



## **Interim Financial Statements of**

## **Canadian Spirit Resources Inc.**

*(Unaudited – Prepared by Management)*

**For the nine-month period ended September 30, 2020**

**(Expressed in Canadian Dollars)**

2. MANAGEMENT'S COMMENTS ON THE UNAUDITED INTERIM FINANCIAL STATEMENTS
3. STATEMENTS OF FINANCIAL POSITION
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## **Canadian Spirit Resources Inc.**

**Dated November 27, 2020**

### **Management's Comments on Unaudited Interim Financial Statements**

The accompanying unaudited interim financial statements of Canadian Spirit Resources Inc for the nine months ended September 30, 2020 and 2019 have been prepared by management, reviewed by the Audit Committee and approved by the Board of Directors of the Company.

In accordance with National Instrument 51-102 released by the Canadian Securities Administrators, the Company discloses that its auditors have not reviewed the unaudited interim financial statements for the nine-month period ended September 30, 2020.

# Canadian Spirit Resources Inc.

## Statements of Financial Position

As at September 30, 2020 and December 31, 2019

(Unaudited - Expressed in Canadian Dollars)

	September 30, 2020	December 31, 2019
<b>ASSETS</b>		
<b>Current assets</b>		
Cash and cash equivalents	\$ 642,278	\$ 639,696
Accounts receivables	8,506	27,691
Prepaid expenses and deposits	-	35,676
	<u>650,784</u>	<u>703,063</u>
Exploration and evaluation assets (Note 6)	32,354,046	32,263,477
Property and equipment (Note 7)	3,315,079	3,528,643
Right-of-use assets (Note 8)	38,979	43,011
Restricted deposits (Note 5)	1,531,540	1,749,420
Royalty credits (Note 12)	307,460	307,460
	<u>37,547,104</u>	<u>37,892,011</u>
	<b>\$ 38,197,888</b>	<b>\$ 38,595,074</b>
<b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>		
<b>Current</b>		
Accounts payable and accrued liabilities (Note 21)	\$ 178,955	\$ 111,162
Accrued settlement of claims (Note 20)	514,552	-
Loan payable (Note 9)	610,000	-
Lease liability (Note 10)	3,958	3,576
	<u>1,307,465</u>	<u>114,738</u>
<b>Non-current liabilities</b>		
Decommissioning liabilities (Note 13)	2,089,925	2,060,873
Lease liability (Note 10)	38,063	41,618
	<u>2,127,988</u>	<u>2,102,491</u>
	<u>3,435,453</u>	<u>2,217,229</u>
<b>Shareholders' equity</b>		
Common shares (Note 14)	118,177,558	118,177,558
Contributed surplus	9,519,909	9,503,382
Deficit	(92,935,032)	(91,303,095)
	<u>34,762,435</u>	<u>36,377,845</u>
<b>Total shareholders' equity</b>	<b>34,762,435</b>	<b>36,377,845</b>
	<b>\$ 38,197,888</b>	<b>\$ 38,595,074</b>

Going concern and basis of presentation (Note 1)

ON BEHALF OF THE BOARD:

*(signed)* "Louisa DeCarlo"

Director

*(signed)* "Stuart Ross"

Director

The accompanying notes are an integral part of these financial statements

## Canadian Spirit Resources Inc.

### Statements of Loss and Comprehensive Loss

For the three and nine months ended September 30, 2020 and 2019

(Unaudited - Expressed in Canadian Dollars)

	Three months ended		Nine months ended	
	September 30, 2020	September 30, 2019	September 30, 2020	September 30, 2019
<b>Other income and gains</b>				
Interest and other income	\$ 44	\$ 4,905	\$ 8,753	\$ 24,879
Gain on sale of property, plant and equipment (Note 7)	-	-	14,450	52,942
	44	4,905	23,203	77,821
<b>Expenses</b>				
Operating costs	59,363	94,928	198,568	236,013
General and administrative (Note 20)	195,721	231,304	674,018	711,027
Exploration and evaluation (Note 6)	-	186,955	6,708	354,426
Depletion and depreciation (Notes 7 and 8)	72,532	72,532	217,596	218,822
Finance costs (Notes 10 and 13)	7,448	10,900	27,171	46,237
Share-based compensation (Note 15)	11,155	14,920	16,527	38,295
Settlement of claims (Note 20)	-	-	514,552	-
	(346,219)	(611,539)	(1,655,140)	(1,604,820)
<b>Net loss and comprehensive loss for the period</b>	\$ (346,175)	\$ (606,634)	\$ (1,631,937)	\$ (1,526,999)
Basic and diluted loss per common share	\$ (0.00)	\$ (0.00)	\$ (0.01)	\$ (0.01)
Weighted average shares outstanding basic and diluted	196,177,583	196,177,583	196,177,583	196,177,583

The accompanying notes are an integral part of these financial statements

## Canadian Spirit Resources Inc.

### Statements of Changes in Shareholders' Equity

(Unaudited - Expressed in Canadian Dollars)

	Common Shares		Contributed Surplus	Deficit	Total
	Number	Amount			
Unlimited number of common shares with no par value					
<b>Balance as at December 31, 2018</b>	<b>196,177,583</b>	<b>\$ 118,177,558</b>	<b>\$ 9,452,680</b>	<b>\$ (89,881,661)</b>	<b>\$ 37,748,577</b>
Net loss and comprehensive loss	-	-	-	(1,526,999)	(1,526,999)
Share-based compensation (Note 15)	-	-	38,295	-	38,295
<b>Balance as at September 30, 2019</b>	<b>196,177,583</b>	<b>118,177,558</b>	<b>9,490,975</b>	<b>(91,408,660)</b>	<b>36,259,873</b>
Net loss and comprehensive loss	-	-	-	105,565	105,565
Share-based compensation (Note 15)	-	-	12,407	-	12,407
<b>Balance as at December 31, 2019</b>	<b>196,177,583</b>	<b>118,177,558</b>	<b>9,503,382</b>	<b>(91,303,095)</b>	<b>36,377,845</b>
Net loss and comprehensive loss	-	-	-	(1,631,937)	(1,631,937)
Share-based compensation (Note 15)	-	-	16,527	-	16,527
<b>Balance as at September 30, 2020</b>	<b>196,177,583</b>	<b>\$ 118,177,558</b>	<b>\$ 9,519,909</b>	<b>\$ (92,935,032)</b>	<b>\$ 34,762,435</b>

The accompanying notes are an integral part of these financial statements

## Canadian Spirit Resources Inc.

### Statements of Cash Flows

For the nine months ended September 30, 2020 and 2019

(Unaudited - Expressed in Canadian Dollars)

	September 30, 2020	September 30, 2019
<b>Cash Flows used in Operating Activities:</b>		
Net loss and comprehensive loss	\$ (1,631,937)	\$ (1,526,999)
Add items not affecting cash:		
Interest on loan advances	10,000	-
Depletion and depreciation (Note 7 and 8)	217,596	218,822
Exploration and evaluation (Note 6)	-	354,426
Accretion (Notes 10 and 13)	22,344	41,070
Loss on remeasurement of ARO	6,708	-
Gain on sale of property, plant and equipment	(14,450)	(52,942)
Share-based compensation (Note 15)	16,527	38,295
	<u>(1,373,212)</u>	<u>(927,328)</u>
Changes in non-cash working capital		
Accounts receivable	19,185	(35,789)
Prepaid expenses and other deposits	35,676	40,355
Accounts payable and other accruals	67,793	5,659
Accrued settlement of claims (Note 20)	514,552	-
	<u>(736,006)</u>	<u>(917,103)</u>
<b>Cash Flows from (used in) Financing Activities:</b>		
Loan advances	600,000	-
Principal and accretion payments of lease liabilities (Note 10)	(3,173)	(2,833)
	<u>596,827</u>	<u>(2,833)</u>
<b>Cash Flows used in Investing Activities:</b>		
Exploration and evaluation expenditures (Note 6)	(90,569)	(149,159)
Property, plant and equipment expenditures	-	(444)
Proceeds on sale of property, plant and equipment	14,450	52,942
Restricted deposits	217,880	-
	<u>141,761</u>	<u>(96,661)</u>
<b>Change in cash and cash equivalents</b>	<b>2,582</b>	<b>(1,016,597)</b>
<b>Cash and cash equivalents, beginning of the period</b>	<b>639,696</b>	<b>1,944,702</b>
<b>Cash and cash equivalents, end of the period</b>	<b>\$ 642,278</b>	<b>\$ 928,105</b>
Cash paid for interest	\$ 15,000	\$ -
Cash paid for tax	\$ -	\$ -

The accompanying notes are an integral part of these financial statements

# Canadian Spirit Resources Inc.

## Notes to the Financial Statements

For the nine months ended September 30, 2020

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### 1. CORPORATE INFORMATION, GOING CONCERN AND BASIS OF PRESENTATION

#### Corporate Information

Canadian Spirit Resources Inc. (“CSRI” or the “Corporation”) is a natural resources company focusing on the identification and development of opportunities in the unconventional natural gas sector of the energy industry and its shares are listed under the trading symbol “SPI” on the TSX Venture Exchange (the “Exchange”). The Corporation is continued under the laws of the province of Alberta and its head office is located at Suite 900, 140 - 4<sup>th</sup> Avenue S.W., Calgary, Alberta, Canada T2P 3N3.

#### Going Concern

These financial statements have been prepared using International Financial Reporting Standards (“IFRS”) as they apply to a going concern, which contemplates the realization of assets and settlement of liabilities in the normal course of operations as they come due. For the period ended September 30, 2020, the Corporation has reported a net loss and comprehensive loss of \$1,631,937 (December 31, 2019: \$1,421,434) and an accumulated deficit at September 30, 2020 of \$92,935,032 (December 31, 2019: \$91,303,095). In addition to covering on-going working capital requirements and recurring negative cash flows used in operating activities, the Corporation will need to secure additional funding for any future exploration and development programs. In conjunction with recent energy price fluctuations, the current natural gas market continues to experience low commodity prices due to excess supply and lack of additional international markets to sell into. These circumstances lend significant doubt as to the ability of the Corporation to meet its obligations as they come due and, accordingly, the appropriateness of the use of accounting principles applicable to a going concern.

During the period ended September 30, 2020 and during the year ended December 31, 2019 the Corporation did not raise equity capital, it did however, issue to its largest shareholder, Elmag Investment Inc., a redeemable secured debenture to borrow \$600,000 (see Note 9). In recognition of the circumstances in 2018, the Corporation completed a rights offering in December 2018 for gross proceeds of \$1.5 million (see Note 13). Due to petroleum and natural gas market prices, the Corporation shut in its production facilities to reduce costs and losses, thus, in the near future will not have any revenues related to petroleum and natural gas until prices increase to cover costs of operations. During the year ending December 31, 2019, management also undertook steps to reduce general and administrative expenses, including, but not limited to, field operational efficiencies, renegotiation of its office lease terms and reductions in staffing levels/remuneration. During the period ended September 30, 2020, management continued to reduce general and administrative expenses by eliminating its office lease and staff and replacing them with consultants.

These undertakings, while significant, are not sufficient in and of themselves to enable the Corporation to fund all aspects of its forecasted operations and any future exploration and development, and accordingly, management will need to pursue other financing alternatives to fund the Corporation so that it may continue as a going concern. The necessary financing may be secured through either the issue of new equity or debt instruments or entering into new joint venture or farm-in arrangements. Nevertheless, there is no assurance that such initiatives will be successful.

The Corporation's ability to continue as a going concern is dependent upon its ability to fund any future exploration and development programs as well as generate positive cash flows from operating activities. These financial statements do not reflect any adjustments to the carrying values and classifications of assets and liabilities, or to the reported revenues and expenses that would be necessary if the Corporation were unable to realize its assets and settle its liabilities as a going concern in the normal course of operations. Such adjustments could be material.

# Canadian Spirit Resources Inc.

## Notes to the Financial Statements

For the nine months ended September 30, 2020

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### 1. CORPORATE INFORMATION, GOING CONCERN AND BASIS OF PRESENTATION (Continued)

#### Statement of Compliance

These interim financial statements are unaudited and have been prepared in accordance with IAS 34 'Interim Financial Reporting' ("IAS 34") using accounting policies consistent with the International Financial reporting Standards ("IFRS") issued by the International Accounting Standards Board ("IASB") and Interpretations of the International Financial Reporting Interpretations Committee ("IFRIC").

These financial statements have been prepared on the basis of IFRS standards that are effective for the Company's reporting period ended September 30, 2020. The Board of Directors approved the financial statements for issue on November 27, 2020.

#### Basis of Presentation

The financial statements have been prepared on a going concern basis using the historical cost convention, except as detailed in the accounting policies disclosed in Note 2. The preparation of the financial statements requires Management to use judgments, estimates and assumptions that affect the reported amounts of assets, liabilities and the disclosure of contingencies at the date of the financial statements, and revenues and expenses during the reporting period. Accordingly, actual results could differ from those estimated. Significant estimates and judgments used in the preparation of the financial statements are detailed in Note 3.

### 2. SIGNIFICANT ACCOUNTING POLICIES

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

#### a) Cash and Cash Equivalents

Cash and cash equivalents include cash on hand, market deposits and similar type instruments with an original maturity of three months or less when purchased.

#### b) Exploration and Evaluation Assets

Costs incurred relating to establishing the commercial viability and technical feasibility of exploration and evaluation ("E&E") assets are initially capitalized as either intangible E&E petroleum and natural gas properties or as tangible E&E facilities and equipment. These include costs such as land and lease acquisition, geological and geophysical expenditures, and the drilling and completion of test wells. However, costs incurred relating to general prospecting prior to obtaining any legal rights to explore are expensed as incurred. E&E costs are not depleted and are carried forward at cost until proved reserves are determined to exist. A review of all exploration or drilling licences is carried out at least annually to determine if reserves exist. Upon the determination of proved reserves, the carried forward E&E costs together with the accumulated developed and producing ("D&P") costs of the related cost generating unit ("CGU") are tested for impairment, and are then reclassified as intangible petroleum and natural gas properties or tangible facilities and equipment within property, plant and equipment. E&E assets would be determined to be impaired if both commercial viability and technical feasibility are not established through the determination of proved reserves, or if there are no future plans for activity and leases have expired.

# Canadian Spirit Resources Inc.

## Notes to the Financial Statements

For the nine months ended September 30, 2020

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### 2. SIGNIFICANT ACCOUNTING POLICIES (Continued)

#### c) Property, Plant and Equipment

Unless initially classified as E&E assets, all costs related to the continuing acquisition, exploration and development of intangible petroleum and natural gas properties and tangible facilities and equipment are capitalized as property, plant and equipment (“PP&E”) and are measured at cost less accumulated depletion and depreciation and accumulated impairment losses. These costs include land and lease acquisition costs, annual charges on producing and non-producing properties, geological and geophysical costs, costs of drilling and completing productive and non-productive wells, costs for production facilities, decommissioning costs, and carrying costs. Repair and maintenance costs are expensed as incurred. Intangible petroleum and natural gas properties and tangible facilities and equipment are accumulated in CGUs.

Costs are depleted or depreciated using the unit-of-production method based upon estimated proved plus probable reserves. Costs subject to depletion include estimated future costs to develop proved plus probable reserves and exclude estimated salvage value. Reserve and production volumes of natural gas are converted to common units on the equivalency basis of six thousand cubic feet (“Mcf”) to one barrel of oil, reflecting the approximate relative energy content. Proceeds from the disposition of intangible petroleum and natural gas properties or tangible facilities and equipment are offset against the accumulated costs of the properties sold and any gains or losses are recorded in the statement of loss and comprehensive loss in the period when the disposition occurred.

Water pipeline project expenditures, included as tangible facilities and equipment, are recorded at cost. Once commissioned, and therefore upon the determination of being available for use, water pipeline costs are amortized on a straight-line basis over the life of the water licence issued by the regulatory authority.

#### d) Capitalization of Exploration and Development Costs

The Corporation capitalizes, within both E&E assets and PP&E assets, the portion of overhead costs that are directly attributable to the respective exploration and development activity, including cash and share-based compensation costs paid to CSRI personnel dedicated to capital projects. The Corporation did not capitalize overhead costs during the period ended September 30, 2020 and for the year ended December 31, 2019.

#### e) Impairment

##### *Financial Assets*

A financial asset is assessed at each reporting date to determine whether there is any objective evidence that it is impaired. Loss allowances are measured at an amount equal to the lifetime expected credit losses on the asset. Expected credit losses are a probability-weighted estimate of credit losses and are measured as the present value of all cash shortfalls for financial assets that are not credit-impaired at the reporting date and as the difference between the gross carrying amount and the present value of estimated future cash flows for financial assets that are credit-impaired at the reporting date. Loss allowances for expected credit losses for financial assets measured at amortized cost are presented in the statement of financial position as a deduction from the gross carrying amount of the asset.

##### *Non-financial Assets*

The carrying amounts of the Corporation’s non-financial assets, including the water pipeline assets and royalty credits receivable, are reviewed whenever there are indicators of impairment. If any such indicators exist, the asset’s recoverable amount is estimated.

For the purpose of impairment testing, D&P assets are allocated by CGU, being the smallest group of assets that generate cash inflows from continuing use that are largely independent of the cash inflows of other assets or groups of assets. The recoverable amount of D&P assets within a CGU is the greater of its value in use and its fair value less costs of disposal.

# Canadian Spirit Resources Inc.

## Notes to the Financial Statements

For the nine months ended September 30, 2020

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### 2. SIGNIFICANT ACCOUNTING POLICIES (Continued)

#### e) Impairment (Continued)

##### *Non-financial Assets (Continued)*

In assessing fair value less costs of disposal of D&P assets within a CGU, the estimated future cash flows are discounted to their present value using an after-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. Fair value less costs of disposal is generally computed by reference to the present value of the future cash flows expected to be derived from production of proved plus probable reserves (less royalties and operating costs plus future development costs).

E&E assets are allocated by CGU and are assessed for impairment if sufficient data exists to undermine technical feasibility and commercial viability, or facts and circumstances, including comparison to comparable market transactions, suggest that the carrying amount exceeds the recoverable amount.

An impairment loss is recognized if the carrying amount of an asset or its CGU exceeds its estimated recoverable amount. Impairment losses are recognized in the statement of loss and comprehensive loss.

Impairment losses recognized in prior years are assessed at each reporting date for indicators that the loss has decreased or no longer exists. An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's or CGUs carrying amount does not exceed the carrying amount that would have been determined, net of depletion and depreciation or amortization, if no impairment loss had been recognized.

#### f) Office Equipment and Fixtures

Office equipment and fixtures, are recorded at cost and amortized on a straight-line basis over their estimated useful life (3 - 5 years).

#### g) Financial Instruments

##### *Non-derivative Financial Instruments*

Non-derivative financial instruments are comprised of cash and cash equivalents, accounts receivable, deposits, restricted deposits, accounts payable, and lease liabilities. Non-derivative financial instruments are recognized initially at fair value plus, for instruments not at fair value through profit or loss, any directly attributable transaction costs. Subsequent to initial recognition, non-derivative financial instruments are measured as described below.

Cash and cash equivalents is comprised of cash on hand, term deposits held with banks and other short-term highly liquid investments with original maturities of three months or less and are measured at amortized cost. Bank overdrafts that are repayable on demand and form an integral part of the Corporation's cash management, whereby management has the ability and intent to net bank overdrafts against cash, are included as a component of cash and cash equivalents for the purpose of the statement of cash flows.

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

#### h) Finance Income and Expenses

Finance income comprises interest and other income and is recognized in the statement of loss and comprehensive loss as it accrues using the effective interest rate.

Finance expense consists of accretion on the decommissioning liability and lease liability.

# Canadian Spirit Resources Inc.

## Notes to the Financial Statements

For the nine months ended September 30, 2020

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### 2. SIGNIFICANT ACCOUNTING POLICIES (Continued)

#### i) Loss per Share

The Corporation computes basic loss per share using net loss divided by the weighted average number of common shares outstanding during the period. The Corporation uses the treasury stock method in computing the weighted average number of diluted common shares outstanding.

This method assumes that the proceeds upon exercise of in-the-money stock options and share purchase warrants are used to repurchase the Corporation's common shares at the average market price during the relevant period. No adjustment to diluted loss per share is made if the result of this calculation is anti-dilutive.

#### j) Flow-through Shares

The Corporation has from time to time financed a portion of its exploration and development activities through the issue of flow-through shares. Under the terms of these share issuances, the related resource expenditure deductions for income tax purposes are renounced to investors. In the period the shares are issued, a premium liability is recorded if there is a difference between the offering price and the market price on the Exchange on the date of announcement of the offering. Accordingly, in the period the expenditures are incurred the premium liability is extinguished and is offset by the recording of a flow-through shares premium income item. The deferred income tax effect of both the flow-through shares renouncement and the flow-through shares premium income is reflected in the period the expenditures are incurred.

#### k) Income Taxes

Income tax expense represents the sum of current tax and deferred tax expense. Income tax is recognized in the statement of loss and comprehensive loss except to the extent it relates to items recognized directly in shareholders' capital, in which case the income tax expense is recognized in shareholders' capital. Current income taxes are measured at the amount, if any, expected to be recoverable from or payable to taxation authorities based on the income tax rates enacted or substantively enacted at the end of the reporting period. The Corporation follows the liability method of accounting for income taxes. Under this method, deferred income tax assets or liabilities are recorded to reflect differences between the accounting and tax base of assets and liabilities, and income tax loss carry-forwards. Deferred income taxes are measured using tax rates that are expected to apply to the period when the deferred tax asset is realized or deferred tax liability is settled, based on tax rates and tax laws that have been enacted or substantively enacted by the end of the reporting period. The effect of any changes in tax rates is recognized in the statement of operations in the period in which the change occurs or in shareholders' capital, depending on the nature of the item(s) affected by the adjustment. Deferred income tax assets are recognized for deductible temporary differences to the extent it is probable that future taxable profit will be available against which the deferred tax assets can be utilized.

The carrying amount of deferred income tax assets is reviewed at the end of each reporting period and reduced to the extent it is no longer probable that sufficient taxable profits will be available to allow the asset to be recovered.

#### l) Decommissioning Liability

The Corporation recognizes the estimated net present value of future decommissioning liabilities associated with E&E assets and PP&E assets as a liability in the period in which they are incurred, normally when the asset is purchased or developed. The liability is based on the estimated costs to abandon and reclaim the net ownership interest in all wells and facilities and the estimated timing of the costs to be incurred in future periods.

# Canadian Spirit Resources Inc.

## Notes to the Financial Statements

For the nine months ended September 30, 2020

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### 2. SIGNIFICANT ACCOUNTING POLICIES (Continued)

#### l) Decommissioning Liability (Continued)

This estimate is evaluated on a periodic basis and any adjustments are made to the carrying amount. The change in net present value of the future decommissioning liabilities due to the passage of time and calculated using an estimated risk-free nominal discount rate for the period is expensed as finance costs, accretion. The decommissioning cost, which is the net present value of the decommissioning liabilities at the inception of the assets, is capitalized as part of the cost of the related long-lived asset and amortized using the unit-of-production method. Actual decommissioning liabilities settled during the period reduce the decommissioning liability.

#### m) Jointly Controlled Operations

Certain of the Corporation's petroleum and natural gas operations are conducted under joint operating agreements with external parties, whereby two or more parties jointly control the assets.

These financial statements reflect the Corporation's proportionate interest in such jointly controlled assets and, upon production, a proportionate share of the relevant revenue and related operating costs.

#### n) Revenue Recognition (see Note 2(s))

Revenue from the sale of commodities, which may include natural gas, condensate and natural gas liquids are measured based on the consideration specified in contracts with customers. The Corporation recognizes revenue when it transfers control of the product to the buyer. This is generally at the time the customer obtains legal title to the product and when it is physically transferred to the custody transfer point agreed with the customer, often terminals, pipelines or other transportation methods. Payment terms for CSRI's commodity sales contracts are on the 25th of the month following delivery. CSRI does not have any contracts where the period between the transfer of the promised goods or services to the customer and payment by the customer exceeds one year and therefore the Corporation does not adjust its revenue transactions for the time value of money.

The Corporation evaluates its arrangements with third parties and partners to determine if the Corporation acts as the principal or as an agent. In making this evaluation, management considers if the Corporation obtains control of the product delivered, which is indicated by the Corporation having the primary responsibility for the delivery of the product, having the ability to establish prices or having inventory risk. If the Corporation acts in the capacity of an agent rather than as a principal in a transaction, then the revenue is recognized on a net-basis, only reflecting the fee, if any, realized by the Corporation from the transaction.

#### o) Share Purchase Warrants

In conjunction with certain financing activities the Corporation issues units, which are comprised of common shares and share purchase warrants. Share purchase warrants are accounted for using the residual method, which calculates the value of unit issuance proceeds as common shares equal to the market price on the Exchange on the date of announcement with the remainder assigned to share purchase warrants.

#### p) Share-based Compensation

The Corporation accounts for share-based compensation using the fair-value method of accounting for stock options granted using the Black-Scholes pricing model. Share-based compensation is recorded over the vesting period with a corresponding amount reflected as contributed surplus. Share-based compensation is calculated as the estimated fair value for the related stock options at the time of grant, amortized over their vesting period using graded vesting. When stock options are exercised, the associated amounts previously recorded as contributed surplus are reclassified to common shares. The amounts expensed or capitalized are adjusted for an estimated forfeiture rate for options that will not vest, which is adjusted as actual forfeitures occur, until the options are fully vested. The Corporation capitalizes, within both E&E assets and PPE&E assets, the portion of share-based compensation that is directly attributable to the respective exploration and development activity.

# Canadian Spirit Resources Inc.

## Notes to the Financial Statements

For the nine months ended September 30, 2020

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### 2. SIGNIFICANT ACCOUNTING POLICIES (Continued)

#### q) Leases

##### *Policy Applicable from January 1, 2019*

Effective January 1, 2019, the Corporation has adopted IFRS 16, “Leases” (“IFRS 16”). Refer to Note 2 (s) for policy.

##### *Policy Applicable Before January 1, 2019*

Payments made under operating leases are recognized as an expense in the statement of loss and comprehensive loss on a straight-line basis over the lease term. Lease incentives received are recognized as part of the total lease expense over the lease term.

#### r) Foreign Currency

The functional and presentation currency of the Corporation is the Canadian dollar which is the principal currency of the primary economic environment in which it operates. Monetary assets and liabilities denominated in foreign currencies are translated to Canadian dollars at the exchange rate at the end of the year. Non-monetary assets and liabilities denominated in foreign currencies that are measured at fair value are translated to the functional currency at the exchange rate at the date that the fair value was determined. Foreign currency transaction differences arising on translation are recognized in the statement of loss and comprehensive loss.

#### s) Adoption of Accounting Policies

##### *IFRS 16 Leases*

The Corporation adopted IFRS 16 effective January 1, 2019, and the standard was applied using the modified retrospective method. The modified retrospective method does not require restatement of prior period financial information as it recognizes the cumulative effect, if any, as an adjustment to opening retained earnings and applies the standard prospectively. Accordingly, comparative information in the Corporation’s financial statements are not restated and continue to be reported under IAS 17. The Corporation has applied the new standard using the modified retrospective approach. The modified retrospective approach does not require restatement of prior period financial information as it recognizes the cumulative effect as an adjustment to opening retained earnings and applies the standard prospectively. Therefore, the comparative information in the Corporation’s balance sheet, statements of loss and comprehensive loss, equity attributable to common shareholders and cash flows have not been restated.

The Corporation has elected to use the following practical expedients permitted under the standard:

- apply a single discount rate to a portfolio of leases with reasonably similar characteristics;
- account for leases with a remaining term of less than twelve months as short-term leases;
- account for leases with a low dollar value (less than \$5,000) as an expense; and
- the use of hindsight in determining the lease term where the contract contains terms to extend or terminate the lease.

On adoption of IFRS 16, the Corporation has recognized right-of-use (“ROU”) assets and a corresponding lease liability in relation to all lease arrangements, excluding commitments in relation to arrangements not containing leases (service agreements), measured at the present value of the remaining lease payments as at December 31, 2018. ROU assets and a lease liability of \$48,387 were recorded as of January 1, 2019, with no impact on the Corporation’s deficit. The ROU assets for CSRI arose from surface lease arrangements with landholders. When measuring the lease liability, the Corporation discounts lease payments using the interest rate implicit in the lease, or the Corporation’s incremental borrowing rate if the interest rate implicit in the lease cannot be readily determined. The weighted-average incremental borrowing rate applied on adoption was 12%.

# Canadian Spirit Resources Inc.

## Notes to the Financial Statements

For the nine months ended September 30, 2020

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### 2. SIGNIFICANT ACCOUNTING POLICIES (Continued)

#### s) Adoption of Accounting Policies (Continued)

##### *IFRS 16 Leases (Continued)*

The Corporation assesses new contracts at inception to determine whether it contains a lease. This assessment involves the exercise of judgement about whether the asset is specified for the Corporation, whether the Corporation obtains substantially all the economic benefits from use of that asset, and whether the Corporation has the right to direct the use of the asset.

Leases are recognized as a ROU asset with a corresponding liability at the date of which the leased asset is available for use by the Corporation. Each lease payment is allocated between the lease liability and finance expense. The finance expense is charged to the statement of comprehensive income over the lease term to produce a constant periodic rate of interest on the remaining balance of the liability for each reporting period. The ROU asset is depreciated over the shorter of the asset's useful life and the lease term on a straight-line basis.

Assets and liabilities arising from a lease are initially measured on a present value basis. Lease liabilities include the net present value of fixed payments, less any lease incentives receivable, variable lease payments that are based on an index or a rate, amounts expected to be payable by the lessee under residual value guarantees, the exercise price of a purchase option if the lessee is reasonably certain to exercise that option, and payments of penalties for terminating the lease, if the late term reflects the lessee exercising that option. It is remeasured when there is a change in the future lease payments arising from a change in an index or rate, if there is a change in the amount expected to be payable under a residual value guarantee or if there is a change in the assessment of whether the Corporation will exercise a purchase, extension or termination option that is within the control of the Corporation. The lease payments are discounted using the interest rate implicit in the lease, if that rate can be determined, or the Corporation's incremental borrowing rate.

ROU assets are measured at cost comprising of the amount of the initial measurement of lease liability, any lease payments made at or before the commencement date, any initial direct costs and restoration costs.

A lease modification will be accounted for as a separate lease if the modification increases the scope of the lease and if the consideration for the lease increases by an amount commensurate with the stand-alone price for the increase in scope. For a modification that is not a separate lease or where the increase in consideration is not commensurate, at the effective date of the lease modification, the Corporation will remeasure the lease liability using the Corporation's incremental borrowing rate, when the rate implicit to the lease is not readily available, with a corresponding adjustment to the ROU asset. A modification that decreases the scope of the lease will be accounted for by decreasing the carrying amount of the ROU asset, and recognizing a gain or loss in net income and comprehensive income that reflects the proportionate decrease in scope.

##### *IFRS 3 - Business Combinations ("IFRS 3")*

The Corporation adopted IFRS 3 effective January 1, 2020. The standard has been amended to revise the definition of a business to include an input and a substantive process that together significantly contribute to the ability to create outputs. The amendment to IFRS 3 had no impact for the Corporation.

##### *IAS 1 - Presentation of financial statements ("IAS 1") and IAS 8 - Accounting policies, changes in accounting estimates and errors ("IAS 8")*

The Corporation adopted IAS 1 and IAS 8 effective January 1, 2020. IAS 1 and IAS 8 have been amended to (i) use a consistent definition of materiality throughout IFRSs and the Conceptual Framework for Financial Reporting; (ii) clarify the explanation of the definition of material; and (iii) incorporate guidance in IAS 1 regarding immaterial information. These amendments had no impact for the Corporation.

# Canadian Spirit Resources Inc.

## Notes to the Financial Statements

For the nine months ended September 30, 2020

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### 3. MANAGEMENT JUDGMENTS AND ESTIMATION UNCERTAINTY

The preparation of the financial statements in accordance with IFRS requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities as at the dates of the financial statements and the reported amounts of revenues and expenses during the reported periods. Actual results could differ materially from those estimates and assumptions.

The estimates and underlying assumptions are reviewed by management on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimate is revised if the revision affects only that period or in the period of the revision and future periods if the revision affects both current and future periods.

The areas involving a higher degree of judgment or complexity, or where assumptions and estimates are significant to the financial statements include:

- reserves base;
- determination of cash generating units (CGU's);
- impairment indicators and calculation of impairment;
- decommissioning liability; and
- going concern assumption.

#### **Reserves base**

Reserve estimates impact a number of estimates made by the Corporation, including the valuation of petroleum and natural gas properties and the calculations of depletion and depreciation.

The effects of changes in estimates on the unit of production calculations are accounted for prospectively over the estimated remaining recoverable reserves.

Independent reservoir engineering consultants are retained to evaluate the Corporation's recoverable reserves and to prepare an evaluation report at least annually. Reserves evaluation requires significant judgments to be made on future petroleum and natural gas prices, expected rates of production, future capital expenditures and engineering data. Future costs to develop are estimated by the independent reservoir engineers by taking into account the level of development required to produce the reserves by reference to operators, and where applicable, to internal engineers. The Corporation expects that over time its reserve estimates will be revised upward or downward based on updated information such as the results of drilling, testing and production levels. Reserves are determined pursuant to National Instrument 51-101: *Standards of Disclosure for Oil and Gas Activities*, and the Canadian Oil and Gas Evaluations Handbook.

#### **Determination of cash generating units**

The Corporation's assets are aggregated into CGUs. CGUs are based on an assessment of the unit's ability to generate independent cash inflows. The determination of these CGUs was based on management's judgment in regard to shared infrastructure, geographical proximity, stratigraphic formation type, and exposure to market risk and materiality. The Farrell Creek Montney, the Farrell Creek Gething, the Farrell Creek Montney – D&P land and the Williston Reservoir Water Pipeline have been determined to be the Corporation's CGUs.

# Canadian Spirit Resources Inc.

## Notes to the Financial Statements

For the nine months ended September 30, 2020

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### 3. MANAGEMENT JUDGMENTS AND ESTIMATION UNCERTAINTY (Continued)

#### **Impairment indicators and calculation of impairment**

At each reporting date, CSRI assesses whether (or not) there are circumstances that indicate a possibility that the carrying values of E&E assets, PP&E assets and royalty credits receivable are not recoverable, or impaired. Such circumstances include, but are not limited to, incidents of physical damage, deterioration of commodity prices, changes in the regulatory environment, a reduction in estimates of proved and probable reserves, recent transaction metrics or significant increases to expected costs to produce and transport reserves.

When management determines that circumstances indicate potential impairment, PP&E is tested for impairment by comparing the carrying values to recoverable amounts. The recoverable amount is the higher of value in use or fair value less costs of disposal. Fair value less costs of disposal is calculated as estimated future net revenue from proved plus probable reserves (less royalties and operating costs plus future development costs). If the carrying value exceeds the recoverable amount, the excess is recorded as an impairment of petroleum and natural gas properties. These calculations require the use of estimates and assumptions, that are subject to change as new information becomes available including information on future commodity prices, expected production volumes, quantity of reserves, discount rates, comparable land sales, future development costs and operating costs.

#### **Decommissioning Liability**

Decommissioning costs will be incurred by the Corporation at the end of the operating life of the Corporation's wells and facilities. The ultimate decommissioning costs are uncertain and cost estimates can vary in response to many factors including changes to relevant legal and regulatory requirements, the emergence of new restoration techniques or experience at other production sites. The expected timing and amount of expenditure can also change, for example, in response to changes in reserves or changes in laws and regulations. The Corporation selected a risk-free nominal discount rate to calculate the net present value of the future decommissioning costs.

Changes in the amount and timing of future cash outflows, the discount rate, or the inflation rate for determining future decommissioning costs could have a significant effect on the carrying amount of the decommissioning liability.

#### **Going Concern Assumption**

The Board of Directors has considered the Corporation's current activities, funding position and projected funding requirements for the period of at least twelve months from the date these financial statements, in determining the ability of the Corporation to adopt the going concern basis in preparing the financial statements for the period ended September 30, 2020. The assessment of the Corporation's ability to execute its strategy to meet its future funding requirements involves judgment.

### 4. DETERMINATION OF FAIR VALUES

A number of the Corporation's accounting policies and disclosures require the determination of fair value, for both financial and non-financial assets and liabilities. Fair values have been determined for measurement and/or disclosure purposes based on the following methods. When applicable, further information about the assumptions made in determining fair values is disclosed in the notes specific to that asset or liability.

# Canadian Spirit Resources Inc.

## Notes to the Financial Statements

For the nine months ended September 30, 2020

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### 4. DETERMINATION OF FAIR VALUES (Continued)

The Corporation's financial instruments recorded at fair value require disclosure about how the fair value was determined based on significant levels of inputs described in the following hierarchy:

- (a) Level 1: Quoted prices are available in active markets for identical assets or liabilities as of the reporting date. Active markets are those in which transactions occur in sufficient frequency and volume to provide pricing information on an ongoing basis.
- (b) Level 2: Pricing inputs are other than quoted prices in active markets included in Level 1. Prices are either directly or indirectly observable as of the reporting date. Level 2 valuations are based on inputs, including quoted forward prices for commodities, time value and volatility factors, which can be substantially observed or corroborated in the marketplace.
- (c) Level 3: Valuations in this level are those with inputs for the asset or liability that are not based on observable market data, such as used in the impairment testing models for E&E assets and PP&E assets.

#### **Exploration and Evaluation Assets and Property, Plant and Equipment**

The fair values of PP&E assets and E&E assets recognized in an acquisition are based on market values. The fair values of PP&E assets and E&E are the estimated amounts for which they could be exchanged on the acquisition date between a willing buyer and a willing seller in an arm's length transaction after proper marketing wherein the parties had each acted knowledgeably, prudently and without compulsion. The fair value of petroleum and natural gas interests included in PP&E assets is estimated with reference to the discounted cash flows expected to be derived from petroleum and natural gas production, based on externally prepared reserve reports. The risk adjusted discount rate is specific to the asset with reference to general market conditions. The fair value of petroleum and natural gas interests included in E&E assets is estimated either by measuring comparable merger and acquisition metrics and prevailing land tender prices, comparing to resource, reserve or market capitalization values, or by determining the feasible future potential development opportunities available.

#### **Cash and Cash Equivalents, Accounts Receivable, Restricted Deposits, Accounts Payable and Other Accrued Liabilities and Lease Liabilities.**

The fair value of cash and cash equivalents, accounts receivable and other accrued receivables, restricted deposits, accounts payable and other accrued liabilities and lease liabilities are estimated as the present value of future cash flows, discounted at the market rate of interest at the reporting date. At September 30, 2020 and December 31, 2019, the fair value of these balances approximated their carrying value.

#### **Stock Options**

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

### 5. RESTRICTED DEPOSITS

For operations in British Columbia, the Corporation is required to provide deposits towards future abandonment and reclamation costs based on the number of wells and facilities for which the Corporation is the primary permit holder. Based on a Liability Management Rating ("LMR") performed by the British Columbia Oil and Gas Commission ("BCOGC"), the Corporation has been assessed \$1,531,540 in aggregate as at September 30, 2020 (December 31, 2019: \$1,749,420) and these amounts are secured by cash deposits. Since these cash deposits are held against future abandonment and reclamation liabilities, the balance is considered by management to be restricted in use and is therefore classified as a non-current asset.

# Canadian Spirit Resources Inc.

## Notes to the Financial Statements

For the nine months ended September 30, 2020

### 6. EXPLORATION AND EVALUATION ASSETS

	Petroleum and Natural Gas Properties	Facilities and Equipment	Total
<b>As at December 31, 2018</b>	<b>\$ 31,763,894</b>	<b>\$ 397,466</b>	<b>\$ 32,161,360</b>
Gross additions	179,389	-	179,389
Change in decommissioning liability	(77,272)	-	(77,272)
<b>As at December 31, 2019</b>	<b>31,866,011</b>	<b>397,466</b>	<b>32,263,477</b>
Gross additions	90,569	-	90,569
<b>As at September 30, 2020</b>	<b>\$ 31,956,580</b>	<b>\$ 397,466</b>	<b>\$ 32,354,046</b>

E&E assets comprise the Corporation's exploration and evaluation projects which are pending the determination of commercial viability and technical feasibility. Exploration and evaluation expense relates to the derecognition and expiry of the historical cost of land lease exploration rights that occurred during the period, primarily for the Farrell Creek Gething area.

### 7. PROPERTY, PLANT AND EQUIPMENT

	Petroleum and Natural Gas Properties	Facilities and Equipment	Office Equipment and Fixtures	Total
<b>Cost</b>				
<b>As at December 31, 2018</b>	<b>\$ 17,242,664</b>	<b>\$ 8,888,430</b>	<b>\$ 228,198</b>	<b>\$ 26,359,292</b>
Change in decommissioning liability	(1,518)	4,346	-	2,828
<b>As at September 30, 2020 and December 31, 2019</b>	<b>\$ 17,241,146</b>	<b>\$ 8,892,776</b>	<b>\$ 228,198</b>	<b>\$ 26,362,120</b>
<b>Accumulated depletion, depreciation and impairment</b>				
<b>As at December 31, 2018</b>	<b>\$ 17,241,146</b>	<b>\$ 5,079,381</b>	<b>\$ 226,972</b>	<b>\$ 22,547,499</b>
Depletion and depreciation	-	284,752	1,226	285,978
<b>As at December 31, 2019</b>	<b>17,241,146</b>	<b>5,364,133</b>	<b>228,198</b>	<b>22,833,477</b>
Depletion and depreciation	-	213,564	-	213,564
<b>As at September 30, 2020</b>	<b>\$ 17,241,146</b>	<b>\$ 5,577,697</b>	<b>\$ 228,198</b>	<b>\$ 23,047,041</b>
<b>Carrying amounts</b>				
As at December 31, 2019	\$ -	\$ 3,528,643	-	3,528,643
As at September 30, 2020	\$ -	\$ 3,315,079	-	3,315,079

# Canadian Spirit Resources Inc.

## Notes to the Financial Statements

For the nine months ended September 30, 2020

### 7. PROPERTY, PLANT AND EQUIPMENT (Continued)

During the period ended September 30, 2020, the Corporation capitalized \$Nil (December 31, 2019 - \$Nil) of general and administrative costs within both E&E assets and PP&E assets directly related to the respective exploration and development activities. During the period ended September 30, 2020, the Corporation also capitalized \$Nil (December 31, 2019 - \$Nil) of share-based compensation for those employees of the Corporation directly involved in exploration and development activities. Included in the calculation of depletion for the period ended September 30, 2020, are future development costs of \$Nil (December 31, 2019 - \$Nil).

The Williston Reservoir Water Pipeline licence term expires on December 31, 2031, thus on a straight-line basis the Corporation has recorded depreciation for the period ended September 30, 2020 of \$213,564 (December 31, 2019: \$284,752).

During the period ended September 30, 2020, the Corporation received proceeds of \$14,450 (December 31, 2019 - \$52,942) on fully depreciated idle equipment resulting in a gain on disposition of \$14,450 (December 31, 2019 - \$52,942).

### 8. RIGHT-OF-USE ASSETS

The following is the continuity of the cost and accumulated depreciation of right-of-use assets (operating premise leases) as at and for the period ended September 30, 2020 and December 31, 2019:

	September 30, 2020	December 31, 2019
<b>Cost</b>		
<b>Balance, beginning of period</b>	\$ 48,387	\$ 48,387
<b>Accumulated depreciation</b>		
<b>Balance, end of period</b>	(5,376)	-
Depreciation	(4,032)	(5,376)
	(9,408)	(5,376)
<b>Ending balance</b>	\$ 38,979	\$ 43,011

### 9. LOAN PAYABLE

The Corporation issued to its largest shareholder, Elmag Investment Inc., a redeemable secured debenture to borrow \$600,000 with a term of one year at 10% interest per annum payable in quarterly instalments on the 15th day of each of August, November, February and May. The debenture is secured by a general security agreement and a first floating charge on the Corporation's real property and acquired rights. As at September 30, 2020, the loan balance includes accrued interest of \$10,000.

# Canadian Spirit Resources Inc.

## Notes to the Financial Statements

For the nine months ended September 30, 2020

### 10. LEASE LIABILITY

	September 30, 2020	December 31, 2019
<b>Balance, beginning of period</b>	<b>\$ 45,194</b>	<b>\$ 48,387</b>
Lease payments	(7,205)	(8,569)
Interest accretion on lease liabilities	4,032	5,376
<b>Balance, end of period</b>	<b>42,021</b>	<b>45,194</b>
Current portion	3,958	3,576
<b>Non-current portion</b>	<b>\$ 38,063</b>	<b>\$ 41,618</b>

Payments recognized in the financial statements relating to short-term leases and low-value assets for the period ended September 30, 2020 were \$17,500 (December 31, 2019: \$45,487). The Corporation's short-term leases and low-value assets consist of office leases all of which were terminated effective May 31, 2020.

### 11. IMPAIRMENT

#### E&E Assets

The Corporation performed impairment tests as at December 31, 2019 to assess the recoverable value of E&E assets of both the Corporation's Farrell Creek Montney CGU and the Farrell Creek Gething CGU. Estimates of fair value less costs of disposal for the Montney E&E assets were determined in part using merger and acquisition metrics, prevailing land tender prices in the Farrell Creek/Altares area, as well as resource and reserve values as at December 31, 2019 prepared by independent reservoir engineering consultants. Based on these and other factors, the estimated recoverable amount of the Farrell Creek Montney E&E assets was calculated to be greater than the carrying value and as such there was no impairment. As at December 31, 2019, the estimated value of facility remained unchanged and therefore no further impairment was recorded.

#### Property, Plant and Equipment

During the year ended December 31, 2018, the Corporation performed an impairment test of the Farrell Creek Montney - D&P CGU within PP&E assets under the fair value less costs of disposal model and noted that the recoverable amount was substantially below the carrying amount, and accordingly, an impairment of \$1,246,000 was recorded, which brought the Farrell Creek Montney - D&P CGU to a carrying value of \$Nil. No indicators noted to suggest a reversal of impairment should be recorded as at September 30, 2020.

As at September 30, 2020 and December 31, 2019, the Corporation determined that there was no impairment required for the 25% interest in the Williston water pipeline.

The following table summarizes the components of the impairment charges for the periods ended September 30, 2020 and December 31, 2019:

	September 30, 2020	December 31, 2019
Royalty credits	\$ -	\$ 148,595
	<b>\$ -</b>	<b>\$ 148,595</b>

# Canadian Spirit Resources Inc.

## Notes to the Financial Statements

For the nine months ended September 30, 2020

### 12. ROYALTY CREDITS

The British Columbia Ministry of Energy and Mines provides certain oil and gas drilling incentives including royalty credits.

Since CSRI's development activities have, at some point, either qualified or qualify for each of the Deep Royalty Credit Program, the Summer Drilling Credit Program and the road and pipeline facilities royalty deduction program, total credits in the amount of \$4,176,422 have been earned and recorded to date by the Corporation. The royalty credits are offset against PP&E assets and the unapplied royalty credits are subsequently drawn down as production and revenue are recognized for the wells qualifying for the royalty credits. During the period ended September 30, 2020, the Corporation applied \$Nil (December 31, 2019: \$Nil) of royalty credits against Crown royalties that would otherwise have been payable.

The Corporation assessed the future recoverability of the undrawn balance of the Deep Royalty Credits (available for use only against royalties assessed on the wells that gave rise to the credit) by comparing to the proven plus probable future cash flow forecast prepared by the Corporation's independent reserve engineers. As a result of this assessment, the Corporation recorded an impairment charge during the period of \$Nil (December 31, 2019: \$148,595).

A summary of the unapplied royalty credits available to the Corporation is as follows:

	September 30, 2020	December 31, 2019
<b>Balance, beginning of period</b>	<b>\$ 307,460</b>	<b>\$ 456,055</b>
Impairment (Note 10)	-	(148,595)
<b>Balance, end of period</b>	<b>307,460</b>	<b>307,460</b>
Current portion	-	-
<b>Non-current portion</b>	<b>\$ 307,460</b>	<b>\$ 307,460</b>

### 13. DECOMMISSIONING LIABILITY

	September 30, 2020	December 31, 2019
<b>Balance, beginning of period</b>	<b>\$ 2,060,873</b>	<b>\$ 2,350,222</b>
Changes in discount rates	6,708	142,432
Changes in estimated life and estimated future cash flows	-	(480,326)
Accretion	22,344	48,545
<b>Non-current portion</b>	<b>\$ 2,089,925</b>	<b>\$ 2,060,873</b>

# Canadian Spirit Resources Inc.

## Notes to the Financial Statements

For the nine months ended September 30, 2020

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### 13. DECOMMISSIONING LIABILITY (Continued)

The total future decommissioning liability, including costs to reclaim and abandon wells and facilities plus the years in which such costs are expected to be incurred, is estimated by management. As at September 30, 2020 the estimated total undiscounted future liability of \$2,241,444 (December 31, 2019: \$2,286,273) had a net present value of \$2,089,925 (December 31, 2019: \$2,060,873) assuming expected decommissioning payments are to be made over the next 12 years, using an estimated risk-free nominal interest rate of 1.30% (December 31, 2019: 1.30%), and an inflation rate of 2.00% (December 31, 2019: 2.00%).

The decommissioning liability is comprised of both the Corporation's proportionate interest in its jointly controlled operations as well as its own 100% operations. The restricted deposits held toward future abandonment and reclamation costs (see Note 5) as at September 30, 2020 of \$1,531,540 (December 31, 2019: \$1,749,420) are secured against the Corporation's 100% operations, where the Corporation is the primary permit holder.

The revisions to the estimated future obligation are due to the increases or decreases in the estimated risk-free nominal interest rate and changes in the abandonment and reclamation assumptions by well. Liabilities incurred relate to new wells drilled or fracture stimulated during the year, and liabilities settled refer to well-bores abandoned or well-sites reclaimed during the year. During the period ended September 30, 2020, financing costs of \$22,344 (December 31, 2019: \$48,545) relate to the accretion of the decommissioning liability.

### 14. SHAREHOLDERS' CAPITAL

#### Common Shares

The Corporation has authorized share capital of an unlimited number of common shares with no par value.

The issued and outstanding common shares of the Corporation:

- no changes for the period ended September 30, 2020; and
- no changes for the year ended December 31, 2019.

#### Share Purchase Warrants

The Corporation had no share purchase warrants outstanding as at September 30, 2020 and December 31, 2019.

### 15. SHARE-BASED COMPENSATION PLANS

#### Stock Options

The Corporation has a 10% rolling stock option plan for directors, executive officers, employees and consultants which provides for the granting of options to acquire common shares. Under the terms of the plan, options vest over periods as determined by the Board of Directors of the Corporation and expire to a maximum of five years. The number of common shares available for grant of additional options under the plan as at September 30, 2020 was 17,767,758 (December 31, 2019: 14,592,758).

# Canadian Spirit Resources Inc.

## Notes to the Financial Statements

For the nine months ended September 30, 2020

### 15. SHARE-BASED COMPENSATION PLANS (Continued)

As at September 30, 2020, options to acquire 1,850,000 (December 31, 2019: 5,025,000) common shares were outstanding of which 1,100,000 (December 31, 2019: 4,631,250) had vested and 750,000 (December 31, 2019: 393,750) remained unvested, as follows:

	For the period ended September 30, 2020		For the year ended December 31, 2019	
	Number of Options	Weighted Avg. Exercise Price	Number of Options	Weighted Avg. Exercise Price
<b>Balance, beginning of year</b>	<b>5,025,000</b>	<b>\$ 0.13</b>	<b>6,298,000</b>	<b>\$ 0.17</b>
Expired	(4,175,000)	0.13	(1,273,000)	(0.32)
Granted	1,000,000	0.05	-	-
<b>Balance, end of period</b>	<b>1,850,000</b>	<b>\$ 0.08</b>	<b>5,025,000</b>	<b>\$ 0.13</b>
<b>Options exercisable, end of period</b>	<b>1,100,000</b>	<b>\$ 0.105</b>	<b>4,631,250</b>	<b>\$ 0.13</b>

The following table summarizes the information about stock options outstanding as at September 30, 2020 and December 31, 2019:

Expiry Date	Exercise Price	For the period ended September 30, 2020		For the year ended December 31, 2019	
		Number of Options Outstanding	Remaining Contractual Life (in years)	Number of Options Outstanding	Remaining Contractual Life (in years)
January 17, 2021	\$ 0.20	100,000	0.30	1,200,000	1.05
August 21, 2022	0.12	375,000	1.89	1,625,000	2.64
August 28, 2023	0.10	375,000	2.91	1,900,000	3.66
November 27, 2023	0.10	-	-	300,000	3.91
August 30, 2025	0.05	1,000,000	4.92	-	-
	<b>0.08</b>	<b>1,850,000</b>	<b>3.65</b>	<b>5,025,000</b>	<b>2.72</b>

The following table summarizes the information about stock options vested as at September 30, 2020 and December 31, 2019:

Expiry Date	Exercise Price	For the period ended September 30, 2020		For the year ended December 31, 2019	
		Number of Options Vested	Remaining Contractual Life (in years)	Number of Options Vested	Remaining Contractual Life (in years)
January 17, 2021	\$ 0.20	100,000	0.30	1,200,000	1.05
August 21, 2022	0.12	375,000	1.89	1,625,000	2.64
August 28, 2023	0.10	375,000	2.91	1,831,250	3.66
November 27, 2023	0.10	-	-	225,000	3.91
August 30, 2025	0.05	250,000	4.92	-	-
	<b>\$ 0.105</b>	<b>1,100,000</b>	<b>2.78</b>	<b>4,881,250</b>	<b>2.69</b>

# Canadian Spirit Resources Inc.

## Notes to the Financial Statements

For the nine months ended September 30, 2020

### 15. SHARE-BASED COMPENSATION PLANS (Continued)

During the period ended September 30, 2019, the Company granted 1,000,000 (December 31, 2019: Nil) stock options with an estimated weighted average fair value of \$0.045 (December 31, 2019: \$Nil) calculated using the Black-Scholes option pricing model. The fair value of stock options vested during the year and recognized as share-based payments expense was \$16,527 (December 31, 2019: \$50,702).

Option pricing models require the use of estimates and assumptions including the expected volatility. Changes in underlying assumptions can materially affect the fair value estimates. The following weighted average assumptions were used for the Black-Scholes valuation of options granted during the year:

	September 30, 2020
Share price	\$0.065
Risk-free interest rate	1.00%
Expected life of options	5 years
Annualized volatility based on historical volatility	80.31%
Dividend rate	0.00%
Forfeiture rate	0.00%
Fair value per option	\$0.45
Exercise price	\$0.05

\* Annualized volatility was determined by reference to historic volatility of the Company.

### 16. PER SHARE AMOUNTS

Per share amounts have been calculated on the weighted average number of shares outstanding. The weighted average shares outstanding for the period ended September 30, 2020 was 196,177,583 (September 30, 2019: 196,177,583).

The diluted loss per share calculations for the periods ended September 30, 2020 and 2019 were not affected by the outstanding stock options as they are anti-dilutive.

### 17. DEFERRED INCOME TAXES

The reconciliations of deferred income tax recovery as computed by applying the combined Canadian Federal and Provincial statutory income tax rates to net losses are as follows:

	December 31, 2019
Net loss and comprehensive loss	\$ (1,421,434)
Statutory income tax rate	27.0%
Expected deferred income tax recovery	(383,787)
Deferred income tax effects of:	
Non-deductible share-based compensation	13,690
Non-deductible expenses	221
Effect of change in statutory income tax rate	-
Unrecognized income tax benefits	369,876
Recovery of deferred income taxes	\$ -

# Canadian Spirit Resources Inc.

## Notes to the Financial Statements

For the nine months ended September 30, 2020

### 17. DEFERRED INCOME TAXES (Continued)

The Corporation has not recorded deferred tax assets arising from the excess of income tax bases over carrying value due to the uncertainty related to the realization of such assets. As at December 31, 2019 and 2018, no deferred tax assets were recognized in the statements of financial position for the following deductible temporary differences:

	December 31, 2019
Property, plant and equipment	\$ 14,880,366
Decommissioning liability	2,060,873
Right-of-use asset	(43,011)
Lease liability	45,194
Share issue costs	83,235
Capital losses carried forward	25,932
Non-capital losses	52,714,657
	<u>\$ 69,767,246</u>

At December 31, 2019, the Corporation has an approximate tax bases of \$102,998,476 available for deduction against future taxable income. The Corporation has non-capital losses of \$52,714,657 that will expire between 2027 and 2039.

### 18. FINANCIAL RISK MANAGEMENT

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

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

Credit risk is the risk of financial loss to the Corporation if a counterparty to a financial instrument fails to meet its contractual obligations. The maximum exposure to credit risk at September 30, 2020 and December 31, 2019 is the carrying amount of the Corporation's accounts receivable balances.

# Canadian Spirit Resources Inc.

## Notes to the Financial Statements

For the nine months ended September 30, 2020

### 18. FINANCIAL RISK MANAGEMENT (Continued)

The following summarized the Corporation's accounts receivable as at September 30, 2020 and December 31, 2019:

	September 30, 2020	December 31, 2019
Joint venture	\$ -	\$ 20,493
GST and other	8,506	7,198
	<b>\$ 8,506</b>	<b>\$ 27,691</b>

The Corporation did not incur any write-offs relating to accounts receivable balances during the periods ended September 30, 2020 and December 31, 2019. Accounts receivable at September 30, 2020 and December 31, 2019 were all current. Any receivables from natural gas marketers are normally collected on the 25<sup>th</sup> day of the month following production. The Corporation's policy to mitigate credit risk associated with these balances is to establish marketing relationships with large purchasers.

The Corporation applies the simplified approach to providing for expected credit losses prescribed by IFRS 9 which permits the use of the lifetime expected loss provision for all trade receivables. The Corporation historically has not experienced any collection issues with its natural gas marketer. Receivables from joint venture partners are typically collected within one to two months of the joint venture bill being issued. However, the accounts receivable 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, escalating costs and the risk of unsuccessful drilling. In addition, further risk exists with joint venture partners if a disagreement were to arise, which may increase the potential for non-collection.

Market risk is the risk that changes in market indices, such as foreign exchange rates, interest rates and commodity prices, will affect the Corporation's income, cash flow, or the value of its held financial instruments. The Corporation has a loan liability, holds its cash and cash equivalents in the form of bank deposits and has limited dealings with foreign currency exchange, the Corporation's exposure to market risk is currently minimal and dependant on interest rates on its bank deposits its outstanding loan liability. The Corporation is exposed to commodity price risk from the production and sale of natural gas, which is sold at prevailing market prices. There are no forward sales contracts and the Corporation does not currently engage in price hedging activities.

Liquidity risk is the risk that the Corporation will not be able to meet its obligations as they become due. CSRI manages its liquidity risk by synchronizing its forecasted cash requirements for operations with its anticipated capital financing activities and maintaining significant cash balances. The impacts on the Corporation's liquidity risk due to current equity and commodity price market conditions include: a) increased uncertainty in raising additional funds on reasonable terms for future capital projects; and b) a reduction in the Corporation's ability to generate sufficient revenues from the sale of natural gas to cover administrative and operating costs. See Note 1 for further discussion regarding the Corporation's ability to operate as a going concern.

# Canadian Spirit Resources Inc.

## Notes to the Financial Statements

For the nine months ended September 30, 2020

### 19. CAPITAL MANAGEMENT

The Corporation defines capital as shareholders' capital plus working capital based on the Corporation's financial statements as follows:

	September 30, 2020	December 31, 2019
Working capital:		
Current assets	\$ 650,784	\$ 703,063
Current liabilities	(1,307,465)	(114,738)
	(656,681)	588,325
Shareholders' Equity	34,762,435	36,377,845
	<b>\$ 34,105,754</b>	<b>\$ 36,966,170</b>

The current objectives of the capital management process are to maximize long term shareholder value by (i) ensuring sufficient funding to enable the Corporation's unconventional natural gas resource project to reach the stage of reserves, production and cash flows and by (ii) minimizing the Corporation's cost of capital consistent with a low level of financial and liquidity risk.

The policies followed by the Corporation in managing its capital include:

- (a) targeting a minimum working capital position that covers all budgeted capital commitments, anticipated administration and field operating costs for a minimum period of three months, current reclamation obligations, and other non-contingent financial liabilities;
- (b) funding 100% of capital requirements through the issue of equity instruments and debt instruments until such time as cash generated from operations exceeds anticipated overhead expenses prior to capitalization; and
- (c) holding the proceeds of equity and funding in deposit accounts of major financial institutions providing for immediate access.

The Corporation manages its capital by continuously monitoring the quality and level of working capital and the amount of its financial commitments and current obligations. An annual funding plan is approved by the Board of Directors in conjunction with the capital budget process and capital commitments are made based on a quarterly budget review and approval process (see Note 1 – Going Concern). The capital management process takes into account exploration and development results, economic conditions, cost inflation, commodity prices and capital market conditions.

The Corporation manages its liquidity risk by synchronizing its forecasted cash requirements for operations with its anticipated capital financing activities and maintaining significant cash balances. In order to finance the Corporation's capital programs and to cover administrative and overhead expenses, the Corporation is reducing its overall expenses and will be seeking equity and/or debt financing. Many factors influence the Corporation's ability to raise funds, including the health of the resource market, the climate for investment, the Corporation's track record, and the experience and caliber of its management.

# Canadian Spirit Resources Inc.

## Notes to the Financial Statements

For the nine months ended September 30, 2020

### 20. GENERAL AND ADMINISTRATIVE

#### General and Administrative Expenses (“G&A”)

	Three months ended		Nine months ended	
	September 30, 2020	September 30, 2019	September 30, 2020	September 30, 2019
Salaries, incentives and benefits	\$ -	\$ 129,147	\$ 164,537	\$ 403,191
Office premises and insurance	10,832	28,908	49,306	80,931
Professional fees	60,428	29,362	162,096	74,374
Consulting fees	84,273	9,100	210,931	34,375
Directors’ fees	8,000	16,000	13,000	41,333
Office supplies and software licences	7,106	10,896	20,667	39,471
Investor relations and filing fees	4,578	4,247	19,646	24,323
Interest	18,261	-	25,000	-
Staffing costs	707	3,233	733	12,083
Other expenses	1,536	411	8,101	946
	\$ 195,721	\$ 231,304	\$ 674,017	\$ 711,027

#### Executive Compensation

Executive compensation relates to amounts paid to or earned by executive officers and fees paid and/or accrued to non-executive directors, and also includes non-cash share-based compensation as follows:

	September 30, 2020	September 30, 2019
Salaries, incentives and benefits	\$ 150,241	\$ 342,948
Professional fees (non-executive)	28,093	17,850
Professional fees (executive)	63,000	-
Share-based compensation, gross	16,527	38,295
Directors’ fees	13,000	41,333
	\$ 270,861	\$ 440,426

In the case of a change of control or the termination of employment of two of the Corporation’s executive officers there was a \$514,552 commitment as at March 31, 2020, (December 31, 2019: \$514,552). The Corporation terminated the employment of such executive officers in April 2020 and is negotiating settlements of the \$514,552 commitment. The Company may or may not be successful in negotiating a lesser amount and as such accrued the \$514,522 in the Statements of Loss and Comprehensive Loss during the period ended June 30, 2020.

# Canadian Spirit Resources Inc.

## Notes to the Financial Statements

For the nine months ended September 30, 2020

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### 21. RELATED PARTY TRANSACTIONS

Transactions with related parties are recorded at exchange amounts for services provided. During the periods ended September 30, 2020 and 2019, the transactions the Corporation had with its directors, related persons or controlled entities in the normal course of business are as follows:

The Corporation retains Jeffrey E. Dyck Professional Corporation (“DyckCorp”) to provide legal, director and corporate secretary services. During the period ended September 30, 2020, the Corporation incurred \$29,498 (September 30, 2019: \$18,690) of total fees and disbursements, including taxes, from DyckCorp. Such fees have been recorded at amounts agreed upon by the respective parties. As at September 30, 2020 an accounts payable balance of \$Nil (December 31, 2019: \$6,552) was outstanding to DyckCorp.

### 22. SUBSEQUENT EVENTS

- In November 2020, the Company issued 20,000,000 units at \$0.05 per share for gross proceeds of \$1,000,000. Each unit consisted of a common share and warrant exercisable into a common share at a price of \$0.08 for 2 years. The offering was taken by a related party transaction under Multilateral Instrument 61-101, where Elmag Investments Inc. (Investissements Elmag Inc.), an insider and control entity of the corporation was be exempt from the formal valuation and minority shareholder approval requirements of MI 61-101 as the fair market value of the insider's participation in the offering did not exceed 25 per cent of the corporation's market capitalization.
- In November 2020, the Company settled its \$600,000 debenture by issued 12,000,000 shares at \$0.05 per share. The debenture was with a related party where Elmag Investments Inc. (Investissements Elmag Inc.), an insider and control entity of the corporation was be exempt from the formal valuation and minority shareholder approval requirements of MI 61-101 as the fair market value of the insider's participation in the offering did not exceed 25 per cent of the corporation's market capitalization.
- Significant declines in petroleum and natural gas prices and in stock market values at times have occurred for various reasons linked to the Coronavirus pandemic and other conditions impacting worldwide petroleum and natural gas prices. The impairment tests for the Corporation’s petroleum and gas assets are based on fair value less costs of disposal. As required by IFRS, the Corporation has not reflected these conditions in the recoverable amount estimates of the Corporation’s assets as at September 30, 2020. However, impairment indicators for the Corporation’s PP&E and E&E assets could exist subsequent to Subsequent 30, 2020, if current conditions persist. Management continues to work on revisions to the Corporation's forecasts and development plans in light of the current conditions and will use these updated assumptions and forecasts in the Corporation’s impairment indicator analysis and for impairment tests in the fourth quarter of 2020, if such tests are required.