

XXL ENERGY CORP.

Consolidated Financial Statements December 31, 2021 and 2020 (Expressed in US Dollars)

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INDEPENDENT AUDITORS' REPORT

TO THE SHAREHOLDERS OF XXL ENERGY CORP.

Opinion

We have audited the consolidated financial statements of XXL Energy Corp. and its subsidiary (the "Company"), which comprise:

- ♦ the consolidated statements of financial position as at December 31, 2021 and 2020;
- ♦ the consolidated statements of operations and comprehensive loss for the years then ended;
- ♦ the consolidated statements of changes in shareholders' deficiency for the years then ended;
- ♦ the consolidated statements of cash flows for the years then ended; and
- ♦ the notes to the consolidated financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the consolidated financial position of the Company as at December 31, 2021 and 2020, and its consolidated financial performance and its consolidated cash flows for the years then ended in accordance with International Financial Reporting Standards ("IFRS").

Basis for Opinion

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

Material Uncertainty Related to Going Concern

We draw attention to note 1 in the consolidated financial statements, which indicates that the Company incurred a net loss of \$2,910,708 during the year ended December 31, 2021 and, as of that date, had an accumulated deficit of \$119,511,406. As stated in note 1, these events or conditions, along with other matters as set forth in note 1, indicate that a material uncertainty exists that may cast significant doubt on the Company's ability to continue as a going concern. Our opinion is not modified in respect of this matter.

Other Information

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

Our opinion on the consolidated financial statements does not cover the other information and we do not express any form of assurance conclusion thereon. In connection with our audits of the consolidated financial statements, our responsibility is to read the other information identified above and, in doing so, consider whether the other information is materially inconsistent with the consolidated financial statements or our knowledge obtained in the audits, and remain alert for indications that the other information appears to be materially misstated.

We obtained Management's Discussion and Analysis prior to the date of this auditors' report. If, based on the work we have performed on this other information, we conclude that there is a material misstatement of this other information, we are required to report that fact in this auditors' report. We have nothing to report in this regard.

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

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

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

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

Auditors' Responsibilities for the Audit of the Consolidated Financial Statements

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

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

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- ♦ Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Company to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

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

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

The engagement partner on the audit resulting in this independent auditors' report is Michelle Chi Wai So.

Smythe LLP

Chartered Professional Accountants

Vancouver, British Columbia
April 22, 2022

Vancouver

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XXL Energy Corp.
Consolidated Statements of Financial Position
As at December 31,
(Expressed in US dollars)

| | Notes | 2021 | 2020 |
|--|-----------|---------------|---------------|
| ASSETS | | | |
| Current assets | | | |
| Cash | | \$ 650,008 | \$ 328,926 |
| Accounts receivable | 7 | 375,604 | 347,014 |
| Prepaid expenses | | 754 | 752 |
| | | 1,026,366 | 676,692 |
| Non-current assets | | | |
| Reclamation bond | 10 | 25,000 | 25,000 |
| Exploration and evaluation assets | 8 | 29,542 | 29,542 |
| Developed and producing properties | 8, 12, 13 | 4,010,234 | 3,810,188 |
| | | \$ 5,091,142 | \$ 4,541,422 |
| LIABILITIES AND EQUITY | | | |
| Current liabilities | | | |
| Accounts payable and accrued liabilities | | \$ 425,707 | \$ 506,727 |
| Loan payable | 12 | 502,528 | 731,311 |
| Loans payable to related parties | 13 | 33,403,099 | 29,651,061 |
| Due to related parties | 14 | 1,281,559 | 1,274,093 |
| | | 35,612,893 | 32,163,192 |
| Non-current liabilities | | | |
| Loans payable | 12 | 1,100,085 | 1,603,340 |
| Loans payable to related party | 13 | 553,450 | 544,871 |
| Decommissioning obligations | 9 | 1,340,476 | 801,618 |
| | | 38,606,904 | 35,113,021 |
| SHAREHOLDERS' DEFICIENCY | | | |
| Capital stock | 11 | 85,314,772 | 85,314,772 |
| Contributed surplus | 13 | (293,163) | (293,163) |
| Translation reserve | | 974,035 | 1,007,490 |
| Deficit | | (119,511,406) | (116,600,698) |
| | | (33,515,762) | (30,571,599) |
| | | \$ 5,091,142 | \$ 4,541,422 |

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

Approved on behalf of the Board:

"Alistair Palmer"
Director

"Fletcher FitzGibbon"
Director

XXL Energy Corp.

Consolidated Statements Operations and Comprehensive Loss

Years Ended December 31,

(Expressed in US dollars)

| | Notes | 2021 | 2020 |
|--|-------|--------------------|--------------------|
| Revenue | | | |
| Petroleum and natural gas sales | | \$ 3,307,256 | \$ 2,130,779 |
| Royalties | | (821,451) | (634,729) |
| | | 2,485,805 | 1,496,050 |
| Direct Operating Expenses | | | |
| Production | | 947,323 | 793,258 |
| Depletion and depreciation | 8 | 343,295 | 1,434,791 |
| | | 1,290,618 | 2,228,049 |
| Operating Income (loss) | | | |
| | | 1,195,187 | (731,999) |
| General and Administrative Expenses | | | |
| Finance | 13 | 3,858,393 | 3,529,501 |
| General and administrative fees | 14 | 102,172 | 99,438 |
| Foreign exchange gain | | (1,228) | (17,405) |
| Professional fees | | 120,824 | 126,236 |
| Filing and transfer agent fees | | 11,973 | 12,243 |
| Director and officer fees | 14 | 13,761 | 13,418 |
| | | 4,105,895 | 3,763,431 |
| Other Income (Loss) | | | |
| Impairment of developed and producing properties | 8 | - | (4,916,493) |
| Impairment of exploration and evaluation assets | 8 | - | (108,309) |
| Recovery of accounts payable | | - | 406,922 |
| | | - | (4,617,880) |
| Net Loss for the Year | | | |
| | | (2,910,708) | (9,113,310) |
| Other Comprehensive Loss | | | |
| Items that may be reclassified subsequently to profit or loss | | | |
| Foreign exchange gain (loss) on translating foreign operations | | \$ (33,455) | (229,385) |
| Total Comprehensive Loss for the Year | | | |
| | | (2,944,163) | (9,342,695) |
| Basic and Diluted Loss Per Share | | | |
| | | \$ (0.40) | \$ (1.26) |
| Weighted Average Number of Common Shares Outstanding | | | |
| | | 7,252,943 | 7,252,943 |

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

XXL Energy Corp.
Consolidated Statements of Changes in Shareholders' Deficiency

(Expressed in US dollars)

| | Capital Stock | | Contributed Surplus | Translation Reserve | Deficit | Total |
|--|---------------------|----------------------|------------------------|------------------------|-------------------------|------------------------|
| | Number of Shares | Amount | | | | |
| Balance as at December 31, 2019 | 7,252,943 | \$ 85,314,772 | \$ (293,163) | \$ 1,236,875 | \$ (107,487,388) | \$ (21,228,904) |
| Foreign exchange gain on translating foreign operations | - | - | - | (229,385) | - | (229,385) |
| Net loss for the year | - | - | - | - | (9,113,310) | (9,113,310) |
| Balance as at December 31, 2020 | 7,252,943 | \$ 85,314,772 | \$ (293,163) | \$ 1,007,490 | \$ (116,600,698) | \$ (30,571,599) |

| | Capital Stock | | Contributed Surplus | Translation Reserve | Deficit | Total |
|--|---------------------|----------------------|------------------------|------------------------|-------------------------|------------------------|
| | Number of Shares | Amount | | | | |
| Balance as at December 31, 2020 | 7,252,943 | \$ 85,314,772 | \$ (293,163) | \$ 1,007,490 | \$ (116,600,698) | \$ (30,571,599) |
| Foreign exchange loss on translating foreign operations | - | - | - | (33,455) | - | (33,455) |
| Net loss for the year | - | - | - | - | (2,910,708) | (2,910,708) |
| Balance as at December 31, 2021 | 7,252,943 | \$ 85,314,772 | \$ (293,163) | \$ 974,035 | \$ (119,511,406) | \$ (33,515,762) |

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

XXL Energy Corp.
Consolidated Statements of Cash Flows
Years Ended December 31,
(Expressed in US dollars)

| | 2021 | 2020 |
|---|-------------------|-------------------|
| Cash Provided by (Used in): | | |
| Operating Activities | | |
| Net income (loss) for the year | \$ (2,910,708) | \$ (9,113,310) |
| Adjustments for items not involving cash | | |
| Depletion and depreciation | 343,295 | 1,434,791 |
| Impairment of exploration and evaluation assets | - | 108,309 |
| Impairment of developed and producing properties | - | 4,916,493 |
| Recovery of accounts payable | - | (406,922) |
| Unrealized foreign exchange gain | (60,680) | (49,919) |
| Accrued finance fees on loans payable | 3,858,393 | 3,340,070 |
| | 1,230,300 | 229,512 |
| Changes in non-cash working capital | | |
| Accounts receivable | (28,576) | 32,955 |
| Prepaid expenses | (2) | (16) |
| Accounts payable and accrued liabilities | (85,506) | 9,667 |
| Due to related parties | (58,724) | (24,009) |
| Cash Provided by Operating Activities | 1,057,492 | 248,109 |
| Investing Activity | | |
| Expenditures on petroleum and natural gas properties | (4,483) | (22,538) |
| Cash Used in Investing Activity | (4,483) | (22,538) |
| Financing Activity | | |
| Payments on loan payable | (732,038) | (940,349) |
| Proceeds from loan payable | - | 200,000 |
| Cash Used in Financing Activities | (732,038) | (740,349) |
| Foreign Exchange Effect on Cash | 111 | 1,738 |
| Change in Cash During the Year | 321,082 | (513,040) |
| Cash, Beginning of the Year | 328,926 | 841,966 |
| Cash, End of the Year | \$ 650,008 | \$ 328,926 |
| Supplemental cash flow information | | |
| Petroleum and natural gas interest - revision of estimates relating to decommissioning obligation (notes 8, 9) | \$ 538,160 | \$ (20,834) |

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

XXL Energy Corp.

Notes to the Consolidated Financial Statements

For the Years Ended December 31, 2021 and 2020

(Expressed in US dollars, unless otherwise noted)

1. NATURE OF OPERATIONS AND GOING CONCERN

XXL Energy Corp. (the “Company” or “XXL Energy”) is a petroleum and natural gas entity engaged in the acquisition, exploration and development of petroleum and natural gas properties located in the United States of America.

The Company is a publicly listed company incorporated in Canada with limited liability under the legislation of the province of British Columbia. The Company’s shares are listed on the TSX Venture Exchange.

The records of the Company are located at 1500 West 16th Avenue, Vancouver, British Columbia, Canada, V6J 2L6. The Company’s registered address is 595 Howe Street, Suite 700, Vancouver, British Columbia, Canada, V6C 2T5.

These consolidated financial statements have been prepared on a going concern basis, which assumes that the Company will be able to continue in operation for the foreseeable future and will be able to realize its assets and discharge its liabilities and commitments in the normal course of business.

The Company incurred a net loss of \$2,910,708 (2020 - \$9,113,310) during the year ended December 31, 2021, and as at December 31, 2021 has a working capital deficit of \$34,586,527 (2020 - \$31,486,500), an accumulated deficit of \$119,511,406 (2020 - \$116,600,698), limited resources, no significant source of operating cash flow, and no assurances that sufficient funding will be available to maintain or conduct further exploration and development of its petroleum and natural gas interests. The Company will require additional equity and/or debt financing to meet its administrative overhead costs, to continue exploration work on its petroleum and natural gas interests and settle its current and long-term liabilities.

The application of the going concern concept is dependent upon the Company’s ability to generate future profitable operations and receive continued financial support from its shareholders, related parties and from continued forbearance from debt holders. Management is actively seeking to raise the necessary capital to meet its funding requirements and has undertaken available cost-cutting measures. There can be no assurance that management’s plan will be successful.

The outbreak of the novel strain of coronavirus, specifically identified as “COVID-19”, resulted in governments worldwide enacting emergency measures to combat the spread of the virus. These measures included the implementation of travel bans, self-imposed quarantine periods and physical distancing. This created a dramatic slowdown in the global economy and global energy consumption had been materially impacted which resulted in lower oil and natural gas prices throughout the globe, including Canada and the United States. As a result of unprecedented energy prices, many energy companies shut-in their production until better commodity prices could be realized or were impacted by impairment indicators of their petroleum and natural gas assets. The duration and impact of the COVID-19 outbreak is unknown at this time, as is the efficacy of the government and central bank interventions. It is not possible to reliably estimate the length and severity of these developments and the impact on the financial results and condition of the Company in future periods.

The Company’s business and results of operations may be further negatively affected by economic and other consequences from Russia’s military action against Ukraine and the sanctions imposed in response in late February 2022. Certain countries, including Canada and the United States, have imposed strict financial and trade sanctions against Russia, which may have far reaching effects on the global economy. Russia is a major exporter of oil and natural gas; therefore, disruption of supplies of oil and natural gas from Russia could cause a significant worldwide supply shortage of oil and natural gas and have a significant impact on worldwide prices of oil and natural gas. The long-term impacts of the conflict and the sanctions imposed on Russia remain uncertain.

XXL Energy Corp.
Notes to the Consolidated Financial Statements
For the Years Ended December 31, 2021 and 2020

(Expressed in US dollars, unless otherwise noted)

1. NATURE OF OPERATIONS AND GOING CONCERN (continued)

These matters indicate material uncertainties that may cast significant doubt about the Company's ability to continue as a going concern. These consolidated financial statements do not include any adjustments relating to the recoverability of assets and classification of assets and liabilities that might be necessary should the Company be unable to continue as a going concern. Such adjustments could be material.

2. BASIS OF PREPARATION

(a) Statement of compliance

These consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS"), as issued by the International Accounting Standards Board ("IASB").

The accounting policies set out in note 3 have been applied consistently to all periods presented by the Company and its subsidiary, Exxel Energy (USA) Inc. ("Exxel Energy").

(b) Basis of measurement

These consolidated financial statements have been prepared on a historical cost basis, except for certain financial instruments, which are measured at fair value. In addition, these consolidated financial statements have been prepared using the accrual basis of accounting, except for cash flow information.

(c) Functional and presentation currency

The functional currency of the Company is the Canadian dollar. The functional currency of Exxel Energy is the US dollar. These consolidated financial statements are presented in US dollars.

(d) Use of estimates and judgments

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

Following are the accounting policies subject to such judgments and the key sources of estimation uncertainty that the Company believes could have the most significant impact on the reported results and financial position.

XXL Energy Corp.
Notes to the Consolidated Financial Statements
For the Years Ended December 31, 2021 and 2020

(Expressed in US dollars, unless otherwise noted)

2. BASIS OF PREPARATION (continued)

(d) Use of estimates and judgments (continued)

Critical accounting judgments

Reserves

The estimate of petroleum and natural gas reserves is integral to the calculation of the amount of depletion charged to the consolidated statements of operations and comprehensive loss and is also a key determinant in assessing whether the carrying value of any of the Company's development and production assets have been impaired. Changes in reported reserves can impact asset carrying values and the decommissioning provision due to changes in expected future cash flows. The Company's reserves are evaluated and reported on by independent reserve engineers at least annually in accordance with Canadian Securities Administrators' National Instrument 51-101 *Standards of Disclosure of Oil and Gas Activities*. Reserve estimation is based on a variety of factors including engineering data, geological and geophysical data, projected future rates of production, commodity pricing and timing of future expenditures, all of which are subject to significant judgment and interpretation.

Identification of cash-generating units ("CGUs")

The Company's assets are aggregated into CGUs for the purpose of calculating impairment. 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 with regard to shared infrastructure, geographical proximity, petroleum type and similar exposure to market risk and materiality.

Recoverability of long-lived asset values

At each reporting date, the Company assesses its petroleum and natural gas properties and exploration and evaluation assets for possible impairment, to determine if there is any indication that the carrying amounts of the assets may not be recoverable. An assessment is also made at each reporting date to determine whether there is an indication that previously recognized impairment losses no longer exist or have decreased. Determination as to whether and how much an asset is impaired or no longer impaired, involves management estimates on highly uncertain matters, such as future commodity prices, discount rates, production profiles, operating costs, future capital costs and reserves. Changes in circumstances may impact these estimates, which may impact the recoverable amount of assets. Any change in the impairment loss or reversal of impairment loss could have a material financial impact in future periods, but future depletion expense would be impacted as a result.

Going concern

The assessment of whether the going concern assumption is appropriate requires management to take into account all available information about the future, which is at least, but not limited to, twelve months from the end of the reporting period. The Company is aware that material uncertainties related to events or conditions may cast significant doubt upon the Company's ability to continue as a going concern.

XXL Energy Corp.
Notes to the Consolidated Financial Statements
For the Years Ended December 31, 2021 and 2020

(Expressed in US dollars, unless otherwise noted)

2. BASIS OF PRESENTATION (continued)

(d) Use of estimates and judgments (continued)

Critical accounting judgments (continued)

Joint arrangements

Judgment is required to determine when the Company has joint control over an arrangement, which requires an assessment of the relevant activities and when the decisions in relation to those activities require unanimous consent. Judgment is also required to classify a joint arrangement. Classifying the arrangement requires the Company to assess their rights and obligations arising from the arrangement including whether the arrangement is structured through a separate vehicle, in which case judgment is also required to assess the rights and obligations arising from the legal form of the separate vehicle, terms of the contractual arrangement, and other relevant facts and circumstances. This assessment often requires significant judgment, and a different conclusion on joint control and whether the arrangement is a joint operation or a joint venture may materially impact the accounting. Management has assessed that its petroleum and natural gas activities involve jointly controlled operations.

Determination of functional currency

The functional currency of the Company and its subsidiary is the currency of the primary economic environment and the Company reconsiders the functional currency if there is a change in events and conditions, which determines the primary economic environment.

Loans and discount rates

For loans measured at amortized cost under IFRS 9 *Financial Instruments*, judgment is used by management in determining the fair value for the loan at inception of the lending arrangement. The fair value of the loan is calculated based on the present value of the future loan payments, discounted using an interest rate that would be charged by another market participant for a financing arrangement with similar characteristics. Judgment is used by management in determining what the interest rate would be for sourcing a similar financing arrangement in the market.

Critical accounting estimates

Decommissioning obligations

Amounts recorded for decommissioning obligations require the use of management's best estimates of future decommissioning expenditures, expected timing of expenditures, future inflation rates and expected discount rates. The estimates are based on internal and third-party information and calculations are subject to change over time and may have a material impact on profit or loss or financial position.

Recoverability of accounts receivable

Accounts receivable are recorded at the estimated recoverable amount, which involves an estimate of uncollectable accounts.

XXL Energy Corp.
Notes to the Consolidated Financial Statements
For the Years Ended December 31, 2021 and 2020

(Expressed in US dollars, unless otherwise noted)

2. BASIS OF PRESENTATION (continued)

- (d) Use of estimates and judgments (continued)

Critical accounting estimates (continued)

Income taxes

Related assets and liabilities are recognized for the estimated tax consequences between amounts included in the consolidated financial statements and their tax basis using substantively enacted future income tax rates. Timing of future revenue streams and future capital spending changes can affect the timing of any temporary differences, and accordingly, affect the amount of the deferred tax asset or liability calculated at a point in time. These differences could materially impact earnings.

- (e) Approval of the consolidated financial statements

The consolidated financial statements of XXL Energy Corp. for the years ended December 31, 2021 and 2020 were reviewed, approved and authorized for issue by the Board of Directors on April 22, 2022.

3. SIGNIFICANT ACCOUNTING POLICIES

- (a) Basis of consolidation

- (i) Subsidiary

The consolidated financial statements include the accounts of the Company and its wholly owned subsidiary, Exxel Energy. A subsidiary is an entity in which the Company has control, where control requires exposure or rights to variable returns and the ability to affect those returns through power over the investee. All intercompany transactions and balances have been eliminated upon consolidation.

- (ii) Jointly controlled operations and jointly controlled assets

The Company's petroleum and natural gas activities involve jointly controlled operations. The consolidated financial statements include the Company's share of costs, deferred costs and liabilities incurred in respect of its interests in jointly controlled operations.

- (b) Foreign currency translation

Transactions in foreign currencies are translated to the respective functional currencies of the Company and Exxel Energy, at the exchange rates at the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies are translated into the respective functional currency at the reporting date and foreign currency gains or losses are recognized in net loss for the year.

XXL Energy's financial information is translated from Canadian dollars, its functional currency, at each reporting period to US dollars, the Company's reporting currency. Assets and liabilities are translated at the exchange rates prevailing at the consolidated statement of financial position dates, and revenue and expenses are translated on the basis of average exchange rates during the year. Any recognized and unrecognized gains or losses arising from the translation of these amounts are recorded in other comprehensive income (loss) and classified as a component of equity.

XXL Energy Corp.
Notes to the Consolidated Financial Statements
For the Years Ended December 31, 2021 and 2020

(Expressed in US dollars, unless otherwise noted)

3. SIGNIFICANT ACCOUNTING POLICIES (continued)

(c) Financial instruments

(i) Financial assets

Initial recognition and measurement

A financial asset is measured initially at fair value plus, for an item not at fair value through profit or loss, transaction costs that are directly attributable to its acquisition or issue. On initial recognition, a financial asset is classified as measured at amortized cost or fair value through profit or loss or fair value through other comprehensive income. A financial asset is measured at amortized cost if it meets the conditions that i) the asset is held within a business model whose objective is to hold assets to collect contractual cash flows, ii) the contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding, and iii) is not designated as fair value through profit or loss.

Subsequent measurement

The subsequent measurement of financial assets depends on their classification as follows:

Financial assets at fair value through profit or loss ("FVTPL")

Financial assets measured at fair value through profit and loss are carried in the consolidated statement of financial position at fair value with changes in fair value therein, recognized in the statement of operations.

Financial assets measured at fair value through other comprehensive income ("FVTOCI")

Financial assets measured at fair value through other comprehensive income are measured at fair value with changes in fair value included as "financial asset at fair value through other comprehensive income" in other comprehensive income.

Financial assets measured at amortized cost

A financial asset is subsequently measured at amortized cost, using the effective interest method and net of any impairment allowance.

Derecognition

A financial asset or, where applicable, a part of a financial asset or part of a group of similar financial assets, is derecognized when:

- The contractual rights to receive cash flows from the asset have expired; or
- The Company has transferred its rights to receive cash flows from the asset or has assumed an obligation to pay the received cash flows in full without material delay to a third party under a 'pass-through' arrangement; and either (a) the Company has transferred substantially all the risks and rewards of the asset, or (b) the Company has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

XXL Energy Corp.
Notes to the Consolidated Financial Statements
For the Years Ended December 31, 2021 and 2020

(Expressed in US dollars, unless otherwise noted)

3. SIGNIFICANT ACCOUNTING POLICIES (continued)

(c) Financial instruments (continued)

(ii) Financial liabilities

Financial liabilities are recognized when the Company becomes a party to the contractual provisions of the financial instrument. A financial liability is derecognized when it is extinguished, discharged, cancelled or when it expires. Financial liabilities are classified as either financial liabilities at fair value through profit or loss or financial liabilities subsequently measured at amortized cost. All interest-related charges are reported in profit or loss within interest expense, if applicable.

(iii) Fair value hierarchy

Fair value measurements of financial instruments are required to be classified using a fair value hierarchy that reflects the significance of inputs used in making the measurements. The levels of the fair value hierarchy are defined as follows:

- Level 1 - Quoted prices (unadjusted) in active markets for identical assets or liabilities.
- Level 2 - Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly.
- Level 3 - Inputs for assets or liabilities that are not based on observable market data value at one of three levels according to the relative reliability of the inputs used to estimate the fair value:

(d) Revenue recognition

Revenue from the sale of petroleum and natural gas is recorded when performance obligations are satisfied. Performance obligations are satisfied at the point in time when products are delivered based on volumes to customers at contractual delivery points, and prices have been agreed with the purchaser and collectability is reasonably assured. Delivery is generally at the time the petroleum enters the tanks and when the natural gas enters the pipeline. The costs associated with the delivery, including operating and maintenance costs, transportation and production-based royalty expenses, are recognized during the same year in which the related revenue is earned and recorded.

(e) Petroleum and natural gas properties

Exploration and evaluation ("E&E") assets

Once a legal right to explore has been acquired the costs of the following: exploration licenses, unproved property acquisition costs, geological and geophysical costs, and costs directly associated with an exploration well and appraisal activities are capitalized as E&E assets. The costs are accumulated in cost centers by well, field or exploration area pending determination of technical feasibility and commercial viability.

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3. SIGNIFICANT ACCOUNTING POLICIES (continued)

(e) Petroleum and natural gas properties (continued)

Exploration and evaluation ("E&E") assets (continued)

The technical feasibility and commercial viability are based upon estimates of the recoverability of capitalized costs by future exploitation or sale and where the activities have reached a stage that permits reasonable assessment of the existence of proved and proven reserves. A review of each exploration license or field will be carried out, at least annually, to ascertain whether proven plus probable reserves have been discovered. Upon determination of proven plus probable reserves, E&E assets attributable to those reserves will be first tested for impairment and then reclassified from E&E assets to developed petroleum and natural gas properties.

Certain of the Company's properties in Wyoming are classified as E&E assets.

Developed and producing properties

Items in developed and producing properties are measured at cost less accumulated depletion and depreciation and accumulated impairment losses. Development assets are grouped into CGUs for impairment testing. As at December 31, 2021, the Company has three CGUs based on geographic locations, which are Green River Basin, Wyoming, Pinedale Field, Wyoming and Piceance Basin, Colorado.

Gains and losses on disposal of developed petroleum and producing properties are determined by comparing the proceeds from disposal with the carrying amount of the asset and are recognized net within profit or loss.

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

Depletion and depreciation

The net carrying value of development or production assets is depleted using the unit-of-production method by reference to the ratio of production in the year of the related proved and probable reserves. These estimates are reviewed by independent reserve engineers at least annually.

Proven and probable reserves are estimated using independent reserve engineer reports and represent the estimated quantities of crude oil, natural gas and natural gas liquids, which geological, geophysical and engineering data demonstrate with a specified degree of certainty to be recoverable in future years from known reservoirs and which are considered commercially viable. There should be a minimum 90% statistical probability that the actual quantity of recoverable reserves will be more than the amount estimated as proven and a maximum 10% statistical probability that it will be less. Such reserves may be considered commercially viable if management has the intention of developing and producing them and such intention is based upon:

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3. SIGNIFICANT ACCOUNTING POLICIES (continued)

(e) Petroleum and natural gas properties (continued)

Depletion and depreciation (continued)

- A reasonable assessment of the future economics of such production;
- A reasonable expectation that there is a market for all or substantially all the expected oil and natural gas production; and
- Evidence that the necessary production, transmission and transportation facilities are available or can be made available.

Reserves may only be considered proven if future economic feasibility is supported by either actual production or conclusive formation testing. The area of reservoir considered proven includes (a) that portion delineated by drilling and defined by gas-oil and/or oil-water contacts, if any, or both, and (b) the immediately adjoining portions not yet drilled, but which can be reasonably judged as economically productive on the basis of available geophysical, geological and engineering data. In the absence of information on fluid contacts, the lowest known structural occurrence of oil and natural gas controls the lower proved limit of the reservoir.

(f) Impairment

Financial assets

A financial asset is assessed at each reporting date to determine whether there is any objective evidence that it is impaired. A financial asset is considered to be impaired if objective evidence indicates that one or more events have had a negative effect on the estimated future cash flows of that asset.

An impairment loss in respect of a financial asset measured at amortized cost is the present value of the estimated future cash flows discounted at the asset's original effective interest rate.

Individually significant financial assets are tested for impairment on an individual basis. The remaining financial assets are assessed collectively in groups that share similar credit risk characteristics. All impairment losses are recognized in profit or loss.

Exploration and evaluation assets and petroleum and natural gas assets are assessed for impairment if facts and circumstances suggest that the carrying amount exceeds the recoverable amount. An impairment test is completed if any such indication exists. For the purpose of impairment testing, assets are grouped together into the smallest group of assets that generates cash inflows from continuing use that are largely independent of the cash inflows of other assets or groups of assets (the CGU). The recoverable amount of an asset or a CGU is the greater of its value in use and its fair value less costs to sell.

E&E assets are also assessed for impairment when they are reclassified to developing and producing assets, as developed petroleum and natural gas properties.

Fair value less costs to sell is determined to be the amount for which the asset could be sold in an arm's length transaction. Fair value less costs to sell can be determined by using an observable market or by using discounted future net cash flows of proved and probable reserves using forecasted prices and costs. Value in use is determined by estimating the present value of the future net cash flows expected to be derived from the continued use of the asset or CGU.

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3. SIGNIFICANT ACCOUNTING POLICIES (continued)

(f) Impairment (continued)

An impairment loss would be recognized if the carrying amount of an asset or its CGU exceeds its estimated recoverable amount. Impairment losses are recognized in profit or loss.

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

(g) Income taxes

Income tax expense comprises current and deferred tax. Income tax expense is recognized in net loss, except to the extent that if the income tax expense related to items recognized directly in equity, the income tax expense would also be recognized in equity.

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

Deferred tax is recognized using the asset and liability method providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is measured at the tax rates that are expected to be applied to temporary differences when they reverse, based on the laws that have been enacted or substantively enacted at the reporting date. Deferred tax assets and liabilities are offset if there is a legally enforceable right to offset, and they relate to income taxes levied by the same tax authority on the same taxable entity, or on different taxable entities, but they intend to settle current tax liabilities and assets on a net basis or their tax assets and liabilities will be realized simultaneously.

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

(h) Earnings (loss) per share

Basic earnings (loss) per share is calculated by dividing net income (loss) attributable to common shareholders of the Company by the weighted average number of common shares outstanding during the year. Diluted earnings (loss) per share is computed using the treasury stock method. In accordance with the treasury stock method, the weighted average number of common shares outstanding is increased to include additional shares for the assumed exercise of stock options and warrants, if dilutive. The number of additional shares is calculated by assuming that outstanding stock options and warrants were exercised and that the proceeds from such exercises were used to acquire common stock at the average market price during the reporting periods. Diluted earnings (loss) per share excludes the exercise of options and warrants and other convertible features to the extent they are anti-dilutive.

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3. SIGNIFICANT ACCOUNTING POLICIES (continued)

(i) Share-based payments

The Company may grant share options to acquire common shares of the Company to directors, officers, employees and consultants. The fair value of share-based payments to employees is measured at grant date, using the Black-Scholes option pricing model, and is recognized over the vesting period for employees using the graded method. Fair value of share-based payments to non-employees is recognized and measured at the date the goods or services are received based on the fair value of such goods or services. If it is determined that the fair value of goods and services received cannot be reliably measured, the share-based payment is measured at the fair value of the equity instruments issued using the Black-Scholes option pricing model.

For both employees and non-employees, the fair value of share-based payments is recognized as either an expense or as petroleum and natural gas properties with a corresponding increase in options reserve. The amount recognized as expense is adjusted to reflect the number of share options expected to vest. Consideration received on the exercise of stock options is recorded in capital stock and the related share-based payment in options reserve is transferred to capital stock. For those options that expire, the recorded value is transferred to deficit.

(j) Decommissioning obligations

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

Decommissioning obligations are measured at the present value of management's best estimate of expenditure required to settle the present obligation at the consolidated statement of financial position date. Subsequent to the initial measurement, the obligation is adjusted at the end of each year to reflect the passage of time and changes in the estimated future cash flows underlying the obligation. The increase in the provision due to the passage of time is recognized as finance costs whereas increases/decreases due to changes in the estimated future cash flows are capitalized. Actual costs incurred upon settlement of the decommissioning obligations are charged against the provision to the extent the provision was established.

(k) Provisions

A provision is recognized if, as a result of a past event, the Company has a present obligation (legal or constructive) that can be estimated reliably, and it is probable that an expenditure will be required to settle the obligation. Provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflect current market assessments of the time value of money and the risks specific to the liability. Provisions are not recognized for future operating losses.

(l) New accounting pronouncements:

At the date of authorization of these consolidated financial statements, certain new standards, amendments and interpretations to existing standards have been published, but are not yet effective, and have not been early-adopted by the Company. The Company does not expect these new pronouncements to have a significant impact on its consolidated financial statements.

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4. FINANCIAL INSTRUMENTS

Fair value

The carrying values of cash, accounts receivable, accounts payable and accrued liabilities and due to related parties approximate their fair values due to the short-term maturity of these financial instruments. The loan payable and loans payable to related parties are valued as Level 2 financial instruments on the fair value hierarchy.

Classification

The Company classifies its financial instruments as follows: cash is classified as a financial asset at FVTPL, accounts receivable, at amortized cost, and accounts payable and accrued liabilities, loan payable, due to related parties and loans payable to related parties, at amortized cost.

5. FINANCIAL RISK MANAGEMENT

(a) Overview

The Company has exposure to the following risks from its use of financial instruments:

- Market risk;
- Credit risk; and
- Liquidity risk.

(b) Market risk

Market risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate due to changes in market prices. Market risk comprises three types of risk: foreign currency risk, interest rate risk and other price risk.

(i) Foreign currency risk

The Company is exposed to foreign currency risk to the extent that expenditures incurred or funds received and balances maintained by the Company are denominated in currencies other than the Canadian dollar (primarily US dollars) and funds received and balances maintained by Exxel Energy that are denominated in currencies other than the US dollar (primarily Canadian dollars).

The Company operates in Canada and the United States and a significant portion of its expenses are incurred in US dollars. A significant change in the exchange rate between the Canadian dollar relative to the US dollar could have a significant effect on the Company's financial performance, financial position and cash flows.

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5. FINANCIAL RISK MANAGEMENT (continued)

(b) Market risk (continued)

(i) Foreign currency risk (continued)

The Company is exposed to currency risk through the following financial assets and liabilities denominated in Canadian dollars:

| | December 31, 2021 | December 31, 2020 |
|----------------------|------------------------------|------------------------|
| Cash | \$ 24,275 | \$ 43,326 |
| Accounts payable | (99) | (217) |
| Loans payable | (11,538,866) | (10,324,606) |
| | \$ (11,514,690) | \$ (10,281,497) |
| US dollar equivalent | \$ (9,082,419) | \$ (8,075,320) |

A 10% (2020 - 10%) change in the Canadian dollar against the US dollar at December 31, 2021 would result in a change of approximately \$908,000 (2020 - \$808,000) in comprehensive loss.

(ii) Interest rate risk

The Company's cash is held in bank accounts and, due to the short-term nature of this financial instrument, fluctuations in market interest rates do not have a significant impact on the fair value as at December 31, 2021.

The Company's loans are at fixed interest rates, and therefore, the Company has exposure to interest rate price risk.

(iii) Other price risk

Other price risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate due to changes in market prices, other than those arising from interest rate risk. The Company is not exposed to significant other price risk.

(c) Credit risk

Credit risk is the risk of financial loss to the Company if a counterparty to a financial instrument fails to meet its payment obligations. The Company is exposed to credit risk with respect to its cash and accounts receivable.

The credit risk associated with cash is mitigated, as cash is held at major financial institutions with high credit ratings.

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5. FINANCIAL RISK MANAGEMENT (continued)

(c) Credit risk (continued)

Accounts receivable primarily consists of trade receivables outstanding from operators from the sale of its petroleum and natural gas. To mitigate this risk, the Company regularly reviews the collectability of the accounts receivable to ensure there is no indication that these amounts will not be fully recoverable. As at December 31, 2021, the Company has not recorded any allowance for doubtful accounts. The Company's accounts receivable are due within 60 days.

(d) Liquidity risk

Liquidity risk is the risk that the Company will encounter difficulty in satisfying financial obligations as they become due. The Company assesses its liquidity risk by forecasting cash flows required by operations and anticipated financing activities.

The Company has a working capital deficiency of \$34,520,245 (2020 - \$31,486,500). Based on the current funds held, the Company will need to rely upon the continued forbearance of its creditors and/or additional financing from shareholders and/or debt holders to obtain sufficient working capital. There is no assurance that such financing will be available and on terms and conditions acceptable to the Company.

The amounts listed below are the contractual maturities for financial liabilities held by the Company as at December 31, 2021:

| Due Date | Accounts Payable and Accrued Liabilities | Loans Payable (note 12) | Loans Payable to Related Parties (note 13) | Due to Related Parties (note 14) | Total |
|--------------|--|-------------------------|--|----------------------------------|---------------|
| 0 – 90 days | \$ 425,707 | \$ - | \$ 32,177,348 | 1,281,559 | \$ 33,884,614 |
| 1 year | - | 585,018 | 79,996 | - | 665,014 |
| 2 to 6 years | - | 1,170,036 | 641,930 | - | 1,811,966 |
| | \$ 425,707 | \$ 1,755,054 | \$ 32,899,274 | 1,281,559 | \$ 36,361,594 |

The amounts listed below are the contractual maturities for financial liabilities held by the Company as at December 31, 2020:

| Due Date | Accounts Payable and Accrued Liabilities | Loans Payable (note 12) | Loans Payable to Related Parties (note 13) | Due to Related Parties (note 14) | Total |
|--------------|--|-------------------------|--|----------------------------------|---------------|
| 0 – 90 days | \$ 506,727 | \$ - | \$ 29,651,063 | 1,274,093 | \$ 31,431,883 |
| 1 year | - | 852,255 | - | - | 852,255 |
| 2 to 6 years | - | 1,755,056 | 668,900 | - | 2,423,956 |
| | \$ 506,727 | \$ 2,607,311 | \$ 30,319,963 | 1,274,093 | \$ 33,573,757 |

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6. CAPITAL MANAGEMENT

The Company defines its capital structure as debt and shareholders' deficiency. Capital requirements are driven by the Company's exploration activities on its petroleum and natural gas interests. Management's objective is to ensure that there are sufficient capital resources to safeguard the Company's ability to continue as a going concern. Management reviews its capital management approach on an ongoing basis and believes that its approach, given the relative size of the Company, is reasonable.

Although the Company has been successful at raising funds in the past through obtaining equity and debt financing from shareholders, it is uncertain whether it can continue this financing methodology.

The Board of Directors does not establish a quantitative return on capital criteria for management, but rather relies on the expertise of the Company's management to sustain future development of the business. The Company's capital stock and debt is not subject to any externally imposed capital requirements. The Company did not change its approach to capital management during the years ended December 31, 2021 and 2020.

7. ACCOUNTS RECEIVABLE

| | December 31, 2021 | December 31, 2020 |
|-------------------|------------------------------|----------------------|
| GST receivable | \$ 1,279 | \$ 1,373 |
| Trade receivables | 374,325 | 345,641 |
| | \$ 375,604 | \$ 347,014 |

8. PETROLEUM AND NATURAL GAS PROPERTIES

Exploration and Evaluation Assets

| | Green River Basin, Wyoming |
|----------------------------|-------------------------------|
| December 31, 2019 | \$ 137,851 |
| Impairment | (108,309) |
| December 31, 2020 and 2021 | \$ 29,542 |

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8. PETROLEUM AND NATURAL GAS PROPERTIES (continued)

Developed and Producing Properties

| Cost | Green River Basin, Wyoming | Piceance Basin, Colorado | Pinedale Field, Wyoming | Asset Retirement | Total |
|--|-------------------------------|-----------------------------|----------------------------|------------------|---------------|
| December 31, 2019 | \$ 1,514,291 | \$ 27,827 | \$ 13,421,545 | \$ 617,961 | \$ 15,581,624 |
| Additions | - | - | 22,538 | - | 22,538 |
| Change in estimate of decommissioning obligation | - | - | - | (20,834) | (20,834) |
| December 31, 2020 | 1,514,291 | 27,827 | 13,444,083 | 597,127 | 15,583,328 |
| Additions | - | - | 4,483 | - | 4,483 |
| Change in estimate of decommissioning obligation | - | - | - | 538,160 | 538,160 |
| December 31, 2021 | \$ 1,514,291 | \$ 27,827 | \$ 13,448,566 | \$ 1,135,287 | \$ 16,125,971 |

| Accumulated Depletion and Impairment | Green River Basin, Wyoming | Piceance Basin, Colorado | Pinedale Field, Wyoming | Asset Retirement | Total |
|---|-------------------------------|-----------------------------|----------------------------|------------------|-----------------|
| December 31, 2019 | \$ (1,425,723) | \$ (27,827) | \$ (3,742,311) | \$ (225,845) | \$ (5,421,706) |
| Depletion | (10,362) | - | (1,364,007) | (60,572) | (1,434,941) |
| Impairment | (78,206) | - | (4,838,287) | - | (4,916,493) |
| December 31, 2020 | (1,514,291) | (27,827) | (9,944,605) | (286,417) | (11,773,140) |
| Depletion | - | - | (314,659) | (27,938) | (342,597) |
| December 31, 2021 | \$ (1,514,291) | \$ (27,827) | \$ (10,259,264) | \$ (314,355) | \$ (12,115,737) |

| Carrying Amounts | Green River Basin, Wyoming | Piceance Basin, Colorado | Pinedale Field, Wyoming | Asset Retirement | Total |
|-------------------------|-------------------------------|-----------------------------|----------------------------|------------------|--------------|
| December 31, 2020 | \$ - | \$ - | \$ 3,499,478 | \$ 310,710 | \$ 3,810,188 |
| December 31, 2021 | \$ - | \$ - | \$ 3,188,899 | \$ 772,543 | \$ 4,010,234 |

Properties

- (i) Green River Basin (Wyoming) and Williston Basin (North Dakota)

Green River Basin

In the Green River Basin, the Company currently has interests in six wells and three royalty interest wells.

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8. PETROLEUM AND NATURAL GAS PROPERTIES (continued)

Properties (continued)

(ii) Piceance Basin (Colorado)

On March 16, 2005, the Company acquired an interest in certain oil and gas leases and related assets in Piceance Basin, Colorado.

The Company developed its interests in the properties in a joint venture with a third-party operator and drilled four wells. As at December 31, 2021, all the wells are shut-in and are awaiting pending reclamation activities. The Company has a 75% working interest in the wells and a corresponding decommissioning obligation for each of the wells.

Included in the acreage purchased, the Company holds a 16.98% working interest in the well.

(iii) Pinedale Field (Wyoming)

In September 2018, the Company's wholly owned subsidiary, Exxel USA, closed a Farmout Agreement (the "Farmout Agreement") with Standard Energy ("Standard"), a Nevada corporation. Standard is related to the Company as it is controlled by a director of the Company.

Standard is the owner of certain working interests ranging from 18.75% to 21.25% in oil and gas leases located in the Warbonnet area of Pinedale Field, Sublette County, Wyoming (the "Farmout Lands").

Pursuant to the Farmout Agreement, the Company acquired the right to earn the working interests owned by Standard in up to approximately 70 development and extension wells to be drilled on oil and gas leases located in the Farmout Lands. The Company will earn its interest in each well through the payment of Standard's entire cost of drilling, testing and completing the wells on a well-by-well basis. Should the Company elect not to participate in any well, Standard may thereupon terminate the Farmout Agreement or permit the Company to participate in future wells. For wells in which the Company participates, upon testing and completion of a well as a commercial producer, Standard will assign 100% of its interest in the well and lease rights to the Company. With respect to each well assigned to the Company, Standard will retain a 3% overriding royalty interest, subject to its right to convert the royalty on a well-by-well basis to a 25% working interest upon the successful completion of the well and the return to the Company of its actual costs of drilling, testing and completing the well.

Standard funded the Company's initial drilling, testing and completion costs, until such time as the Company arranged traditional reserve-based financing. The advances from Standard bear interest at an annual rate of 10% (note 13).

As of December 31, 2021, fifteen of the wells are online and producing.

(iv) Impairment

During the year ended December 31, 2021, the Company performed an assessment of potential impairment indicators. Management determined that there were no indicators of impairment on its developed and producing petroleum and natural gas assets.

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8. PETROLEUM AND NATURAL GAS PROPERTIES (continued)

(iv) Impairment (continued)

During the year ended December 31, 2020, the Company performed an assessment of potential impairment indicators of its developed and producing properties. As at December 31, 2020, management determined that with the decline in crude oil and natural gas prices that an impairment test on its developed and producing petroleum and natural gas assets was required.

During the year ended December 31, 2020, the Company determined that the recoverable amounts of its developed and producing properties in both the Green River Basin CGU and Pinedale Field CGU exceeded their carrying amounts. Accordingly, impairment was recognized. The carrying amount of Green River Basin CGU exceeded its recoverable amount, resulting in impairment of \$78,206 and the carrying amount of the Pinedale Field CGU exceeded its recoverable amount, resulting in impairment of \$4,838,287.

The recoverable amounts were determined based on a fair value less cost to sell model and categorized in Level 3 of the fair value hierarchy. Key assumptions in the determination of cash flows from reserves include crude oil and natural gas prices, loss factors and discount rates specific to the underlying composition of assets residing in the CGUs. The post-tax discount rate used was 15.9%.

The following table show the future crude oil and natural gas price estimates used by the Company's independent reserves evaluator at December 31, 2020:

| 2022: | 2022 | 2023 | 2024 | 2025 | 2026 | 2027 |
|-----------------------------|-------|-------|-------|-------|-------|-------|
| Condensate Price (US\$/bbl) | 72.83 | 68.78 | 66.76 | 68.09 | 69.45 | 70.84 |
| Gas Price (US\$/MMbtu) | 3.850 | 3.438 | 3.174 | 3.236 | 3.303 | 3.367 |

*Prices then escalated 2% on January 1 of each year through December 31, 2033, and held constant thereafter

During the year ended December 31, 2021, the Company performed an assessment of potential impairment indicators. Management determined that there were no indicators of impairment on its exploration and evaluation assets.

During the year ended December 31, 2020, management determined that there were indicators of impairment of its exploration and evaluation assets. In assessing recoverable values management observed the bid prices of recent sales of leases in adjacent properties to those held by the Company.

The Company determined the recoverable amount of the Green River Basin to be less than the carrying amount and therefore recorded an impairment loss at December 31, 2020 of \$108,309. The recoverable amount of \$29,542 is based on the Green River Basin properties' fair value less costs to sell. In estimating the fair value less costs to sell, the Company used a market approach. The Company used sale prices of adjacent properties obtained from the Bureau of Land Management. As this valuation technique requires the use of unobservable inputs including the Company's data about the property and management's interpretation of that data, it is classified within Level 3 of the fair value hierarchy. A value in use calculation is not applicable as the Company does not have any expected cash flows from using the property at this stage of development. In estimating fair value less costs to sell, management's judgment was involved in identifying comparable properties with characteristics similar to the Green River Basin properties (e.g., nature and amount of resources, size and accessibility).

(ii) Risks

Although the Company believes that it has title to its petroleum and natural gas interests, it cannot control or completely protect itself against the risk of title disputes or challenges.

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9. DECOMMISSIONING OBLIGATIONS

The Company's decommissioning obligations result from net ownership interest in petroleum and natural gas properties, including well sites, gathering systems and processing facilities. The Company estimates the total undiscounted amount of cash flows required to settle its decommissioning liabilities is approximately \$636,300 (2020 - \$752,800). An inflation factor of 7.04% (2020 - 1.36%) has been applied to the estimated asset retirement cost. A risk-free rate of 1.915% (2020 - 1.46%) was used to calculate the fair value of the decommissioning obligations. The change in timing of the estimated future obligations, change in inflation rate and a change in the risk-free rate results in a change in estimate in the present value of the decommissioning obligations.

| | | |
|----------------------------|----|-----------|
| Balance, December 31, 2019 | \$ | 822,602 |
| Accretion expense | | (150) |
| Change in estimate | | (20,834) |
| Balance, December 31, 2020 | | 801,618 |
| Accretion expense | | 698 |
| Change in estimate | | 538,160 |
| Balance, December 31, 2021 | \$ | 1,340,476 |

10. RECLAMATION BOND

The Company has a bond with the state of Wyoming authorities for a total of \$25,000 (2020 - \$25,000). The reclamation bond represents funds held in trust to ensure the Company has adequate resources to finance road repairs and any other environmental or reclamation obligations that may arise on its Green River Basin and Williston Basin properties. The reclamation bond may be refunded to the Company upon completion of reclamation obligations.

11. CAPITAL STOCK

(a) Authorized

An unlimited number of common shares without par value.

(b) Issued

No shares were issued during the years ended December 31, 2021 and 2020.

(c) Stock options

In 2008, the Company adopted an incentive stock option plan under which the Company may issue up to a maximum of 20% of the issued shares of the Company as stock options to acquire common shares in the capital of the Company as an incentive to officers, directors, employees and consultants. Options issued to consultants performing investor relations activities must vest in stages over a minimum period of twelve months with no more than 25% of the options vesting in any three-month period. Any options granted under a prior plan shall continue to be governed by the plan under which they were granted.

No options or warrants were granted or outstanding during the years ended December 31, 2021 and 2020.

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12. LOAN PAYABLE

On December 17, 2019, the Company entered into a business loan agreement with the Jonah Bank of Wyoming in the amount of \$3,275,000 (the "Loan"). The Loan has an interest rate of 6% per annum, a maturity date of December 17, 2024 and is collateralized by the Company's Pinedale Field assets. The Company is required to make blended principal and interest monthly payments of \$48,752 for the remaining term. The balance of the principal due within 12 months is \$502,528 with the remaining balance of \$1,100,085 due over the period to December 2024.

13. LOANS PAYABLE TO RELATED PARTIES

| | December 31, 2021 | December 31, 2020 |
|---|----------------------|----------------------|
| Current | | |
| Loan payable to a company with a common director (note 13(a)) | \$ 1,853,389 | \$ 1,766,986 |
| Advances from a company controlled by a director (note 13(b)) | 2,755,391 | 2,378,603 |
| Loan from a director (note 13(c)) | 6,432,082 | 5,633,281 |
| Loan acquired by a director (note 13(d)) | 13,584,370 | 11,772,305 |
| Loan payable to a company controlled by a director (note 13(f)) | 8,711,585 | 8,099,886 |
| Loan from a director (note 13(e)) | 66,282 | - |
| | 33,403,099 | 29,651,061 |
| Non-current | | |
| Loan from a director (note 13(e)) | 553,450 | 544,871 |
| | \$ 33,956,549 | \$ 30,195,932 |

- (a) Loan payable to a company with a common director ("Lender 1" – Giant Energy Ltd.)

On June 23, 2008, the Company issued an unsecured note payable in the amount of \$788,768 (2020 - \$785,423) (C\$1,000,000) due December 17, 2008 to Lender 1. As at December 31, 2021 and 2020, the loan is considered to be in default. The note bears interest at 10% per annum payable at maturity. Accrued interest of \$1,064,621 (C\$1,349,726) (2020 - \$981,563 (C\$1,249,726)) is included in the balance owing.

- (b) Advances from a company controlled by a director ("Lender 2" – Caravel Management Corp.)

The advances of \$575,107 (2020 - \$575,107) are unsecured, with no specified terms of repayment and bear interest at 15% per annum, calculated monthly and compounded quarterly and is payable on demand. Accrued interest of \$2,180,284 (2019 - \$1,803,496) is included in the balance owing.

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13. LOANS PAYABLE TO RELATED PARTIES (continued)

(c) Loan from a director (“Lender 3” – John Hislop)

On February 8, 2010, the Company issued a note payable in the amount of \$1,183,152 (2020 - \$1,178,134) (C\$1,500,000) to Lender 3. The note bore interest at 12% per annum, compounded monthly and was payable at maturity on January 31, 2018. On January 31, 2018, the note plus accrued interest (C\$3,874,000) was renewed adjusting the interest to 15% per annum. All other terms remain unchanged. This loss was recorded in contributed surplus to reflect the effect of the increase in the interest rate from the loan received from a related party.

Continuity of the loan is as follows:

| | Total |
|----------------------------|--------------|
| Balance, December 31, 2019 | \$ 4,782,998 |
| Accretion expense | 119,718 |
| Interest expense | 596,000 |
| Foreign exchange | 134,565 |
| Balance, December 31, 2020 | 5,633,281 |
| Accretion expense | 16,223 |
| Interest expense | 767,423 |
| Foreign exchange | 15,155 |
| Balance, December 31, 2021 | \$ 6,432,082 |

As of December 31, 2021, accrued interest of \$4,272,615 (C\$5,416,821) (2020 - \$3,498,944 (C\$4,454,855)), net of accretion, is included in the balance owing. The note will mature at the earlier of the following:

- (i) January 31, 2025; or
- (ii) 10 business days following the delivery of demand repayment by Lender 3.

As collateral, Lender 3 has a fixed and floating charge over all of the Company’s real and personal assets.

(d) Loan acquired by a director (“Lender 4” – John Hislop)

On November 24, 2008, Warrior Oil and Gas Holdings Inc. (“Warrior”) acquired a note payable from the Company in the amount of \$2,000,000 (including the mortgage attached to the note) from a third party. The note was collateralized by a mortgage over certain petroleum and natural gas interests (note 8). Effective May 30, 2009, the Company commenced accruing interest on the loan at 15% per annum. As of May 2011, they ceased being related parties. On October 30, 2012, Warrior finalized an assignment of debt agreement with Lender 4, whereby Warrior assigned the loan payable to Lender 4. All of the terms and conditions of the loan remained unchanged.

As of December 31, 2021, the total loan was \$13,584,370 (2020 - \$11,772,305), including accrued interest of \$11,084,370 (2020 - \$9,272,305) and a loan modification fee of \$500,000. This loan is currently considered to be in default.

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13. LOANS PAYABLE TO RELATED PARTIES (continued)

(e) Loans from a director (“Lender 5” – John Hislop)

| | Total |
|----------------------------|------------|
| Balance, December 31, 2019 | \$ 472,175 |
| Interest expense | 53,310 |
| Accretion expense | 19,386 |
| Balance, December 31, 2020 | 544,871 |
| Interest expense | 55,700 |
| Accretion expense | 19,161 |
| Balance, December 31, 2021 | \$ 619,732 |

The loans issued during fiscal 2016 and 2017 were revalued on issuance and renewal to account for comparable market interest rates. As a result, the effective interest rate was determined to be 30% and 16% per annum, respectively.

The loans bear interest at 15% per annum, calculated quarterly, and the principal amounts will become due and payable as follows:

| | |
|------------------|------------|
| Next 12 months | \$ 66,282 |
| Next 2 – 5 years | \$ 553,450 |
| After 5 years | - |
| | \$ 619,732 |

(f) Loan payable to a Company controlled by a director (“Lender 6” – Standard)

In September 2018, the Company closed its Farmout Agreement with Standard (note 8). Standard is funding the Company’s initial costs of each well, secured against title to the wells. Funds borrowed by the Company under this arrangement bear interest at the rate of 10% per annum and are repayable upon demand.

On April 8, 2019, the Company made a payment against the interest payable of \$200,000. On December 18, 2019, the Company made a payment against principal of \$3,275,000 from the proceeds of the Jonah Bank loan (note 12). On November 6, 2020, the Company borrowed an additional \$200,000. As of December 31, 2021, the total loan was \$8,711,585 (2020 - \$8,099,886). Accrued interest of \$2,609,142 (2020 - \$1,997,443) is included in the balance owing.

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14. RELATED PARTY TRANSACTIONS

The following is a summary of related party transactions that occurred throughout the years ended December 31, 2021 and 2020 that have not otherwise been disclosed:

- (a) Fees paid to directors and officers of \$13,761 (2020 - \$13,418). There were no post-employment benefits, termination benefits or other long-term benefits paid to key management personnel for the years ended December 31, 2021 and 2020; and
- (b) Administrative fees paid or accrued to a company controlled by a director of \$95,732 (2020 - \$89,452).

Amounts due to related parties not otherwise disclosed consist of the following:

- (a) Included in due to related parties is a total of \$1,281,559 (2020 - \$1,274,093) due to companies controlled by a director of the Company.

Amounts due to related parties are non-interest-bearing, unsecured and due on demand.

15. INCOME TAXES

Income tax expense differs from the amount that would be computed by applying the Canadian statutory income tax rate of 27.00% (2020 - 27.00%) to loss before income taxes. The reasons for the differences are as follows:

| | 2021 | 2020 |
|--|----------------|----------------|
| Loss before income taxes | \$ (2,910,708) | \$ (9,113,310) |
| Statutory income tax rate | 27.00% | 27.00% |
| Expected income tax recovery | (785,759) | (2,460,599) |
| Items not deductible for tax purposes | 13,517 | 254,126 |
| Change in timing differences | (97,349) | (89,731) |
| Impact of foreign exchange on tax assets and liabilities | 64,198 | (20,389) |
| Under provided in prior years | (314,001) | 170,756 |
| Unrecognized benefit of deferred tax assets | 1,119,394 | 2,145,837 |
| Income tax expense | \$ - | \$ - |

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15. INCOME TAXES (continued)

The Company recognizes tax benefits on losses or other deductible amounts where it is probable future taxable income for the recognition of deferred tax assets has been met. The Company carries loans from shareholders with interest lower than market rates. This gives rise to temporary differences that results in deferred tax liabilities for which deferred tax assets can be recognized consisting of the following amount:

| | 2021 | 2020 |
|--|-------------|-------------|
| Deferred tax liability on equity component of debt | \$ (13,904) | \$ (18,463) |
| Deferred tax asset recognized to offset liability | 13,904 | 18,463 |
| | \$ - | \$ - |

Additionally, the Company's unrecognized deductible temporary differences and unused tax losses for which no deferred tax asset is recognized consist of the following amounts:

| | 2021 | 2020 |
|---|----------------------|----------------------|
| Excess of unused exploration expenditures for Canadian tax purposes over carrying value of mineral property and petroleum and natural gas interests | \$ 11,835,220 | \$ 11,966,492 |
| Excess of undepreciated capital cost over carrying value of capital assets | 122,793 | 122,793 |
| Decommissioning obligation | 1,340,476 | 801,618 |
| Non-capital losses carried forward | 67,623,621 | 63,698,190 |
| Net capital losses carried forward - US | 6,044,282 | 6,044,281 |
| Unrecognized deductible temporary differences | \$ 86,966,392 | \$ 82,633,374 |

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15. INCOME TAXES (continued)

The Company has accumulated non-capital losses for Canadian income tax purposes of approximately C\$13,221,000. These losses expire as follows:

| | | |
|------|-----|------------|
| 2026 | C\$ | 1,071,000 |
| 2027 | | 674,000 |
| 2028 | | 3,157,000 |
| 2029 | | 1,189,000 |
| 2030 | | 647,000 |
| 2031 | | 669,000 |
| 2032 | | 702,000 |
| 2033 | | 234,000 |
| 2034 | | 264,000 |
| 2035 | | 345,000 |
| 2036 | | 170,000 |
| 2037 | | 745,000 |
| 2038 | | 974,000 |
| 2039 | | 807,000 |
| 2040 | | 791,000 |
| 2041 | | 782,000 |
| | C\$ | 13,221,000 |

For Canadian tax purposes, the Company has unused cumulative development and exploration expenses of C\$300,000 that may be carried forward indefinitely.

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15. INCOME TAXES (continued)

For US tax purposes, the Company has unused exploration expenditures that may be carried forward indefinitely, unused net capital losses that can be carried forward for five years and accumulated non-capital losses of \$57,341,000. These losses expire as follows:

| | | |
|------|----|------------|
| 2026 | \$ | 15,972,000 |
| 2027 | | 10,367,000 |
| 2028 | | 6,173,000 |
| 2029 | | 9,480,000 |
| 2030 | | 1,171,000 |
| 2031 | | 484,000 |
| 2032 | | 643,000 |
| 2033 | | 5,500,000 |
| 2034 | | 84,000 |
| 2035 | | 296,000 |
| 2036 | | 1,210,000 |
| 2038 | | - |
| 2037 | | 1,032,000 |
| 2039 | | 1,238,000 |
| 2040 | | 1,955,000 |
| 2041 | | 1,736,000 |
| | \$ | 57,341,000 |

16. SEGMENTED DISCLOSURES

The Company operates in one reportable operating segment, being the exploration and development of petroleum and natural gas interests. The Company's long-term assets and activities are located in the US, with the head office located in Canada.