PetroShale

Calgary • Denver

Consolidated Financial Statements

As at December 31, 2017
and for the years ended December 31, 2017 and 2016

CONSOLIDATED STATEMENTS OF FINANCIAL POSITION

As at (thousands of Canadian dollars)	NOTE	December 31, 2017	December 31, 2016
ASSETS			
Current assets			
Cash and cash equivalents		$ 18,421	$ 1,134
Accounts receivable		10,178	4,662
Prepaid expenses and deposits		384	268
		28,983	6,064
Non-current assets			
Restricted cash	14	94	101
Property, plant and equipment	6, 7	184,172	139,866
		184,266	139,967
		$213,249	$146,031
LIABILITIES			
Current liabilities			
Accounts payable and accrued liabilities		$ 38,447	$ 29,573
Financial derivative liability	10	3,149	61
Senior loan		-	30,209
Subordinated loan		-	94,372
		41,596	154,215
Non-current liabilities			
Senior loan	9	49,891	-
Subordinated loan	9, 15, 20	30,640	-
Decommissioning obligation	8	2,473	1,218
		83,004	1,218
Total liabilities		124,600	155,433
SHAREHOLDERS' EQUITY (DEFICIT)			
Share capital	11	142,379	35,658
Warrants	9, 11, 15	684	684
Contributed surplus		3,547	3,597
Deficit		(55,069)	(51,976)
Accumulated other comprehensive income (loss)		(2,892)	2,635
		88,649	(9,402)
Commitments	14		
Subsequent events	20		
		$213,249	$146,031

See accompanying notes to the consolidated financial statements.

Approved by Board of Directors

(Signed) "Brett Herman" — Director

(Signed) "M. Bruce Chernoff" — Executive Chairman

PetroShale
Calgary • Denver

CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE LOSS

(thousands of Canadian dollars, except per share amounts)	NOTE	Years ended December 31, 2017	2016
Revenue			
Oil and natural gas		$ 43,973	$ 23,246
Royalties		(9,092)	(4,769)
		34,881	18,477
Unrealized loss on financial derivatives	5, 10	(3,127)	(61)
		31,754	18,416
Expenses			
Production and operating		10,374	6,460
General and administrative	7	3,342	2,532
Depletion and depreciation	7	12,631	8,923
Finance	9, 15	8,137	13,660
Foreign exchange gain		(71)	(520)
Share-based compensation	11	434	223
		34,847	31,278
Net loss for the year		(3,093)	(12,862)
Currency translation adjustment		(5,527)	(1,493)
Comprehensive loss for the year		$ (8,620)	$(14,355)
Net loss per share, basic and diluted	12	**$ (0.03)**	**$ (0.38)**

See accompanying notes to the consolidated financial statements.

CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY
For the years ended December 31, 2017 and 2016
(thousands of Canadian dollars, except share amounts)

	Non-Voting Common Shares		Voting Common Shares					Accumulated Other Comprehensive Income (Loss)	
	Shares	Amount	Shares	Amount	Warrants	Contributed Surplus	Deficit		Shareholders' Equity (Deficit)
Balances, December 31, 2015	6,700,000	$ -	27,507,574	$ 35,658	$ -	$ 3,344	$ (39,114)	$ 4,128	$ 4,016
Issuance of warrants	-	-	-	-	684	-	-	-	684
Share-based compensation, gross	-	-	-	-	-	253	-	-	253
Net loss	-	-	-	-	-	-	(12,862)	-	(12,862)
Other comprehensive loss	-	-	-	-	-	-	-	(1,493)	(1,493)
Balances, December 31, 2016	6,700,000	$ -	27,507,574	$ 35,658	$ 684	$ 3,597	$ (51,976)	$ 2,635	$ (9,402)
Issuance of voting common shares for cash, net	-	-	122,649,615	106,135	-	-	-	-	106,135
Conversion of non-voting common shares to voting common shares	(6,700,000)	-	6,700,000	-	-	-	-	-	-
Exercise of options to purchase voting common shares for cash	-	-	280,578	586	-	(390)	-	-	196
Settlement of share options	-	-	-	-	-	(39)	-	-	(39)
Share-based compensation, gross	-	-	-	-	-	379	-	-	379
Net loss	-	-	-	-	-	-	(3,093)	-	(3,093)
Other comprehensive loss	-	-	-	-	-	-	-	(5,527)	(5,527)
Balances, December 31, 2017	-	$ -	157,137,767	$ 142,379	$ 684	$ 3,547	$ (55,069)	$ (2,892)	$ 88,649

See accompanying notes to the consolidated financial statements.

PetroShale
Calgary • Denver

CONSOLIDATED STATEMENTS OF CASH FLOWS

(thousands of Canadian dollars)	NOTE	Years ended December 31, 2017	2016
			(note 2)
Operating Activities			
Net loss		$ (3,093)	$ (12,862)
Operating items not affecting cash:			
Depletion and depreciation		12,631	8,923
Unrealized loss on financial derivatives		3,127	61
Share-based compensation		333	223
Finance expense		8,137	13,660
Decommissioning expenditures		-	(14)
Change in non-cash working capital	18	(1,865)	(775)
		19,270	9,216
Investing Activities			
Acquisition of property, plant and equipment	6	(15,457)	(8,382)
Additions to property, plant and equipment	7	(50,260)	(20,579)
Proceeds from disposition of property, plant and equipment		-	648
Change in non-cash working capital	18	23,984	(1,545)
		(41,733)	(29,858)
Financing Activities			
Proceeds from share issuances, net	11	106,135	-
Proceeds from exercise of options	11	196	-
(Repayment of) proceeds from subordinated loan, net	9, 15	(61,142)	21,839
Proceeds from (repayment of) senior loan, net	9	20,831	(121)
Payment of interest		(3,726)	(1,501)
Payment of previously deferred interest	18	(22,330)	-
Change in non-cash working capital	18	-	644
		39,964	20,861
Change in cash and cash equivalents		17,501	219
Effect of foreign exchange rate changes		(214)	93
Cash and cash equivalents, beginning of period		1,134	822
Cash and cash equivalents, end of period		$ 18,421	$ 1,134

See accompanying notes to the consolidated financial statements.

1. BUSINESS AND NATURE OF OPERATIONS

PetroShale Inc. (the "Company") is an oil company engaged in the acquisition, development and consolidation of interests in the North Dakota Bakken/Three Forks.

The Company's head office is located at Suite 3230, 421 - 7th Avenue SW, Calgary, Alberta.

2. BASIS OF PREPARATION

These consolidated financial statements have been prepared by management in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB") and were authorized for issue by the Board of Directors on April 19, 2018.

These financial statements have been prepared using the historical cost basis, except for financial derivative instruments which are measured at fair value.

These consolidated financial statements include the accounts of the Company and its wholly-owned subsidiary, PetroShale (US), Inc.

The Company's presentation and functional currency is the Canadian dollar. The functional currency of the Company's US subsidiary is the US dollar, and its results and balance sheet items are translated to Canadian dollars for purposes of these consolidated financial statements, in accordance with the Company's foreign currency translation accounting policy.

Effective as at June 30, 2017, the Company voluntarily changed its accounting policy in relation to classification of finance expense in its statements of cash flows. The Company now presents interest paid as a financing activity, instead of as an operating activity. The Company believes that the revised presentation better reflects the results of its operating activities, excluding the impact of how these activities were financed, and more properly reflects interest associated with the senior and subordinated loans as a financing activity. The Company has restated the consolidated statement of cash flows for the corresponding period in 2016 to reflect this change. There is no impact to the Company's statements of financial position or statements of operations.

For the year ended December 31, 2017, the change in accounting policy had the following impact on the consolidated statement of cash flows:

	Under previous accounting policy	Effect of change of accounting policy	As currently reported
Operating Activities:			
Net Loss	$ (3,093)	$ -	$ (3,093)
Operating items not affecting cash:			
Depletion and depreciation	12,631	-	12,631
Accretion of decommissioning obligation	5	(5)	-
Amortization of deferred finance costs	733	(733)	-
Unrealized loss on financial derivatives	3,127	-	3,127
Share-based compensation	333	-	333
Deferred finance expense	3,673	(3,673)	-
Finance expense	-	8,137	8,137
Change in non-cash working capital	(24,195)	22,330	(1,865)
	$ (6,786)	$ 26,056	$ 19,270
Financing Activities:			
Proceeds from share issuances, net	$ 106,135	$ -	$ 106,135
Proceeds from exercise of options	196	-	196
Repayment of subordinated loan, net	(61,142)	-	(61,142)
Proceeds from senior loan, net	20,831	-	20,831
Payment of interest	-	(3,726)	(3,726)
Payment of previously deferred interest	-	(22,330)	(22,330)
	$ 66,020	$ (26,056)	$ 39,964

For the year ended December 31, 2016, the change in accounting policy had the following impact on the consolidated statement of cash flows:

	As previously reported	Effect of change of accounting policy	As currently reported
Operating Activities:			
Net Loss	$ (12,862)	$ -	$ (12,862)
Operating items not affecting cash:			
Depletion and depreciation	8,923	-	8,923
Accretion of decommissioning obligation	8	(8)	-
Amortization of deferred finance costs	722	(722)	-
Unrealized loss on financial derivatives	61	-	61
Share-based compensation	223	-	223
Deferred finance expense	11,429	(11,429)	-
Finance expense	-	13,660	13,660
Decommissioning expenditures	(14)	-	(14)
Change in non-cash working capital	(131)	(644)	(775)
	$ 8,359	$ 857	$ 9,216
Financing Activities:			
Proceeds from subordinated loan, net	$ 21,839	$ -	$ 21,839
Repayment of senior loan, net	(121)	-	(121)
Payment of interest	-	(1,501)	(1,501)
Change in non-cash working capital	-	644	644
	$ 21,718	$ (857)	$ 20,861

Critical judgments in applying accounting policies

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

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

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

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

Key sources of estimation uncertainty

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

Estimation of recoverable quantities of proven and probable oil and natural gas reserves include estimates and assumptions regarding future commodity prices, currency exchange rates, discount rates and production and transportation costs for future cash flows as well as the interpretation of complex geological and geophysical models and data. Changes in reported reserves can affect the impairment of assets, the estimation of decommissioning obligations, the economic feasibility of exploration and evaluation assets and the amounts reported for depletion and depreciation of property, plant and equipment. These reserve estimates are verified by third party professional engineers, who work with information provided by the Company to establish reserve determinations in accordance with National Instrument 51-101.

The Company estimates the decommissioning obligations for oil and natural gas wells and their associated production facilities and pipelines. In most instances, removal of assets and remediation occurs many years into the future. Amounts recorded for the decommissioning obligations and related accretion expense require assumptions regarding removal date, future environmental legislation, the extent of reclamation activities required, the engineering methodology for estimating cost, inflation estimates, future removal technologies, and the estimate of the liability specific discount rates to determine the present value of these cash flows.

In a business combination, management makes estimates of the fair value of assets acquired and liabilities assumed which includes assessing the value of oil and natural gas properties based upon the estimation of recoverable quantities of proven and probable reserves being acquired as well as estimating the associated decommissioning obligation.

The Company's estimate of share-based compensation expense associated with stock option grants and the value of warrants issued is dependent upon estimates of expected volatility of the Company's share price and anticipated forfeiture rates of the related securities. The Company's estimate of share-based compensation expense associated with share based awards is dependent on an estimate of anticipated forfeiture rates of such securities.

The Company's deferred tax asset or liability is based on estimates as to the timing of the reversal of temporary differences, substantively enacted tax rates and the likelihood of deferred tax assets being realized.

The Company's estimate of the fair value of derivative financial instruments is dependent on estimated forward prices and volatility in those prices.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accounting policies set out below have been applied consistently to the periods presented in the financial statements, except as described in Note 2 as it relates to the presentation of finance expense in the statements of cash flows.

a) Business Combinations and Consolidation

i) Subsidiaries and business acquisitions

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 consolidated financial statements from the date that control commences until the date that control ceases.

The purchase method of accounting is used to account for acquisitions of subsidiaries and assets that meet the definition of a business under IFRS. The cost of an acquisition is measured as the fair value of assets given, equity instruments issued and liabilities incurred or assumed at the date of exchange. Identifiable assets acquired and liabilities assumed in a business combination are measured initially at their fair values at the acquisition date. The excess of the cost of an acquisition over the fair value of the identifiable assets acquired net of liabilities assumed is recorded as goodwill. If the cost of an acquisition is less than the fair value of the net assets of the subsidiary acquired, the difference is recognized in the statement of operations and comprehensive income.

ii) Jointly controlled operations and jointly controlled assets

The Company's oil and natural gas activities involve jointly controlled assets. The financial statements include the Company's share of these jointly controlled assets and a proportionate share of the relevant revenue and related costs.

iii) Transactions eliminated on consolidation

All intercompany balances and transactions have been eliminated upon consolidation.

b) Revenue Recognition (see Note 4)

Revenues associated with the production and sale of petroleum products owned by the Company are recognized when the significant risks and rewards of ownership are transferred to the buyer, which is typically when the production enters a third party pipeline or loading facility, and provided the amount to be received can be reasonably estimated and collection is reasonably assured.

Royalty payments received from projects in which the Company has an interest are recorded when received or receivable if the amount to be received can be reasonably estimated and collection is reasonably assured.

c) Foreign Currency Translation

The Company's consolidated financial statements are reported in Canadian dollars, which is the Company's presentation currency. Transactions of the Company's US subsidiary are recorded in US

dollars, as this is the primary economic environment in which this subsidiary operates. The US subsidiary has a US dollar functional currency. In translating the financial results from US dollars to Canadian dollars, the Company uses the following method: assets and liabilities are translated at the exchange rate in effect as at the date of the consolidated statement of financial position; revenues and expenses are translated at the rate effective at the time of the transaction or the average rate for the period; and changes in shareholders' equity are translated at the rate effective at the time of the transaction. Unrealized gains and losses resulting from the translation to the Canadian dollar presentation currency are included in other comprehensive income.

Transactions of the US subsidiary that are denominated in a currency other than the US dollar are translated to the US dollar using the following method: monetary assets and liabilities are translated at the exchange rate in effect at the date of the consolidated statement of financial position; non-monetary assets and liabilities are translated at the exchange rate on the date such assets or liabilities are assumed; and revenues and expenses are translated at the average rate for the period. Realized gains and losses resulting therefrom are reflected in the statements of operations as foreign exchange gain or loss.

d) Property, Plant and Equipment

There are two categories of Property, Plant and Equipment ("PP&E"): Developed and Producing ("D&P") assets and Other PP&E assets.

D&P assets include capital costs (i) related to drilling projects where the drilling location is already determined to hold proven and/or probable reserves, (ii) incurred to improve an already technically feasible and commercially viable well, and (iii) related to facilities and equipment projects.

Other PP&E assets typically include furniture, fixtures, leasehold improvements and office equipment.

For statement of financial position presentation, both D&P assets and Other PP&E assets are included in the PP&E category.

i) Recognition and measurement

PP&E is measured at cost less accumulated depletion and depreciation and accumulated impairment losses. For purposes of determining depletion and depreciation expense, when significant parts of PP&E have different useful lives, they are accounted for separately so that depletion and depreciation rates appropriately reflect useful lives.

Gains and losses on disposal of PP&E, property swaps and farm-outs, are determined by comparing the proceeds from disposal with the carrying amount of the PP&E sold, and are recognized on a net basis in profit or loss.

The net carrying value of D&P assets is depleted using the unit-of-production method by calculating the ratio of production in the period to the related proven and probable reserves. Proven and probable reserves are expressed on a barrels of oil equivalent ("Boe") basis where natural gas volumes are converted to Boe using a ratio of 6,000 cubic feet of natural gas to one barrel of oil. The net carrying value to be depleted includes an estimate of future development costs required to bring any related non-producing or undeveloped reserves into production, which may include the costs of drilling and completing wells. These estimates are reviewed at least annually by independent engineers in conjunction with their review of the Company's proven and probable reserves.

For Other PP&E assets, depreciation is recognized in the statement of operations and comprehensive income on a straight-line basis over their estimated useful lives. Finance lease assets are depreciated over the shorter of the lease term and their useful lives unless it is reasonably certain that the Company will obtain ownership by the end of the lease term. Depreciation methods, useful lives and residual values are reviewed at each reporting date.

ii) Impairment

An assessment is made at each reporting period as to whether there are any facts or circumstances which suggest there may be an impairment of D&P assets. If such facts and circumstances exist, the Company would compare the carrying amount of D&P assets to their recoverable amount, on a CGU by CGU basis. The recoverable amount of a CGU is the greater of: (i) its value in use; and (ii) its fair value less selling costs. In assessing value in use for D&P assets, the estimated future cash flows from the production of proven and probable reserves are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. Impairment losses recognized in prior periods are assessed at each reporting date to evaluate if those losses have decreased or no longer exist. If those impairment losses have decreased or no longer exist (recovered), they are reversed accordingly. Previously recognized impairment losses may be recovered in future reporting periods due to changes in estimates used to determine the recoverable amount. An impairment loss recovery is recorded only to the extent that the D&P asset carrying amount does not exceed the carrying amount that would have been determined, net of depletion and depreciation expense, if no impairment loss had been recognized. Impairment losses and recoveries are recorded in the statement of operations and comprehensive income.

iii) Subsequent costs

Costs incurred subsequent to the drilling and completion of a well, or the commissioning of production or transportation facilities, and the costs of replacing parts of property, plant and equipment are recognized as D&P assets only when they increase the future economic benefits embodied in the specific asset to which they relate. All other expenditures are recognized in profit or loss as incurred. Such capitalized costs generally represent costs incurred in developing proven and/or probable reserves and bringing on or enhancing production from such reserves, and are accumulated on a field or geotechnical area basis. The carrying amount of any replaced or sold component is derecognized. The costs of the day to day servicing of property, plant and equipment are recognized in profit or loss as incurred.

e) Decommissioning Obligation

An obligation is recognized if, as a result of a past event, the Company has a future legal or constructive obligation resulting from the retirement and reclamation of tangible long-lived assets and this obligation can be reliably estimated. The obligation is measured at the present value of management's best estimate of the expected expenditures required to settle this obligation and is recorded in the period the related assets are put into use with a corresponding increase to the carrying amount of the related assets. This increase in capitalized costs is depleted and depreciated on a basis consistent with the underlying assets. Subsequent changes in the estimated fair value of the provision are capitalized and depleted over the remaining useful life of the underlying asset.

The obligation is carried in the statement of financial position at its discounted present value and is accreted over time for the change in its present value. The obligation is discounted at a rate that reflects

a current market assessment of the time value of money and the risks specific to the obligation. Accretion of the obligation is included in finance expense in the statement of operations.

f) Income Taxes

Current income taxes are measured at the amount expected to be payable on taxable income for the period, using tax rates enacted or substantively enacted at the end of the reporting period.

The Company follows the asset and liability method of accounting for deferred income taxes. Under this method, deferred income taxes are recognized based on the expected future tax consequences of differences between the carrying amount of statement of financial position items and their corresponding tax basis, using the enacted and substantively enacted income tax rates for the years in which the differences are expected to reverse.

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

g) Share-based Payments

The Company uses the fair value method to recognize the cost associated with stock options granted to employees, directors and other service providers. The fair value of the stock options granted is measured using the Black-Scholes option pricing model. A forfeiture rate is estimated on the grant date and is adjusted to reflect the actual number of options that vest. Under the fair value method, the Company recognizes estimated compensation expense related to stock options over the vesting period of the options granted, with the related credit being charged to contributed surplus. Fair value is measured at the grant date and each tranche is recognized using the graded vesting method over the period during which the options vest. At each reporting date, the amount recognized as an expense is adjusted to reflect the actual number of share options that are expected to vest. Upon exercise of any stock options, amounts previously credited to contributed surplus are reversed and credited to share capital.

Share-based awards to employees, directors and other service providers are measured at the market share price as at the date of grant. A forfeiture rate is estimated on the grant date and the related compensation expense is recognized over the vesting period of the share-based awards, using the graded vesting method, with the related credit being charged to contributed surplus.

h) Earnings per Share

Basic earnings per common share are calculated by dividing the net earnings for the period by the weighted average number of common shares outstanding in each respective period. Diluted earnings per common share reflect the maximum possible dilution from other securities, if dilutive.

i) Financial Instruments

i) Non-derivative financial instruments

These comprise cash and cash equivalents including bank overdrafts, accounts receivable, accounts payable and loans and borrowings. Non-derivative financial instruments are recognized initially at

fair value plus any directly attributable transaction costs. Subsequent to initial recognition, non-derivative financial instruments are measured as described below.

a. Cash and cash equivalents in the statement of financial position comprise cash at banks and on hand and short term deposits with an original maturity of three months or less.

   For the purpose of the statement of cash flows, cash and cash equivalents consist of cash and cash equivalents defined above, net of outstanding bank overdrafts. These balances are reflected at cost.

b. Other non-derivative financial instruments, such as loans and borrowings, accounts receivable and accounts payable, are measured at amortized cost using the effective interest method, less any impairment losses.

ii) Derivative financial instruments

The Company may enter into certain financial derivative contracts in order to manage its exposure to market risks from fluctuations in commodity prices, interest rates and foreign exchange rates. These instruments are not used for trading or speculative purposes. The Company will not designate its financial derivative contracts as effective accounting hedges, and thus will not apply hedge accounting, even though the Company considers all commodities contracts to be economic hedges. As a result, all financial derivative contracts will be classified as fair value through profit and loss and recorded in the statement of financial position at fair value. Related transaction costs such as trading commissions will be recognized in the statement of operations and comprehensive income (loss) when incurred.

Forward physical delivery and sales contracts of oil and natural gas products are entered into under the normal course of business and therefore not recorded at fair value in the statement of financial position. These physical delivery contracts are not considered to be derivative financial instruments or hedges. Settlements on these physical delivery contracts are recognized in oil and natural gas revenue in the statement of operations and comprehensive income (loss). Unrealized gains and losses are recorded based on the changes in the fair values of the derivative instruments. Both the unrealized and realized gains and losses resulting from the contract settlement of derivatives are recorded in the statement of operations.

j) Share Capital

Common shares are classified as equity. Incremental costs directly attributable to the issue of common shares, warrants and stock options are recognized as a reduction from equity, net of any tax effects.

k) Warrants

Common share purchase warrants are recorded at fair value when issued. The warrant amount is based on the fair value as at the grant date as estimated using the Black-Scholes model. There are various assumptions used in calculating the value of the warrants such as the expected share price volatility and the expected warrant life. If the warrants are exercised, the cash proceeds from issuance of the related common shares and the original warrant amount are recorded as share capital in the consolidated statement of financial position. The value of warrants issued in connection with a debt financing is amortized to finance expense over the term of the related debt obligation.

l) Capitalized Overhead

The Company capitalizes to D&P assets certain directly attributable general and administrative costs, including share-based compensation, associated with employees and consultants involved in acquiring licenses or other approvals and drilling, completion and construction activities on the Company's operated lands.

4. FUTURE ACCOUNTING PRONOUNCEMENTS

Certain new accounting standards, interpretations and amendments to existing standards, with future effect, have been issued by the IASB or the International Financial Reporting Interpretation Committee ("IFRIC"). The standards that are applicable to the Company are as follows:

IFRS 9 - "Financial Instruments" is the result of the first phase of the IASB's project to replace IAS 39 - "Financial Instruments: Recognition and Measurement". 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. The standard will come into effect on January 1, 2018 with early adoption permitted. The extent of the impact of the adoption of IFRS 9 is not expected to be material.

IFRS 15 – "Revenue from Contracts with Customers" was issued in May 2014 to replace IAS 11 – "Construction Contracts" and IAS 18 – "Revenue" and related interpretive guidance. IFRS 15 provides a single, principles based model to be applied to all contracts with customers as well as new disclosure requirements with the objective of a more structured approach, improving comparability across entities and industries. Under IFRS 15, an entity will recognize revenue at the amount to which it expects to be entitled in exchange for goods or services on their transfer. IFRS 15 is effective for annual periods beginning on or after January 1, 2018 and will be applied retrospectively. The Company has determined that the adoption of IFRS 15 is not expected to have a material impact on net income (loss). However, the adoption of this new standard is expected to result in enhanced disclosures related to the Company's revenue.

IFRS 16 – "Leases" is a new standard which introduces a single lessee accounting model with required recognition of assets and liabilities for most leases. It is effective for annual periods beginning on or after January 1, 2019 with earlier adoption permitted, and is to be applied retrospectively. The extent of the impact of adoption of this new standard on the Company has not been fully assessed at this time.

5. FAIR VALUE HIERARCHY

Several of the Company's accounting policies require a determination of fair value for certain assets and liabilities. Fair value for measurement or disclosure purposes is determined on the following basis.

Fair value is defined 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. Valuation techniques include the market, income and cost approach. The market approach uses information generated by market transactions involving identical or comparable assets or liabilities; the income approach converts estimated future amounts to a present value; and the cost approach is based on the amount that currently would be required to replace an asset.

The Company is required to classify its financial instruments within a hierarchy that prioritizes the inputs to fair market value. The three levels of the fair value hierarchy are:

Level 1 – Unadjusted quoted prices in an active market for identical assets or liabilities;

Level 2 – Inputs other than quoted prices that are observable for the asset or liability either directly or indirectly; and,

Level 3 – Inputs that are not based on observable market data.

a) Property, plant and equipment

The fair value of property, plant and equipment recognized in a business combination is based on market value. The market value of PP&E is the estimated amount for which PP&E could be exchanged on the acquisition date between a willing buyer and a willing seller in an arm's length transaction after proper marketing wherein the parties had each acted with knowledge and prudence and without compulsion. The market value of oil and natural gas interests included in PP&E is estimated with reference to the discounted future cash flows expected to be derived from oil and natural gas production based on internally and externally prepared reserve reports. The risk-adjusted discount rate is specific to the asset with reference to general market conditions.

b) Cash and cash equivalents, accounts receivable, accounts payable and accrued liabilities, senior loan and subordinated loan

The fair value of cash and cash equivalents, accounts receivable, accounts payable and accrued liabilities, senior loan and subordinated loan are estimated as the present value of future cash flows, discounted at the market rate of interest at the reporting date. As at December 31, 2017 and 2016, the fair value of cash and cash equivalents, accounts receivable, and accounts payable approximated their carrying value due to their short term maturity. The fair value of the senior and subordinated loans approximated their carrying values as their interest rates reflect current market conditions for such credit facilities.

c) Derivatives

The Company does not engage in the use of any derivative instruments for speculative purposes. If it enters into any contracts for the future delivery of non-financial assets, these are done in accordance with its expected sale requirements. As such, these contracts are not considered to be derivative instruments and have not been recorded at fair value in the financial statements. As the Company delivers petroleum products in accordance with the terms of these contracts, any associated revenue will be recorded as oil and natural gas revenue. The fair value of financial forward contracts and swaps is determined by discounting the difference between the contracted prices and published forward price curves as at the statement of financial position date, using the remaining underlying amounts and a risk free interest rate. The fair value of options and costless collars is based on option models that use published information with respect to volatility, prices and interest rates. The Company classifies its derivatives as Level 2 in the fair value hierarchy.

The following table sets forth, by level within the fair value hierarchy, the fair value on a recurring basis of the financial derivatives as of December 31, 2017.

	Total	Level 1	Level 2	Level 3
Balance at December 31, 2016	$ (61)	$ -	$ (61)	$ -
Change	(3,088)	-	(3,088)	-
Balance at December 31, 2017	$ (3,149)	$ -	$ (3,149)	$ -

d) Share-based compensation

The fair value of employee stock options is measured using a Black-Scholes option pricing model. Measurement inputs include share price on measurement date, exercise price of the option, expected volatility of the underlying share price (based on historical experience), weighted average expected life of the option (based on historical experience and general option holder behavior), expected dividends, forfeiture rate and the risk-free interest rate (based on government bonds).

e) Restricted bonus award
The fair value of restricted bonus awards is measured using current market value at the related grant date. Measurement inputs include current market value of the Company's shares with consideration of an expected forfeiture rate.

6. ACQUISITIONS

2017 Non-Producing Property Acquisitions

During the year ended December 31, 2017, the Company purchased oil and gas leases in its focus area in North Dakota. This represents increased working interests in potential drilling units with associated proved undeveloped and probable reserves. The consideration for these leases was approximately US $3.0 million ($3.8 million). There were no assumptions of liabilities associated with these purchases.

2017 Producing Property Acquisition

In June 2017, the Company acquired certain leases with associated proved undeveloped and probable reserves and oil and natural gas producing properties. The Company has treated the transaction as a business combination and has accounted for it using the acquisition method to reflect the fair value of the assets acquired and liabilities assumed. The decommissioning obligation was determined using the Company's estimated timing and costs to remediate, reclaim and abandon the related wells and production infrastructure, discounted at a market rate. Results of operations from the assets acquired were included in the financial statements from the closing date of the transaction. The total purchase price of US$8.7 million was settled with cash funded through the Company's credit facilities and indirectly with proceeds from an equity offering (Note 11).

The aggregate purchase price was allocated as follows:

CONSIDERATION (US$8,659)	$	11,647
NET ASSETS ACQUIRED AT FAIR VALUE		
Developed and producing assets	$	11,942
Decommissioning obligation		(295)
	$	11,647

The following reflects selected pro forma financial information for the year ended December 31, 2017 as if the acquisition had occurred on January 1, 2017 instead of the closing date of the transaction:

		Year ended December 31, 2017
Oil and natural gas revenue, net of royalties	$	801
Production and operating expenses		(297)
Operating income		504
Operating income reported for the year		24,507
Pro forma operating income for the year	$	25,011

2016 Non-Producing Property Acquisitions

During the year ended December 31, 2016, through various transactions, the Company purchased oil and gas leases in its focus area in North Dakota. These represent various working interests in potential drilling units with associated proved undeveloped and probable reserves. The aggregate consideration for these leases was approximately US$2.4 million ($3.3 million). There were no assumptions of liabilities associated with these purchases.

2016 Producing Property Acquisition

In May 2016, the Company acquired certain leases with associated proved undeveloped and probable reserves and oil and natural gas producing properties. The Company has treated the transaction as a business combination and has accounted for it using the acquisition method to reflect the fair value of the assets acquired and liabilities assumed. The decommissioning obligation was determined using the Company's estimated timing and costs to remediate, reclaim and abandon the related wells and production infrastructure, discounted at a market rate. Results of operations from the assets acquired were included in the financial statements from the closing date of the transaction. The total purchase price of US$4.0 million ($5.1 million) was settled with cash funded through the Company's credit facilities.

The aggregate purchase price was allocated as follows:

CONSIDERATION (US$3,950)	$	5,096
NET ASSETS ACQUIRED AT FAIR VALUE		
Developed and producing assets	$	5,219
Accounts receivable		8
Accounts payable		(18)
Decommissioning obligation		(113)
	$	5,096

The following reflects selected pro forma financial information for the year ended December 31, 2016 as if the acquisition had occurred on January 1, 2016 instead of the closing date of the transaction:

	Year ended December 31, 2016
Oil and natural gas revenue, net of royalties	$ 46
Production and operating expenses	(18)
Operating income	28
Operating income reported for the year	12,017
Proforma operating income for the year	$ 12,045

7. PROPERTY, PLANT AND EQUIPMENT

	Developed and Producing Assets	Other	Total
Balances as at December 31, 2015	$ 123,896	$ 47	$ 123,943
Acquisitions	8,505	-	8,505
Additions	20,909	-	20,909
Disposition	(651)	-	(651)
Depletion and depreciation	(8,903)	(20)	(8,923)
Effect of foreign exchange rate changes	(3,915)	(2)	(3,917)
Balances as at December 31, 2016	139,841	25	139,866
Acquisitions	15,897	-	15,897
Additions	51,121	91	51,212
Depletion and depreciation	(12,608)	(23)	(12,631)
Effect of foreign exchange rate changes	(10,170)	(2)	(10,172)
Balances as at December 31, 2017	$ 184,081	$ 91	$ 184,172

Depletion, Depreciation, and Future Development Costs

For the year ended December 31, 2017 and 2016, the Company recorded $12.6 million and $8.9 million, respectively, of depletion and depreciation expense, which reflected an estimated US$274.1 million and US$227.6 million, respectively of future development costs associated with proven plus probable reserves.

Impairment Charges

As at December 31, 2017 there were no facts or circumstances which suggested there is a trigger for impairment of the Company's Developed and Producing Assets. Therefore an impairment test was not required.

Dispositions

During the year ended December 31, 2016, the Company disposed of a minor holding in one of its non-core areas for cash proceeds of US$0.5 million and recorded no gain or loss in the statement of operations.

Capitalized Overhead

During the year ended December 31, 2017, the Company capitalized $815,000 of general and administrative costs and $7,000 of share-based compensation, which are directly attributable to the acquisition and exploitation activities of certain of its personnel in relation to the Company's operated property ($268,000 and $30,000 respectively – December 31, 2016).

8. DECOMMISSIONING OBLIGATION

Balance as at December 31, 2015	$	834
Acquisition of petroleum and natural gas properties (Note 6)		113
Additions		127
Obligations settled		(14)
Disposition		(3)
Revisions of estimated cash flows		173
Accretion		8
Effect of foreign exchange rate changes		(20)
Balance as at December 31, 2016		1,218
Acquisition of petroleum and natural gas properties (Note 6)		295
Additions		721
Revisions of estimated cash flows		369
Accretion		5
Effect of foreign exchange rate changes		(135)
Balance as at December 31, 2017	$	2,473

The Company's decommissioning obligation consists of remediation obligations resulting from its ownership interests in petroleum and natural gas assets. The total obligation is estimated based on the Company's net working interest in wells and related facilities, estimated costs to return these sites to their original condition, costs to plug and abandon the wells and the estimated timing of the costs to be incurred in future years.

The total undiscounted amount of estimated future cash flows required to settle the obligation as at December 31, 2017 is $5.1 million (December 31, 2016 – $2.4 million) which includes an annual inflation factor of 2.4% (December 31, 2016 – 1.7%) on the costs of decommissioning and assumes that the liabilities are settled over approximately the next 35 years in accordance with estimates prepared by independent engineers. The estimated future cash flows as at December 31, 2017 have been discounted at the risk-free interest rate of 2.6% (December 31, 2016 – 2.6%).

9. DEBT

	Senior Loan	Subordinated Loan	Total Debt
Balances as at December 31, 2015	$ 30,082	$ 75,408	$ 105,490
Proceeds from (repayment of loans), net	(121)	21,839	21,718
Net change in unamortized fees	-	(606)	(606)
Effect of foreign exchange rate changes	248	(2,269)	(2,021)
Balances as at December 31, 2016	30,209	94,372	124,581
Proceeds from (repayment of loans), net	20,831	(61,142)	(40,311)
Net change in unamortized fees	-	733	733
Effect of foreign exchange rate changes	(1,149)	(3,323)	(4,472)
Balances as at December 31, 2017	$ 49,891	$ 30,640	$ 80,531

Senior Loan

The Company's senior loan is a revolving credit facility, which as at December 31, 2017 had a borrowing base of US$39.9 million ($49.9 million), which recently increased to US$49.9 million ($62.4 million). The facility revolves until June 30, 2018, at which point, the facility can be extended, at the option of the lender, or if not extended, the facility is converted to a non-revolving facility with a term of 12 months maturing on June 30, 2019. This facility is secured by all of the Company's assets. The facility bears interest at the bank's prime lending rate, bankers' acceptance rates or US$ LIBOR rates plus a margin which is determined by the Company's senior debt to EBITDA ratio.

The borrowing base capacity of the senior loan facility is subject to a review performed at least twice annually by the bank, based on reserve reports associated with the Company's U.S. petroleum and natural gas properties. A decrease in the borrowing base could result in the requirement to make a repayment to the bank. The next borrowing base review is scheduled to be completed before the end of June 2018.

The credit facility is subject to certain financial and non-financial covenants. The financial covenants consist of: (i) a consolidated cash flow to interest expense ratio, as defined in the loan agreement, which is not to be less than 2.50 to 1 on a rolling four-quarter basis; and (ii) a requirement that the ratio of the senior loan amount to EBITDA, on a rolling four quarter basis, not exceed 3.0 to 1. The consolidated cash flow to interest expense ratio is calculated on the basis that interest expense reflects cash interest paid and excludes any deferred and unpaid interest on the subordinated credit facility and other non-cash amortization expense included in finance expense on the Company's statement of operations. Consolidated cash flow is defined as consolidated net income plus finance expense, taxes, and other non-cash expenses, adjusted to reflect the pro forma effects of asset acquisitions and dispositions, plus the proceeds of any equity issued by the Company. The consolidated cash flow to interest expense ratio at December 31, 2017 was 33.4 to 1, and the senior loan to EBITDA ratio was 2.77 to 1. As a result, the Company is in compliance with the financial

covenants as at that date, and is also in compliance with all of the other covenants under the senior loan as at December 31, 2017.

The facility was drawn approximately US$39.8 million as at December 31, 2017 (December 31, 2016 – US$22.5 million).

Subordinated Loan

As at December 31, 2017, the Company had a secured, subordinated, revolving credit facility which was available to be drawn in US dollars and which had a capacity of US$80.0 million ($100.4 million) as at December 31, 2017. Effective November 17, 2017, the Company amended the terms of the facility to extend the maturity date from December 31, 2017 to January 15, 2019. The credit facility bore interest at a rate of 12% per annum, and the Company incurred a 2.5% loan origination fee. The credit facility was provided by two significant shareholders of the Company, one of whom is the Executive Chairman of our Board of Directors. This loan was secured by all of the assets of the Company, but subordinated to the senior loan facility. Among certain non-financial covenants, the subordinated loan required the Company to comply with the financial covenants required by the senior loan agreement. Thus, a default under the terms of the senior loan would create a default under the subordinated loan agreement. This facility was drawn US$24.5 million as at December 31, 2017 (December 31, 2016 - US$70.9 million).

The Company deferred cash interest and origination fee payments under the facility from April 2015 to April 10, 2017 as a condition of the senior loan facility. Following completion of an equity offering in April 2017 (Note 11), the Company settled outstanding deferred interest of $22.3 million. The Company resumed interest payments on a monthly basis effective April 30, 2017.

As described further in Note 20, the subordinated loan facility was settled with the proceedings of a preferred share financing completed in January 2018, and as a condition of that financing, the subordinated loan facility was terminated.

10. FINANCIAL DERIVATIVE INSTRUMENTS

The Company may use swaps and options to reduce the effect of commodity price changes on a portion of its future oil production. The objective of the Company's use of derivative financial instruments is to achieve more predictable cash flows in an environment of volatile oil and natural gas prices and to manage its exposure to commodity price risk. While the use of these derivative instruments limits the downside risk of adverse price movements, such use may also limit the Company's ability to benefit from favorable price movements. The Company may, from time to time, add incremental derivatives to hedge additional production, restructure existing derivative contracts or enter into new transactions to modify the terms of current contracts in order to realize the current value of the Company's existing positions. The Company does not enter into derivative contracts for speculative purposes.

The use of derivatives involves the risk that the counterparty to such instruments will be unable to meet the financial terms of such contracts. The Company's derivative contracts are currently with its senior lender, a Schedule A Canadian Bank, and management does not believe the risk of counterparty failure to be significant.

The amount of loss recognized in the statement of operations related to the Company's derivative financial instruments was $3.1 million for the year ended December 31, 2017 ($61,000 – December 31, 2016).

The Company's commodity derivative instruments are measured at fair value and are included in the accompanying statements of financial position as financial derivative assets and liabilities. Unrealized gains and losses are recorded based on the changes in the fair values of the derivative instruments. Both the unrealized and realized gains and losses resulting from the contract settlement of derivatives are recorded in the statement of operations.

The Company's outstanding commodity derivative contracts are summarized below (in thousands except for volumes and price per Bbl):

Term	Type	Volumes[1]	Price (per Bbl $US)	Reference	Fair Value
January 1, 2018 to December 31, 2018	Collar	500 Bopd	$45.00 - $55.70	WTI	$(1,190)
January 1, 2018 to December 31, 2018	Collar	500 Bopd	$45.00 - $57.00	WTI	(978)
January 1, 2018 to December 31, 2018	Collar	500 Bopd	$47.00 - $56.75	WTI	(981)
Outstanding as at December 31, 2017					$(3,149)

[1] Bopd is barrels of oil per day

11. SHARE CAPITAL

a) Share capital

The Company's authorized share capital includes unlimited Class A preferred shares with rights and privileges to be determined by the Board of Directors prior to issuance, unlimited non-voting common shares, convertible into voting common shares on a 1 for 1 basis, and unlimited voting common shares. As at December 31, 2017, the Company had 157,137,767 voting common shares (December 31, 2016 – 27,507,574) and nil non-voting common shares issued and outstanding (December 31, 2016 – 6,700,000).

The following table reflects the Company's outstanding common shares as at December 31, 2017:

	Number of Voting and Non-Voting Shares	Share Capital
Balance as at December 31, 2016 and 2015	34,207,574	$ 35,658
Issuance of common shares by prospectus, net of issue costs	122,265,000	105,639
Issuance of common shares by private placement, net of issue costs	384,615	496
Exercise of options to purchase common shares	280,578	586
Balance as at December 31, 2017	157,137,767	$142,379

On April 11, 2017, the Company completed an equity offering resulting in the issuance of 122,265,000 voting common shares at a price of $0.90 per share for gross proceeds of approximately $110 million. The Company's Executive Chariman participated in this offering, purchasing 44,444,500 voting common shares. Additionally, in June 2017, the Company completed a private placement of 384,615 voting common shares to the Company's President and CEO for gross proceeds of $500,000. During 2017, 280,578 stock options were exercised at $0.70 for cash proceeds of $196,000. Under the Company's accounting policy, upon exercise of stock options, related amounts previously credited to contributed surplus are transferred to share capital. During 2017, the Company's outstanding 6,700,000 non-voting shares were converted to an equivalent number of voting common shares.

b) Stock options

The following table presents stock option transactions for the years ended December 31, 2017 and December 31, 2016:

	Number of Options	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term (Years)
Balance as at December 31, 2015	2,295,205	$ 1.16	3.36
Granted	1,350,000	0.70	5.00
Forfeited	(908,469)	(1.46)	(1.34)
Balance as at December 31, 2016	2,736,736	0.83	3.01
Exercised	(280,578)	(0.70)	(3.53)
Settled	(75,000)	(0.70)	(0.96)
Forfeited and expired	(832,894)	(1.13)	(1.74)
Balance as at December 31, 2017	1,548,264	$ 0.70	2.13

As at December 31, 2017, the following stock options were outstanding:

Weighted Average Exercise Price	Weighted Average Remaining Contractual Term (Years)	Number of Outstanding Options	Number of Options Exercisable
$0.70	2.13	1,548,264	1,117,427

The Company uses the fair value method to account for all share-based awards granted to employees, officers and directors. The estimated fair value of stock option grants was determined using the Black-Scholes option pricing model and is recorded as a charge to income over the vesting period with a corresponding increase to contributed surplus.

c) Warrants

The Company issued 2 million common share purchase warrants to the Company's subordinated lenders (see Notes 9 and 15) on May 10, 2016. Each warrant entitles the holder to exercise and acquire one common share for $0.75 for a period of two years from the date of grant. In March 2018, the holders of

warrants exercised their right to acquire 2 million common shares resulting in net proceeds to the Company of $1.5 million.

d) Restricted awards

The Company granted 2,625,000 restricted bonus awards ("awards") to certain directors, officers and employees of PetroShale in November 2017. These awards expire in December 2020 and vest in equal tranches in March 2019, March 2020 and December 2020. The estimated fair value of the awards of $4.3 million was determined based on the current market value of the Company's common shares at the date of grant of $1.80 per share and giving consideration to anticipated forfeiture rates. A charge to income is reflected in share based compensation in the statement of operations over the vesting period with a corresponding increase to contributed surplus.

12. NET LOSS PER COMMON SHARE

The following table presents the Company's net loss per common share:

	Years ended December 31,	
(thousands, except for share and per share data)	**2017**	**2016**
Net loss	$ (3,093)	$ (12,862)
Weighted average number of basic and diluted common shares	123,279,448	34,207,574
Net loss per weighted average basic and diluted common share	$ (0.03)	$ (0.38)

13. INCOME TAXES

The provision for income taxes recorded in the financial statements varies from the amount that would be computed by applying the Canadian statutory income tax rate of 26.50% as a result of the following:

	Year ended December 31, 2017	Year ended December 31, 2016
Loss before income tax provision	$ (3,093)	$ (12,862)
Statutory rate	26.50%	26.50%
Income tax recovery at statutory rate	(820)	(3,408)
Tax effect of the following:		
Effect of higher corporate tax rate in US	(183)	(1,329)
Non - deductible expense	210	125
Impact of rate change and other	1,588	(375)
Impact of Tax Cuts and Jobs Act (US)	6,734	-
Change in unrecognized deferred tax asset	(7,529)	4,987
Provision for income taxes	$ -	$ -

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

	December 31, 2017	December 31, 2016
Decommissioning obligation	$ 2,473	$ 1,218
Accrued interest	-	18,773
Non-capital losses (Federal)	55,033	41,887
Non-capital losses (State)	50,781	30,674
Capital losses	739	1,478
Share issue costs	12	23
Share-based compensation	213	977
Unrealized loss on financial derivatives	3,149	61
Other	206	111
	$ 112,606	$ 95,202

As at December 31, 2017, the Company has the following tax losses available to shelter future income:

	December 31, 2017	Expiration Dates
Non-capital losses (U.S.)	$ 79,085	2033 to 2037
Non-capital losses (CAN)	$ 6,121	2032 to 2037
Non-capital losses (Colorado)	$ 42	2035 to 2037
Non-capital losses (Montana)	$ 8,093	2018 to 2024
Non-capital losses (North Dakota)	$ 42,646	2033 to 2037
Capital losses (Canada)	$ 1,478	not applicable

14. COMMITMENTS

The Company has an outstanding letter of credit in favor of an energy regulator in North Dakota in the amount of US$75,000. As security, the Company has set aside an equivalent amount in cash at the financial institution that issued the letter of credit. In addition, the Company has advanced funds to other regulatory agencies in the amount of US$125,000 as security in order to operate in North Dakota.

The Company is committed to monthly rental payments for office space of US$12,000 through July 2020.

15. RELATED PARTY TRANSACTIONS

Related party transactions are measured at the exchange amount, which is the amount of consideration established and agreed to by the related parties.

Compensation of key management personnel

Key management personnel include the Chief Executive Officer (CEO) of the Company, the President of PetroShale (U.S.), Inc. (resigned September 2017), the Chief Financial Officer (CFO) and the directors and other officers of the Company.

	Year Ended December 31, 2017	Year Ended December 31, 2016
Salaries and other short-term benefits	$ 1,123	$ 459
Consulting fees	274	398
Share-based compensation	342	174
	$ 1,739	$ 1,031

As at December 31, 2017, the Company had a secured, subordinated, revolving credit facility which was provided by two significant shareholders of the Company, one of whom is also the Executive Chairman of our Board of Directors. See further details in Note 9 – Debt - Subordinated loan. During the year ended December 31, 2017, fees and the value of warrants issued in connection with this facility were amortized to finance expense in the amount of $726,000 (December 31, 2016 – $722,000). The Company had deferred payment of interest and fees related to the facility from April 1, 2015 through April 10, 2017. Following completion of an equity offering in April 2017, the Company settled accrued interest and origination fees of $22.3 million and paid principal of $53.3 million. Payments of interest subsequently resumed on a monthly basis.

The lenders to this facility agreed to enhance its terms in April 2016. As partial consideration for extending the term of the subordinated loan, increasing the facility capacity and agreeing to continue to defer cash interest payments, the Company granted 2 million common share purchase warrants to the subordinated lenders, pro rata to their participation in the revised commitment amount. Each warrant entitles the holder to acquire one common share at $0.75 for a period of two years from the date of issuance. These warrants were valued at $684,000 on the date of issuance and reflected in shareholders' equity on the statements of financial position.

In January 2018, the Company repaid outstanding balances under, and terminated, the subordinated loan facility following completion of a US$75 million preferred equity financing. See Note 20.

In March 2018, the holders of warrants (see Note 11) exercised their right to acquire 2 million common shares resulting in net proceeds to the Company of $1.5 million.

16. RISK MANAGEMENT

a) Overview

The Company's activities expose it to a variety of financial risks such as credit risk, liquidity risk and market risk that arise as a result of its exploration, development, production and financing activities.

This note presents information about the Company's exposure to each of the above risks, the Company's objectives, policies and processes for measuring and managing risk and the Company's management of capital. Further quantitative disclosures are included throughout these financial statements.

The Board of Directors oversees management's establishment and execution of the Company's risk management framework. Management has implemented and monitors compliance with risk management policies. The Company's risk management policies are established to identify and analyze the risks faced by the Company, to set appropriate risk limits and controls and to monitor risks and market conditions.

b) Credit risk

Credit risk is the risk of financial loss to the Company if a customer or counterparty to a financial instrument fails to meet its contractual obligations.

The carrying amount of the Company's cash and cash equivalents and accounts receivable and the positive fair value of any financial derivatives represent the maximum credit exposure.

With respect to accounts receivable, the Company's exposure to credit risk is influenced mainly by the individual characteristics of each customer.

To the extent the Company's oil and natural gas operations are conducted on a non-operated basis, its accounts receivable mainly reflect joint venture receivables from the operators of those properties. In relation to the Company's operated properties, the Company is exposed to collection risks on the sale of its oil and gas production and collection of well costs incurred on behalf of its working interest partners. The Company attempts to mitigate the risk from joint venture receivables by working with large reputable industry participants. However, the receivables are from participants in the petroleum and natural gas sector and collection of the outstanding balances is dependent on industry factors such as commodity price fluctuations, escalating costs and the risk of unsuccessful drilling. Further risk exists with joint venture partners as disagreements occasionally arise, increasing the risk of non-collection. Sales of oil and natural gas production from our operated properties are made to large industry purchasers.

The Company does not typically obtain collateral from joint venture partners and believes that operators of its non-operated properties, who are responsible for marketing the production from those properties, do not typically obtain collateral from petroleum and natural gas marketers they may utilize. However, the Company mitigates this risk by working with large reputable operators.

With respect to its operated assets, the Company does not anticipate any default on collection of accounts receivable as it transacts with credit-worthy customers. As such, a provision for doubtful accounts has not been recorded as at December 31, 2017 or December 31, 2016.

All of the Company's accounts receivable are from the production of oil and natural gas and joint venture receivables. As at December 31, 2017 there are no significant receivables that are greater than 90 days outstanding.

Should the value of the Company's financial derivative instruments have a positive value, the Company is exposed to that amount should the counterparty to such instruments default. The counterparty to all of the Company's financial derivatives is the Company's senior lender and a Schedule A Canadian Bank. The Company believes any such credit risk is not material.

c) Liquidity risk

Liquidity risk is the risk that the Company will encounter difficulty in meeting its financial obligations as they come due. The financial liabilities in the statement of financial position consist of accounts payable, which are all considered due within one year, financial derivative liability and the senior and subordinated loans. The Company anticipates it will continue to have adequate liquidity to fund its financial liabilities as they come due. The Company forecasts its cash flows from operating activities as well as obligations related to capital spending and settlement of accounts payable in relation to available liquidity from its revolving credit facilities. The Company's accounts payable and accrued liabilities balance at December 31, 2017 is approximately $38.5 million (December 31, 2016 - $29.6 million). It is the Company's practice to pay suppliers within 60 days. As at December 31, 2017, substantially all of the account balances were less than 90 days old.

The Company's financial derivative liability of $3.1 million as at December 31, 2017 ($61,000 – December 31, 2016) reflects the fair value of its oil price management contracts as at that date. Depending on market oil prices at the time, the Company may need to pay the counterparty to such contracts a monthly amount which reflects the positive difference between the market WTI price and the upper price band of the related collars. The Company will fund such liabilities from proceeds of its oil production which will be sold in the market at prices reflecting such higher WTI prices.

The following are the contractual maturities of the Company's debt obligations and anticipated timing of settlements of its other financial liabilities as at December 31, 2017, including estimated interest payments:

(in thousands)	Contractual Cash Flow	Less than 1 Year	1-2 Years	3-5 Years	Thereafter
Accounts payable and accrued liabilities	$ 38,447	$ 38,447	$ -	$ -	$ -
Senior loan [1]	53,249	2,245	51,004	-	-
Subordinated loan[2]	34,589	3,690	30,899	-	-
Total	$ 126,285	$ 44,382	$81,903	$ -	$ -

[1]Includes future interest expense at the rate of 4.5% being the rate applicable at December 31, 2017 to the current maturity date of June 30, 2019.

[2]The amount differs from that presented on the statement of financial position due, in part, to the unamortized portion of warrant amounts, which are offset against the loan principal on the statement of financial position, and future interest expense at the fixed rate of 12.0% as at December 31, 2017. The table reflects the full interest obligation to the maturity date of January 15, 2019. This loan was settled following the issuance of a US$75 million preferred equity financing in January 2018. These preferred shares, if not converted to common shares at the option of the holder, must be redeemed by the Company in January 2023, and bear a coupon rate of 9.0% per annum.

d) Market risk

Market risk is the risk that changes in market prices relating to currency, commodity prices and interest rates will affect the Company's net earnings, future cash flows, the value of financial instruments, or the fair value of its assets and liabilities. The objective of market risk management is to manage and control market risk exposure within acceptable parameters.

Although the Company does not generally sell or transact in foreign currencies, its US subsidiaries conduct their operations primarily in US dollars. Furthermore, exchange rate fluctuations can affect the fair value and cash flow from derivative contracts. For the years ended December 31, 2017 and December 31, 2016, the Company did not enter into any foreign currency derivative contracts.

Commodity prices for crude oil, natural gas liquids and natural gas are also impacted by political events, meteorological conditions and changes in supply and demand. The Company may enter into commodity derivative contracts that provide downside price protection in order to provide some stability of cash flows for capital spending and planning purposes. The Company's risk management activities are conducted pursuant to its risk management policies approved by the Board of Directors.

Interest rate risk is the risk that future cash flows will fluctuate as a result of changes in interest rates. The Company's interest rate risk arises from its floating rate senior loan. For the years ended December 31, 2017 and 2016, the Company did not enter into any interest rate derivative contracts. The impact of a 1% increase in the interest rate associated with the senior loan for the year ended December 31, 2017, would have been an increase in net loss of approximately $0.3 million (December 31, 2016 - $0.3 million).

17. CAPITAL MANAGEMENT

The Company's objective when managing capital is to maintain a flexible capital structure which will allow it to execute on its capital expenditure program, which includes expenditures on 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 manages its capital structure and makes adjustments by continually monitoring its business conditions, including: current economic conditions; the risk characteristics of the Company's petroleum and natural gas assets; the depth of its investment opportunities; current and forecasted net debt levels; current and forecasted commodity prices; and other factors that influence realized commodity prices and funds flow from operations such as quality and basis differential, royalties, operation costs and transportation and processing costs. The Company considers its capital structure to include working capital, any debt and shareholders' equity. The Company monitors capital based on current funds flow from operations compared to forecasted capital and operating requirements.

In order to maintain or adjust the capital structure, the Company will consider: its forecasted funds flow from operations while attempting to finance an acceptable capital expenditure program which may in the future include acquisition opportunities; the current level of credit available from its lenders; the level of credit that may become available from its lenders as a result of oil and gas reserve growth; the availability of other sources of debt with different characteristics than bank debt; the sale of assets; limiting the size of the capital expenditure program and new equity if available on favorable terms. The Company's share capital is not subject to external restrictions. Access to any bank credit facility is determined by the lenders and is generally based upon the lenders' borrowing base models which are based upon the Company's petroleum and natural gas reserves.

18. SUPPLEMENTAL CASH FLOW DISCLOSURES

Changes in non-cash working capital is comprised of:

	Years ended December 31,	
	2017	**2016**
Source / (use) of cash:		
Accounts receivable	$ (5,516)	$ (1,201)
Prepaid expenses and deposits	(116)	(46)
Accounts payable and accrued liabilities	8,874	11,361
	$ 3,242	$ 10,114
Related to operating activities	$ (1,865)	$ (775)
Related to investing activities	23,984	(1,545)
Related to financing activities	-	644
Payment of previously deferred interest	(22,330)	-
Deferred interest and fees	3,673	12,073
Assumed working capital on asset acquisition	-	10
Difference due to foreign exchange	(220)	(293)
	$ 3,242	$ 10,114
Interest paid	$ 3,726	$ 1,501
Income taxes paid	nil	nil

19. SEGMENT DISCLOSURES

The Company operates in one industry segment, the production of petroleum and natural gas and development of oil and natural gas properties.

The Company and its subsidiary operated in two geographical segments during the years reported below, being Canada and the United States.

	Years ended December 31, 2017	Years ended December 31, 2016
Revenue, net of royalties		
United States	$ 34,806	$ 18,414
Canada	75	63
	$ 34,881	$ 18,477
Net loss for the period		
United States	$ (2,042)	$ (12,318)
Canada	(1,051)	(544)
	$ (3,093)	$ (12,862)

	December 31, 2017	December 31, 2016
Property, plant and equipment		
United States	$ 183,567	$ 139,215
Canada	605	651
	$ 184,172	$ 139,866

20. SUBSEQUENT EVENTS

On January 25, 2018, the Company closed a preferred equity financing with a private investor (the "Investor") for gross proceeds of US$75 million. The preferred shares were issued by the Company's US subsidiary and are convertible, at the holder's option, to common shares of the Company at a fixed price of $2.40 per share, subject to certain conditions. The preferred shares have a term of five years (subject to extension for an additional year at the election of the Investor) and entitle the Investor to a cumulative annual dividend of 9% per annum (except that no dividends shall be payable for the extension year, if any), payable quarterly. As part of the financing, the Investor also acquired voting preferred shares of the Company which entitle the Investor to the "as-exchanged" voting rights of the subsidiary preferred shares. The net proceeds of the financing were used to settle outstanding amounts under the Subordinated Loan, with the remaining amounts used to repay amounts drawn under the Senior Loan. As a condition to closing the financing, the Subordinated Loan was terminated.

In March 2018, the holders of warrants (see Note 11) exercised their right to acquire 2 million common shares for net proceeds to the Company of $1.5 million.

In March 2018, the Company closed an acquisition of land, and an interest in a producing oil well, for cash consideration of US$17.8 million. The acquisition was funded from the Company's senior credit facility.