas
Judy Creek	90,000	Gas
Gosfield	66,000	Oil
Brownsfield	34,000	Oil
Olds	28,000	Gas
Grand Forks	1,000	Gas
Westerose	1,000	Gas
	$ 736,000	

6. Property and equipment *(continued from previous page)*

(iv) The forecast prices used to estimate the fair value less cost to sell are those used by the independent reserves engineer as follows:

Year	Light crude oil – EDM. Oil Edmonton Light ($/bbl)	Natural gas – Alberta Plant Gate Spot ($/Mcf)
2014	95.00	4.00
2015	96.50	4.25
2016	97.50	4.55
2017	98.00	4.75
2018	98.30	5.00
2019	99.60	5.25
2020	101.60	5.35

7. Accounts payable and accrued liabilities

	2013	2012
Accounts payable - trade and joint venture	$ 896,221	$ 527,269
Interest payable *(notes 8 & 9)*	81,491	4,067
Accrued liabilities	45,500	53,500
	$ 1,023,212	$ 584,836

8. Notes payable

	2013	2012
Balance, beginning of year	$ -	$ -
Notes issued	300,000	-
Balance, end of year (ii)	**$ 300,000**	**$ -**
Accrued interest, end of year	**$ 14,783**	$ -

(i) The notes are payable on demand, are unsecured and bear an interest of 10%, compounded monthly. For the twelve months ended December 31, 2013, interest on the notes of $14,783 (2012 –$ nil) was recorded as financing costs in the consolidated statements of operation, loss and comprehensive loss.

(ii) At December 31, 2013, $100,000 of the notes payable is due to a related party *(note 20).*

9. Debentures

	2013	2012
Balance, beginning of year	$ 640,000	$ 640,000
Balance, end of year	$ **640,000**	$ 640,000
Accrued debenture interest, end of year	$ **66,708**	$ 4,067

(i) The debentures, which are not convertible, mature on January 31, 2015, and bear interest at a rate of 10% (2012 – 8%) per annum and payable quarterly. The debentures are secured by all present and future assets of the Company. During the year the Company executed a revised agreement for the maturity of the repayment of the debentures effective January 2013 to January 2015. As of December 31, 2013, the Company was in default of the requirement to pay interest quarterly. As a result, the debenture is payable on demand and has been recorded as a current liability.

(ii) For the year ended December 31, 2013, interest expense on the debenture of $64,000 (2012- $51,059) was recorded as financing costs in the consolidated statements of operations, loss and comprehensive loss.

(iii) At December 31, 2013, $370,000 of the debenture balance payable is due to related parties (note 20).

10. Decommissioning liabilities

The following table presents the reconciliation of the carrying amount of the obligation associated with the decommissioning of the Company's property and equipment:

	2013	2012
Decommissioning liabilities, beginning of year	$ 3,778,928	$ 3,798,277
Liabilities settled	(26,065)	(43,245)
Effect of change in estimates	362,851	(21,594)
Accretion (i)	57,475	45,490
Decommissioning liabilities, end of year	**$ 4,173,189**	**$ 3,778,928**

The following significant assumptions were used to estimate the decommissioning liabilities:

	2013	2012
Undiscounted cash flows	$ 4,515,318	4,055,860
Discount rate	1.62%	1.30%
Inflation rate	2.25%	2.50%
Weighted average expected timing of cash flows	4.92 years	4.65 years

(i) Accretion expense is included under financing costs in the Consolidated Statements of Operations, Loss and Comprehensive Loss.

(ii) Discount rate based on Government of Canada marketable bond yields for 3-5 year term.

(iii) Inflation rate based on Bank of Canada consumer price index.

11. Share capital

a) Authorized

Unlimited number of common shares, without nominal or par value

b) Issued and outstanding common shares

	2013		2012	
	Number	**Amount**	Number	Amount
Balance, beginning of year	30,259,707	$ 4,525,521	29,753,707	$ 4,367,233
Agent options exercised *(Note 12)*	-	-	506,000	112,000
Option value transferred to share capital from contributed surplus	-	-	-	46,288
Balance, end of year	**30,259,707**	**$ 4,525,521**	30,259,707	$ 4,525,521

c) Escrow

At December 31, 2013, the Company has 924,674 (2012 - 2,774,022) common shares subject to an escrow agreement. 924,650 shares will be released from escrow during March and September of each year until 2014.

12. Share-based compensation

The Company has a stock option plan under which the Board of Directors may grant options to directors, officers, other employees and key consultants. The Company may also grant options to agents.

Under the plan, the number of shares reserved for issuance pursuant to the exercise of all options under the plan may not exceed 10% of the issued and outstanding common shares at any time. The options expire not more than five years from the date of grant (except for 949,000 options issued during 2010, which expire after ten years from the date of grant), or earlier if the individual ceases to be associated with the Company, and vest over terms determined at the time of grant. The fair value of each option grant is estimated on the date of grant using the Black-Scholes option pricing model.

During the year ended December 31, 2013, the Company granted nil options (2012 - 1,400,000), to its directors, officers and consultants. The options granted in fiscal 2012 vested immediately upon grant and expire 5 years after grant date.

The share-based compensation expense at for the year ended December 31, 2013 is $nil (2012 - $163,175).

The following tables summarize information about directors, officers and consultants stock options outstanding as at, and for the year ended December 31:

	2013		2012	
	Options	**Weighted average exercise price**	Options	Weighted average exercise price
Opening	2,624,501	$ 0.18	2,819,000	$ 0.27
Granted	-	-	1,400,000	0.10
Forfeited	-	-	(1,594,499)	0.27
Closing	**2,624,501**	**$ 0.18**	2,624,501	$ 0.18

12. Share-based compensation *(continued from previous page)*

Range of exercisable price	Number outstanding	Weighted-average remaining contractual life (years)	Weighted-average exercise price	Number Exercisable
$ 0.10	1,400,000	3.79	$ 0.10	1,400,000
0.20	474,501	6.43	0.20	474,501
0.30	650,000	2.17	0.30	650,000
0.35	100,000	2.46	0.35	100,000
	2,624,501	3.82	$ 0.18	2,624,501

The following tables summarize information about agent stock options outstanding as at, and for the year ended December 31:

	2013		2012	
	Options	**Weighted average exercise price**	Options	Weighted average exercise price
Opening	1,011,885	$ 0.28	1,517,885	$ 0.28
Exercised	-	-	(506,000)	0.22
Expired	(1,011,885)	-	-	-
Closing	**-**	**$ 0.28**	1,011,885	$ 0.31

The Black-Scholes pricing model was used to estimate the fair value of options granted issued based on the following significant assumptions:

	2012
Weighted average fair value per option	$ 0.08
Risk-free interest rate	1.19%
Expected volatility	132%
Dividend yield	0%
Estimated forfeiture rate	0%
Expected life of each option granted	5 years

13. Warrants

The following table summarizes information about warrants outstanding as at, and for the year ended December 31:

	2013						2012				
	Number of warrants		**Weighted average exercise price**		**Fair value ascribed**		Number of warrants		Weighted average exercise price		Fair value ascribed
Opening	14,168,456	$	0.51	$	870,773		14,168,456	$	0.51	$	870,773
Expired	(14,168,456)		0.51		(870,773)		-		-		-
Closing	**-**	**$**	**-**	**$**	**-**		14,168,456	$	0.51	$	870,773

14. Petroleum and natural gas sales

		2013		2012
Petroleum and natural gas sales (gross)	$	1,062,417	$	1,364,886
Less: Royalty expense		(165,685)		(204,338)
Petroleum and natural gas sales (net)	**$**	**896,732**	$	1,160,548

The Company derived approximately 38% (2012 – 36%) of its revenue from its Ronalane property. The property is operated by the Company and the product is sold to exclusively to one marketer.

15. Other Income

		2013		2012
Gain on sale of property and equipment	$	-	$	83,000
Interest income		2,300		12,070
Total	**$**	**2,300**	**$**	**95,070**

16. Financing costs

		2013		2012
Interest expense on debentures	$	64,000	$	56,329
Interest on notes payable		14,783		-
Other interest charges		14,329		
Accretion on decommissioning liabilities		57,475		45,490
Total	**$**	**150,587**	**$**	**101,819**

17. Business investigation costs

Included in general and administrative expenses in the Consolidated Statements of Operations, Loss and Comprehensive Loss are business investigation costs as follows:

		2013		2012
To related parties (note 20)				
Consulting fee, to related parties	$	10,500	$	141,000
Legal and administrative fees paid to a law firm in which one director of the Company is counsel		-		85,925
To others:				
Consulting fee, others		-		79,863
Legal fees paid to unrelated law firms		-		65,543
Non-refundable deposit to Grisham Assets Corp.		-		100,440
Travel and other expenses		6,715		204,540
Total Business investigation costs	**$**	**17,215**	$	677,311

For the year ended December 31, 2012, these costs related to the acquisition of leases for offshore drilling in Namibia.

18. Net loss per share

Basic and diluted earnings per common share are calculated as follows:

		2013		2012
Net loss and comprehensive loss	$	(1,600,023)	$	(2,771,348)
Weighted average number of shares (basic)		30,259,707		30,099,756
Weighted average number of shares (diluted)		30,259,707		30,099,756
Loss per share:				
Basic	$	(0.05)	$	(0.09)
Diluted	$	(0.05)	$	(0.09)

19. Change in non-cash working capital

		2013		2012
Accounts receivable	$	(208,045)	$	70,428
Prepaid expenses and deposits		(22,617)		2,943
Accounts payable and accrued liabilities		438,376		(846,232)
Total	**$**	**207,714**	$	(772,861)
Allocated as follows:				
Operating	$	141,808	$	224,690
Investing		65,906		(997,551)
Total	**$**	**207,714**	$	(772,861)

20. Related party disclosures

		2013		2012
Key management personnel compensation:				
Administration and consulting fees	$	251,062	$	278,695
Stock options		-		124,551
(Key management personnel are comprised of the Company's directors and officers.)				
Other related party transactions:				
Legal and administrative fees charged by a law firm of which one director of the Company is council.		-		115,845
Interest expense on the Company's debentures and promissory notes, held by a director of the Company, and companies controlled by a director of the Company.	$	43,108	$	29,622

		2013		2012
Amount owing to / from related parties				
Accounts payable and accrued liabilities for administration and consulting fees, legal fees, and debenture interest.	$	108,456	$	62,169
Debenture – Principal outstanding.		370,000		370,000
Promissory note – Principal outstanding	$	100,000	$	-

21. Financial instruments and financial risk management

The Company's risk management policies are established by the Board of Directors to identify and analyze the risks faced by the Company, to set appropriate risk limits and controls, and to monitor risks and adherence to market conditions and the Company's policy.

The Company's financial instruments include cash and cash equivalents, accounts receivable, accounts payable and accrued liabilities, notes payable and debentures. The carrying values of accounts receivable, accounts payable and accrued liabilities and the fair value of notes payable approximate their fair values due to their relatively short periods to maturity. The fair value of debentures approximates its carrying value as it bear interest at a rate that is comparable to current rates offered to the Company for debt with similar terms.

The Company has exposure to credit risk, liquidity risk and market risk as a result of its use of financial instruments. This note presents information about the Company's exposure to each of the above risks and the Company's objectives, policies and processes for measuring and managing these risks. Further quantitative disclosures are included throughout these financial statements.

21. Financial instruments and financial risk management *(continued from previous page)*

a) Fair values

The Company is required to classify fair value measurements using a hierarchy that reflects the significance of the inputs used in making the measurements. The fair value hierarchy is as follows:

- Level 1 – quoted prices in active markets for identical assets or liabilities;
- Level 2 - inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly or indirectly; and
- Level 3 - inputs for the asset or liability that are not based on observable market data.

The fair value of cash is determined using level 1 inputs and the fair value of debentures is determined using level 2 inputs.

The fair value of the amounts due to related parties is less than carrying value, as the amounts are non-interest bearing. As the amounts have no terms of repayment, the fair value cannot be calculated with any degree of certainty, therefore the Company has classified these as Level 3 financial instruments.

b) Credit risk

Credit risk is the risk of an unexpected loss if a customer or third party to a financial instrument fails to meet its commercial obligations. This arises principally from joint venture partners and natural gas marketers.

Virtually all of the Company's accounts receivable are with companies in the petroleum and natural gas industry within Canada and are subject to normal industry credit risks. The Company generally extends unsecured credit to these companies and therefore, the collection of accounts receivable may be affected by changes in economic or other conditions. Management believes the risk is mitigated by the size and reputation of the companies to which they extend credit. The Company's maximum credit risk exposure is limited to the carrying value of its accounts receivable. However, the receivables are from participants in the oil and gas sector and collection of the outstanding balances is dependent on industry factors such as commodity price fluctuations, escalation costs and the risk of unsuccessful drilling.

As at December 31, 2013, the Company has approximately $390,000 due from a company that has filed for receivership subsequent to the year end. The Company has a lien on the assets of that company and management has determined that the full amount will be recovered.

The Company does not typically obtain collateral from petroleum and natural gas marketers or joint venture partners; however, the Company does have the ability to withhold production from joint venture partners in the event of non-payment.

21. Financial instruments and financial risk management *(continued from previous page)*

c) Liquidity risk

Liquidity risk is the risk that the Company will incur difficulties meeting its financial obligations as they are due. The Company's approach to managing liquidity is to ensure, as far as possible, that it will have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions without incurring unacceptable losses or risking harm to the Company's reputation.

The Company prepares annual capital expenditure budgets, which are regularly monitored and updated as considered necessary. The Company uses authorizations for expenditures on both operated and non-operated projects to further manage capital expenditures.

The Company anticipates it will continue operations in the foreseeable future and it will have adequate liquidity to fund its financial liabilities through its future cash flows. At December 31, 2013, the Company had a working capital deficiency of $1,066,047 (December, 2012 – $341,906).

The Company's financial liabilities are comprised of accounts payable and accrued liabilities, notes payable and debentures. The accounts payable and accrued liabilities and notes payable have expected maturities of less than one year resulting in their current classification on the consolidated statement of financial position. The full balance of the debentures matures in fiscal 2015.

d) Market risk

Market risk is the risk that changes in market factors, such as foreign exchange rates, commodity prices, and interest rates will affect the Company's cash flows, net income, liquidity or the value of financial instruments. The objective of market risk management is to mitigate market risk exposures where considered appropriate and maximize returns.

i. Interest rate risk
Interest rate risk is the risk that future cash flows will fluctuate as a result of changes in market interest rates. The Company is exposed to interest rate risk on its cash and cash equivalents. The Company had no interest rate swap or financial contracts in place at December 31, 2013 or 2012. For the year ended December 31, 2013 or 2012, an increase or decrease of interest rates by one percent would not have materially affected the financial results of the Company.

ii. Currency risk
Foreign currency exchange rate risk is the risk that the fair value or future cash flows will fluctuate as a result of changes in foreign exchange rates. All of the Company's petroleum and natural gas sales are denominated in Canadian dollars; however, the underlying market prices in Canada for petroleum and natural gas are impacted by changes in the exchange rate between the Canadian and United States dollar. The Company had no outstanding forward exchange rate contracts in place at December 31, 2013 or 2012.

iii. Commodity price risk
Commodity price risk is the risk that the fair value or future cash flows will fluctuate as a result of changes in commodity prices. Commodity prices for petroleum and natural gas are impacted by world economic events that dictate the levels of supply and demand as well as the relationship between the Canadian and United States dollar, as outlined above. Significant changes in commodity prices may materially impact the Company's financial results.

If production remained constant and the Company is realized prices changed by $1.00 per barrel of oil equivalent, the Company's net loss would vary by approximately $21,000 during the year ended December 31, 2013.

22. Capital Management

The Company's objective when managing capital is to maintain a flexible capital structure which will allow it to execute its capital expenditure program, which includes expenditures in oil and gas activities which may or may not be successful. Therefore, the Company monitors the level of risk incurred in its capital expenditures to balance the proportion of debt and equity in its capital structure.

The Company considers its capital structure to include shareholders equity and debentures.

The Company monitors capital based on annual funds from operations and capital expenditure budgets, which are updated as necessary and are reviewed and periodically approved by the Company's Board of Directors. In order to maintain or adjust the capital structure, from time to time the Company may issue common shares, debt or other securities, sell assets or adjust capital spending to manage current and projected debt levels.

At December 31, 2013, the Company's capital structure was not subject to external restrictions.

The Company anticipates it will continue operations in the foreseeable future and it will have adequate liquidity to fund its financial liabilities through its future cash flows.

23. Income taxes

i. Deferred tax recovery

The provision for income tax reflects an effective income tax rate which differs from federal and provincial statutory income tax rates. The main differences are as follows:

	2013	2012
Loss before income taxes	$ (1,600,023)	$ (2,771,348)
Statutory tax rate	25.0%	25.0%
Expected income tax recovery	(400,006)	(692,837)
Increase (decrease) in taxes resulting from:		
Stock-based compensation	-	40,794
Change in tax pool estimates	(4,790)	396,038
Change in tax benefits not recognized	404,796	256,005
Deferred tax (recovery)	**$ -**	**$ -**

23. Income Taxes *(continued from previous page)*

ii. Components of the net deferred tax asset (liability)

Temporary differences that give rise to the net deferred tax asset as of December 31, 2013 and 2012 are as follows:

	2013	2012
Non-capital losses	$ 1,717,715	$ 1,537,576
Decommissioning liability	1,043,297	944,732
Property, plant and equipment	174,635	14,777
Share issue costs	59,453	93,219
Total gross deferred tax assets	2,995,100	2,590,304
Tax benefits not recognized	(2,995,100)	(2,590,304)
Net deferred tax assets	**$ -**	$ -

The tax benefits not recognized offsets the net deferred tax assets for which there is no assurance of recovery. The tax benefits not recognized is evaluated considering positive and negative evidence about whether the deferred tax assets will be realized. At the time of evaluation, the tax benefits not recognized is either increased or reduced. Reduction could result in the complete elimination of the tax benefits not recognized, if positive evidence indicated that the value of the deferred tax assets is no longer impaired and the tax benefits not recognized is no longer required.

iii. Tax pools

As at December 31, 2013, the Company has available for deduction against future taxable income, the following approximate amounts:

	2013
Operating loss carry forwards	$ 6,871,000
Share issue costs	$ 227,000
Canadian exploration expenditures	$ 891,000
Canadian development expenditures	$ 57,000
Canadian oil and gas property expenditures - regular	$ 532,000
Capital cost allowances	$ 469,000

The availability of deduction of the operating loss carry forwards against future taxable income expires as follows:

Year expire:	
2026	$ 173,000
2027	1,019,000
2028	802,000
2039	794,000
2030	377,000
2031	1,018,000
2032	1,967,000
2033	721,000
Total	$ 6,871,000

24. Letters of Credit

	2013	2012
Letter of Credit issued to Saskatchewan Ministry of Energy and Resources under the Saskatchewan License Liability Rating (LLR) Program	$ 74,743	$ 74,045

25. Contingency

A former director of the Company has made a claim for payment of amounts alleged to be owed to him (or a company controlled by him) under a consulting agreement. The claimant commenced an action in the Alberta Court of Queen's Bench on September 27, 2012, seeking judgment against the Company for the principal amount of $54,000, plus unspecified amounts for interest, taxes and costs. The Company denies that there is any amount owing to the claimant, and believes that the claimant was overpaid for services provided under the consulting agreement by an amount of $12,600, improperly invoiced by the claimant. The Company has filed a Statement of Defense and Counterclaim in the action, and intends to vigorously defend the claim.

26. Subsequent Events

Sedna Oil and Gas Ltd. (“Sedna”) is a 50% working interest partner in certain wells located at Ronalane and Retlaw and a 40% working interest in a facility. Sedna has an account in arrears with the Company in the amount of approximately $390,000 as at December 31, 2013. On February 19, 2014, Sedna was placed into receivership and on April 22, 2014 the Company tendered a bid to the receiver for the acquisition of Sedna’s working interest in the Ronalane and Retlaw assets. A refundable deposit of $150,000 representing the amount of the offer was submitted. In recording the purchase of these assets, the Company will be applying the net amount owing from Sedna to the cost of the properties resulting in value of the properties consistent with the present cash value of the assets as disclosed in the Company’s reserve report. The application has been submitted to the Court of Queen’s Bench of Alberta.

On February 24, 2014 a judgment was issued by the Civil Division of the Provincial Court of Alberta to the Company in respect of certain amounts in arrears owing to a vendor in the amount of $17,570. As of the date of the audit report, the judgment has not been satisfied. The Company is making arrangements to have this outstanding amount settled. The amount is included in accounts payable and accrued liabilities on the statement of financial position for the year-ended December 31, 2013.