

CONDENSED CONSOLIDATED INTERIM BALANCE SHEETS (UNAUDITED)

<i>(\$ thousands)</i>	Note	September 30, 2019	December 31, 2018
Assets			
Current Assets			
Cash and cash equivalents		\$ 27,333	\$ 19,208
Accounts receivable		3,607	1,918
Current portion of risk management contracts	10	105	–
Deposits and prepaid expenses		2,510	2,141
		33,555	23,267
Investments	3	279	287
Right-of-use assets	12	143	–
Property, plant and equipment	4	150,637	142,564
Exploration and evaluation assets	5	58,670	58,092
Goodwill		2,346	2,346
Deferred tax assets		5,824	6,816
		\$ 251,454	\$ 233,372
Liabilities			
Current Liabilities			
Accounts payable and accrued liabilities		\$ 19,058	\$ 18,503
Lease liabilities	12	110	–
Credit facilities	11	16,966	13,842
		36,134	32,345
Lease liabilities	12	36	–
Asset retirement obligation	6	14,318	13,736
		50,488	46,081
Shareholders' Equity			
Share capital	7	429,703	415,747
Contributed surplus		21,201	19,772
Accumulated other comprehensive income		3	10
Deficit		(249,941)	(248,238)
		200,966	187,291
		\$ 251,454	\$ 233,372

The notes are an integral part of these condensed consolidated interim financial statements.

CONDENSED CONSOLIDATED INTERIM STATEMENTS OF NET INCOME (LOSS) AND COMPREHENSIVE INCOME (LOSS) (UNAUDITED)

<i>(\$ thousands)</i>	Note	<i>Three months ended September 30,</i>		<i>Nine months ended September 30,</i>	
		2019	2018	2019	2018
Revenue					
Petroleum and natural gas sales		\$ 8,690	\$ 6,892	\$ 23,814	\$ 26,507
Royalties		146	(225)	(920)	(1,588)
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Petroleum and natural gas revenue, net of royalties		8,836	6,667	22,894	24,919
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Expenses					
Direct operating		3,227	3,092	9,722	8,142
General and administrative		602	818	2,898	3,429
Depletion, depreciation, accretion	4,5,6,12	3,609	2,380	9,856	9,046
Loss on equity investment	3	–	2,021	–	5,094
Gain on disposition of assets	4	–	–	(5)	(213)
Share based compensation	8	169	188	896	494
Interest expense		182	157	536	437
Interest & other (income) expenses		(284)	3	(497)	(66)
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Net income (loss) before taxes		1,331	(1,992)	(512)	(1,444)
Deferred tax expense (recovery)		–	31	1,190	(52)
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Net income (loss)		1,331	(2,023)	(1,702)	(1,392)
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Other comprehensive income (loss), net of tax					
<i>Items that may be reclassified subsequently to net income (loss):</i>					
Foreign currency translation adjustment		180	(48)	1	54
Gain (loss) on foreign exchange on investments	3	4	(204)	(8)	366
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		184	(252)	(7)	420
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Total comprehensive income (loss)		\$ 1,515	\$ (2,275)	\$ (1,709)	\$ (972)
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Net income (loss) per share					
Basic and diluted	7	\$ –	\$ (0.01)	\$ –	\$ –

The notes are an integral part of these condensed consolidated interim financial statements.

CONDENSED CONSOLIDATED INTERIM STATEMENTS OF CHANGES IN EQUITY (UNAUDITED)

<i>(\$ thousands)</i>	Note	<i>Nine months ended September 30,</i>	
		2019	2018
Share Capital			
Balance, beginning of period	7	\$ 415,747	\$ 414,995
Private placements		14,474	–
Warrants exercised		–	713
Options exercised		–	47
Share issue costs (net of tax)		(518)	(8)
Balance, end of period		429,703	415,747
Contributed Surplus			
Balance, beginning of period		19,772	18,171
Share based compensation		1,429	1,129
Balance, end of period		21,201	19,300
Accumulated Other Comprehensive Income (Loss)			
Balance, beginning of period		10	(724)
Other comprehensive income (loss)		(7)	420
Balance, end of period		3	(304)
Deficit			
Balance, beginning of period		(248,239)	(261,703)
Net loss		(1,702)	(1,392)
Balance, end of period		(249,941)	(263,095)
Total Shareholders' Equity		\$ 200,966	\$ 171,648

The notes are an integral part of these condensed consolidated interim financial statements.

CONDENSED CONSOLIDATED INTERIM STATEMENTS OF CASH FLOWS (UNAUDITED)

(\$ thousands)	Note	Three months ended September 30,		Nine months ended September 30,	
		2019	2018	2019	2018
Operating Activities					
Net Income (loss)		\$ 1,331	\$ (2,023)	\$ (1,702)	\$ (1,392)
Adjustments for:					
Depletion, depreciation and accretion	4,5,6,12	3,609	2,380	9,856	9,046
Gain on disposition of assets	4	–	–	(5)	(213)
Loss on equity investment	3	–	2,021	–	5,094
Share based compensation	8	169	188	896	494
Deferred tax expense (recovery)		–	31	1,190	(52)
Interest expense		181	158	536	437
Interest income		(137)	(1)	(328)	(61)
Other items not involving cash		(105)	(48)	(105)	54
Abandonment expenditures	6	(10)	(86)	(91)	(123)
Adjusted Funds Flow from Operations		5,038	2,620	10,247	13,284
Interest paid		(181)	(30)	(536)	(158)
Interest received		293	–	328	–
Change in non-cash working capital		(1,133)	2,139	(3,423)	(1,874)
Net cash from operating activities		4,017	4,729	6,616	11,252
Investing Activities					
Property, plant and equipment expenditures	4	(3,515)	(1,739)	(5,781)	(11,804)
Exploration and evaluation expenditures	5	(3,241)	(4,338)	(11,412)	(10,388)
Change in non-cash working capital		(761)	(1,750)	1,702	110
Net cash used in investing activities		(7,517)	(7,827)	(15,491)	(22,082)
Financing Activities					
Proceeds from issue of share capital	7	–	–	14,474	760
Share issue costs	7	20	–	(518)	(8)
Principal portion of lease payments	12	(27)	–	(80)	–
Increase in credit facilities		11,678	11,458	28,724	38,465
Repayment of credit facilities		(9,400)	(10,811)	(25,600)	(36,612)
Net cash from financing activities		2,271	647	17,000	2,605
Change in cash and cash equivalents		(1,229)	(2,451)	8,125	(8,225)
Cash and cash equivalents, beginning of period		28,562	30,062	19,208	35,836
Cash and cash equivalents, end of period		\$ 27,333	\$ 27,611	\$ 27,333	\$ 27,611

The notes are an integral part of these condensed consolidated interim financial statements.

NOTES TO THE CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS

For the three and nine months ended September 30, 2019 and 2018 (unaudited)

1. Nature of Operations and Basis of Presentation

Questerre Energy Corporation (“Questerre” or the “Company”) is an energy technology and innovation company. It is leveraging its expertise gained through early exposure to low permeability reservoirs to acquire significant high quality resources. These condensed consolidated interim financial statements of the Company as at and for the three and nine months ended September 30, 2019 and 2018 comprise the Company and its wholly-owned subsidiaries.

Questerre is incorporated under the laws of the Province of Alberta and is domiciled in Canada. The address of its registered office is 1650, 801 – 6 Avenue SW, Calgary, Alberta.

These condensed consolidated interim financial statements have been prepared in accordance with International Financial Reporting Standards (“IFRS”) as issued by the International Accounting Standards Board (“IASB”) applicable to the preparation of interim financial statements, including International Accounting Standard 34 Interim Financial Reporting. These condensed consolidated interim financial statements have been prepared following the new IFRS accounting policies and method of computation as the audited annual consolidated financial statements for the year ended December 31, 2018. Taxes in the interim periods are accrued using the tax rate that would be applicable to expected total annual net income (loss). The disclosures provided below are incremental to those included with the annual consolidated financial statements. Certain information and disclosures normally included in the notes to the annual consolidated financial statements have been condensed or have been disclosed on an annual basis only. Accordingly, these condensed consolidated interim financial statements should be read in conjunction with the audited annual consolidated financial statements for the year ended December 31, 2018, which have been prepared in accordance with IFRS as issued by the IASB.

These condensed consolidated interim financial statements of Questerre were approved by the Board of Directors on November 13, 2019.

2. Accounting Policy Changes

IFRS 16 - Leases

The Company applied IFRS 16 effective January 1, 2019. IFRS 16 requires lessees to recognize a lease obligation and right-of-use asset for the majority of leases. For leases entered into prior to January 1, 2019, the Company has chosen to measure the right-of-use assets at an amount equal to the lease liabilities, adjusted by the amount of any prepaid or accrued lease payments relating to that lease recognized in the balance sheet immediately before the date of initial application.

The Company has applied IFRS 16 using the modified retrospective approach on January 1, 2019. Therefore, comparative information has not been restated and continues to be reported under IAS 17 and IFRIC 4. The details

of accounting policies under IAS 17 and IFRIC 4 are disclosed separately if they are different from those under IFRS 16 and the impact of the changes is disclosed in Note 12.

On initial adoption, the Company elected to apply the following practical expedients permitted under the standard:

- the use of a single discount rate to a portfolio of leases with reasonably similar characteristics;
- the accounting for operating leases with a remaining lease term of less than 12 months as at January 1, 2019, as short-term leases;
- the exclusion of initial direct costs for the measurement of the right-of-use assets at the date of initial application; and
- the use of hindsight in determining the lease term where the contract contains options to extend or terminate the lease.

As a lessee, the Company previously classified leases as operating or finance leases based on its assessment of whether the lease transferred significantly all the risks and rewards incidental to ownership of the underlying asset to the Company.

Under IFRS 16, the Company recognizes right-of-use assets and lease liabilities for most leases. Certain short-term leases (less than 12 months) and leases of low-value assets are exempt from the requirements and may continue to be treated as operating leases. The right-of-use assets recognized are subsequently depreciated using the straight-line method from the commencement date to the earlier of the end of the useful life of the right-of-use assets or the end of the lease term. The estimated useful lives of right-of-use assets are determined on the same basis as those of property and equipment. In addition, the right-of-use assets are periodically reduced by impairment losses, if any, and adjusted for certain re-measurements of the lease liabilities.

The lease liabilities are initially measured at the present value of the lease payments that are not paid at the commencement date, discounted using the interest rate implicit in the lease or, if that rate cannot be readily determined, the Company's incremental borrowing rate. The Company uses its incremental borrowing rate as the discount rate.

The lease liabilities are subsequently measured at amortized cost using the effective interest method. It is re-measured when there is a change in future lease payments arising from a change in an index or rate, if there is a change in the Company's estimate of the amount expected to be payable under a residual value guarantee, or if the Company changes its assessment of whether it will exercise a purchase, extension or termination option.

When the lease liabilities are re-measured in this way, a corresponding adjustment is made to the carrying amount of the right-of-use assets or is recorded in profit or loss if the carrying amount of the right-of-use assets has been reduced to \$0. The Company presents right-of-use assets and lease liabilities separately in the balance sheet.

The application of IFRS 16 requires significant judgments and estimations to be made. Areas that require judgment include identifying whether a contract (or part of a contract) includes a lease, determining whether it is reasonably certain that an extension or termination option will be exercised, determining whether variable payments are in substance fixed, establishing whether there are multiple leases in an arrangement and determining the stand-alone amounts for lease and non-lease components. Other sources of estimation uncertainty in the application of IFRS

16 include estimating the lease term, determining the appropriate discount rate to apply to lease payments and assessing whether a right-of-use assets are impaired.

Future Accounting Pronouncements

Except as disclosed below, there were no new or amended accounting standards or interpretations issued during the three month period ended September 30, 2019, that are applicable to the Company in future periods. A detailed description of accounting standards and interpretations that will be adopted by the Company in future periods can be found in the notes to the annual consolidated financial statements for the year ended December 31, 2018.

IFRS 3 Business Combinations, 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 Business Combinations is effective for the years beginning on or after January 1, 2020. The Company is currently assessing the impact of this amendment.

3. Investment in Red Leaf

Red Leaf is a private Utah-based oil shale and technology company whose principal assets are its proprietary EcoShale technology to recover oil from shale and its oil shale leases in the state of Utah.

Questerre currently holds 132,293 common shares, representing approximately 30% of the common share capital of Red Leaf and 288 Series A Preferred Shares, representing less than 0.5% of the issued and outstanding preferred share capital of Red Leaf.

Questerre has determined its investment in Red Leaf will be accounted for using the equity method. This is based on several criteria including its current equity interest in Red Leaf and ability to participate in the decision making process of Red Leaf through its current Board representation.

The Company measured the fair market value of its investment using a net asset valuation approach. The net assets are estimated as the net current assets of Red Leaf less US\$95.58 million representing the original issue price plus accrued but unpaid dividends of the issued and outstanding Series A Preferred Shares of Red Leaf as of September 30, 2019. No value was assigned to the non-current assets of Red Leaf for the purposes of determining the fair value of the Company's investment.

The Company also evaluated the fair value of the preferred shares based on the face value excluding accrued but unpaid dividends as of September 30, 2019.

The investment balance is comprised of the following:

<i>(\$ thousands)</i>	September 30, 2019	December 31, 2018
Investment in Red Leaf	\$ 13,604	\$ 13,604
Equity loss on investment in Red Leaf	(13,325)	(13,317)
	\$ 279	\$ 287

The following table sets out the changes in investment over the respective periods:

<i>(\$ thousands)</i>	September 30, 2019	December 31, 2018
Balance, beginning of year	\$ 287	\$ 9,109
Equity loss on investment	–	(7,631)
Impairment expense	–	(1,703)
Gain (loss) on foreign exchange	(8)	512
Balance, end of period	\$ 279	\$ 287

The equity loss on investment represents the Company's proportionate share of the net loss realized by Red Leaf and the accrued but unpaid dividends on the outstanding Series A Preferred Shares for the period ending September 30, 2019. The assets, liabilities and net loss of Red Leaf as of September 30, 2019, were comprised as follows:

<i>(\$ thousands)⁽¹⁾</i>	
Cash and cash equivalents	\$ 113,291
Other current assets	281
Current liabilities	4,626
Other liabilities	1,689
Net loss ⁽²⁾	\$ (18,771)

⁽¹⁾ Converted at an exchange rate of US\$1=C\$1.3243

⁽²⁾ Converted at an average exchange rate of US\$1=C\$1.3204

For the three months ended September 30, 2019, the loss on foreign exchange relating to investments was \$0.01 million (December 31, 2018: gain of \$0.51 million) which was recorded in other comprehensive income (loss) net of a deferred tax recovery.

4. Property, Plant and Equipment

The following table provides a reconciliation of the Company's property, plant and equipment assets:

<i>(\$ thousands)</i>	Oil and Natural Gas Assets	Other Assets	Total
Cost or deemed cost:			
Balance, December 31, 2017	\$ 246,806	1,334	248,140
Additions	13,337	–	13,337
Transfer from exploration and evaluation assets	14,071	–	14,071
Balance, December 31, 2018	274,214	1,334	275,548
Additions	6,164	–	6,164
Transfer from exploration and evaluation assets	11,377	–	11,377
Balance, September 30, 2019	\$ 291,755	\$ 1,334	\$ 293,089

Accumulated depletion, depreciation and impairment losses:

Balance, December 31, 2017	\$ 147,952	1,295	149,247
Depletion and depreciation	11,751	10	11,761
Reversal of impairment	(28,024)	–	(28,024)
Balance, December 31, 2018	131,679	1,305	132,984
Depletion and depreciation	9,617	8	9,625
Other	(157)	–	(157)
Balance, September 30, 2019	\$ 141,139	\$ 1,313	\$ 142,452

<i>(\$ thousands)</i>	Oil and Natural Gas Assets	Other Assets	Total
Net book value:			
At December 31, 2018	\$ 142,535	\$ 29	\$ 142,564
At September 30, 2019	\$ 150,616	\$ 21	\$ 150,637

During the nine months ended September 30, 2019, the Company capitalized \$0.05 million of administrative overhead charges related to development activities (2018: nil). Included in the September 30, 2019, depletion calculation are future development costs of \$308.83 million (December 31, 2018: \$318.94 million). No impairment indicators were noted.

5. Exploration and Evaluation Assets

The following table provides a reconciliation of the Company's exploration and evaluation assets:

<i>(\$ thousands)</i>	September 30, 2019	December 31, 2018
Balance, beginning of year	\$ 58,092	\$ 53,675
Additions	12,180	19,740
Transfers to property, plant and equipment	(11,376)	(14,071)
Undeveloped lease expiries	(146)	(1,565)
Foreign currency translation adjustment - Jordan	(80)	313
Balance, end of period	\$ 58,670	\$ 58,092

During the period ended September 30, 2019, the Company capitalized administrative overhead charges of \$0.91 million (December 31, 2018: \$2.36 million) and \$0.64 million of share based compensation expense (December 31, 2018: \$0.92 million) directly related to exploration and evaluation activities. In the third quarter of 2019, the Company transferred investments in Kakwa and Antler totalling \$11.38 million year to date (December 31, 2018: \$14.07 million) from exploration and evaluation assets to property, plant and equipment.

In September 2018, the Ministry of Energy and Natural Resources in Quebec introduced regulations effectively prohibiting any exploitation of natural gas in the province including the banning of hydraulic fracturing of shale. The Company filed a legal motion requesting a temporary stay and judicial review to have the specific regulations relating to the ban on hydraulic fracturing to be set aside. The Company was granted a hearing date in early 2019. At the request of the Quebec Ministry of Justice, Questerre agreed to temporarily defer the judicial review in the first quarter of 2019. The Company intends to grant a further deferral until early 2020. The Company is engaged in discussions with the Quebec Government to allow the parties to resolve the issues raised in its legal motion in a constructive manner. Should the Company be unsuccessful in resolving the situation to its satisfaction or the Company's legal motion is ultimately denied, the carrying value of its exploration and evaluation assets in Quebec of \$31.5 million as of September 30, 2019, could be materially impaired.

6. Asset Retirement Obligation

The Company's asset retirement and abandonment obligations result from its ownership interest in oil and natural gas assets. The total asset retirement obligation is estimated based on the Company's net ownership interest in all wells and facilities, estimated costs to reclaim and abandon these wells and facilities, and the estimated timing of the costs to be incurred in future periods. The Company has estimated the net present value of the asset retirement obligation to be \$14.34 million as at September 30, 2019 (December 31, 2018: \$13.74 million) based on an undiscounted total future liability of \$16.46 million (December 31, 2018: \$18.47 million). These payments are expected to be made over the next 40 years. The average discount factor, being the risk-free rate related to the liabilities, is 1.59% (December 31, 2018: 1.99%). An inflation rate of 2.2% (December 31, 2018: 2.2%) over the varying lives of the assets is used to calculate the present value of the asset retirement obligation.

The following table provides a reconciliation of the Company's total asset retirement obligation:

<i>(\$ thousands)</i>	September 30, 2019	December 31, 2018
Balance, beginning of year	\$ 13,736	\$ 12,465
Liabilities incurred	(5)	174
Liabilities settled	(91)	(133)
Revisions due to change in estimates and discount rates	516	978
Accretion	162	252
Balance, end of period	\$ 14,318	\$ 13,736

7. Share Capital

The Company is authorized to issue an unlimited number of Class "A" Common voting shares ("Common Shares"). The Company is also authorized to issue an unlimited number of Class "B" Common voting shares and an unlimited number of preferred shares, issuable in one or more series. At September 30, 2019, there were no Class "B" Common voting shares or preferred shares outstanding.

a) Issued and outstanding – Common Shares

<i>(\$ thousands)</i>	Number <i>(thousands)</i>	Amount <i>(\$ thousands)</i>
Balance, December 31, 2018	389,007	\$ 415,747
Private placement	38,900	14,474
Share issue costs (net of tax effect)	–	(518)
Balance, September 30, 2019	427,907	\$ 429,703

In the second quarter of 2019, the Company completed a private placement for gross proceeds of \$14.47 million consisting of the issuance of 38.9 million Common Shares at \$0.39 per Common Share.

b) Per share amounts

Basic net income (loss) per share is calculated as follows:

<i>(thousands, except as noted)</i>	<i>Three months ended September 30,</i>		<i>Nine months ended September 30,</i>	
	2019	2018	2019	2018
Net income (loss) (\$ thousands)	\$ 1,331	\$ (2,023)	\$ (1,702)	\$ (1,392)
Issued Common Shares at beginning of period	427,907	388,412	389,007	385,331
Effect of shares issued pursuant to:				
Private placements	–	–	22,514	–
Exercise of options and warrants	–	–	–	3,282
Weighted average Common Shares outstanding (basic)	427,907	388,412	411,521	388,613
Basic net loss per share	\$ –	\$ (0.01)	\$ –	\$ –

Diluted net income (loss) per share is calculated as follows:

<i>(thousands, except as noted)</i>	<i>Three months ended September 30,</i>		<i>Nine months ended September 30,</i>	
	2019	2018	2019	2018
Net income (loss) (\$ thousands)	\$ 1,331	\$ (2,023)	\$ (1,702)	\$ (1,392)
Weighted average Common Shares outstanding (basic)	427,907	388,412	411,521	388,613
Effect of outstanding options (diluted)	684	–	–	–
Weighted average Common Shares outstanding	428,591	388,412	411,521	388,613
Diluted net loss per share	\$ –	\$ (0.01)	\$ –	\$ –

Under the current stock option plan, options can be exchanged for Common Shares, or for cash at the Company's discretion. As a result, there are 1.77 million stock options considered potentially dilutive as at September 30, 2019. The average market value of the Company's shares for purposes of calculating the dilutive effect of options was based on quoted market prices for the period that the options were outstanding. For the year to date period, due to the loss sustained, these options are considered anti-dilutive and excluded from the calculation of diluted net loss per share.

8. Share Based Compensation

The Company has a stock option program that provides for the issuance of options to its directors, officers and employees at or above grant date market prices. The options granted under the plan generally vest evenly over a three-year period starting at the grant date or one year from the grant date. The grants generally expire five years from the grant date or five years from the commencement of vesting. The Company accounts for its share-based compensation awards on the basis that the options will be equity settled.

The number and weighted average exercise prices of the stock options are as follows:

	September 30, 2019		December 31, 2018	
	Number of Options (thousands)	Weighted Average Exercise Price	Number of Options (thousands)	Weighted Average Exercise Price
Outstanding, beginning of period	21,412	\$ 0.44	21,387	\$ 0.50
Granted	6,100	0.29	3,288	0.48
Forfeited	–	–	(150)	0.52
Expired	(250)	1.40	(3,003)	0.88
Exercised	–	–	(110)	0.42
Outstanding, end of period	27,262	\$ 0.40	21,412	\$ 0.44
Exercisable, end of period	15,124	\$ 0.36	10,403	\$ 0.34

9. Capital Management

The Company believes with its recent private placement and positive expected funds flow from operations (an additional non-GAAP measure defined as net cash from operating activities before changes in non-cash working

capital and interest paid or received) in the near future, that the Company will be able to meet its foreseeable obligations in the normal course of operations. On an ongoing basis the Company reviews its commitment to incur capital expenditures to ensure that adjusted funds flow from operations or access to credit facilities are available to fund these capital expenditures. Refer to Note 11.

The volatility of commodity prices has a material impact on Questerre's adjusted funds flow from operations. Questerre attempts to mitigate the effect of lower prices by entering into risk management contracts, shutting in production in unusually low pricing environments, reallocating capital to more profitable areas and reducing capital spending based on results and other market considerations.

The Company considers its capital structure to include shareholders' equity and any outstanding amounts under its credit facilities. The Company will adjust its capital structure to minimize its cost of capital through the issuance of shares, securing credit facilities and adjusting its capital spending. Questerre monitors its capital structure based on the current and projected adjusted funds flow from operations.

<i>(\$ thousands)</i>	September 30, 2019	December 31, 2018
Credit facilities	\$ 16,966	\$ 13,842
Shareholders' equity	200,966	187,291

10. Financial Risk Management and Determination of Fair Values

a) *Overview*

The Company'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, liquidity risk and market risk. The Company manages its exposure to these risks by operating in a manner that minimizes this exposure.

b) *Fair value of financial instruments*

The Company's financial instruments as at September 30, 2019 included cash and cash equivalents, accounts receivable, deposits, investments, credit facilities, risk management contracts and accounts payable and accrued liabilities. As at September 30, 2019, the fair values of the Company's financial assets and liabilities approximate their carrying values due to the short-term maturity, with the exception of the Company's investments which are recorded at fair value.

Disclosures about the inputs to fair value measurements are required, including their classification within a hierarchy that prioritizes the inputs to fair value measurement.

Level 1 Fair Value Measurements

Level 1 fair value measurements are based on unadjusted quoted market prices.

The Company does not hold any Level 1 financial instruments.

Level 2 Fair Value Measurements

Level 2 fair value measurements are based on valuation models and techniques where the significant inputs are derived from quoted indices.

The Company's risk management contracts are considered a Level 2 instrument. The Company's financial derivative instruments are carried at fair value as determined by reference to independent monthly forward settlement prices and currency rates.

Level 3 Fair Value Measurements

Level 3 fair value measurements are based on unobservable information.

The Company's investments are considered a Level 3 instrument. The fair values are determined using a discounted cash flow approach.

As at each reporting period, the Company will assess whether a financial asset is impaired, other than those classified as fair value through profit or loss. Any impairment loss will be included in net income (loss) for the period.

c) Market risk

Market risk is the risk that changes in market prices, such as commodity prices, foreign exchange rates and interest rates will affect the Company's profit or loss or the value of its financial instruments. The objective of the Company is to mitigate exposure to these risks while maximizing returns to the Company.

Commodity price risk

Commodity price risk is the risk that the fair value or future cash flows will fluctuate as a result of changes in commodity prices. Commodity prices for oil and natural gas are impacted both by the relationship between the Canadian and United States dollar and world economic events that dictate the levels of supply and demand. The Company may enter into oil and natural gas contracts to protect, to the extent possible, its cash flows from future sales. The contracts reduce the volatility in sales revenue by locking in prices with respect to future deliveries of oil and natural gas.

As at September 30, 2019, the Company held a risk management contract for 200 bbls/d at US\$58.50/bbl for the three months ending December 31, 2019. The realized gain on risk management contracts for the quarter ended September 30, 2019 was \$0.04 million and the unrealized gain was \$0.11 million.

d) Credit risk

Credit risk represents the potential financial loss to the Company if a customer or counterparty to a financial instrument fails to meet or discharge their obligation to the Company. Credit risk arises principally from the Company's receivables from joint venture partners and oil and gas marketers.

11. Credit Facilities

As at September 30, 2019, the credit facilities include a revolving operating demand facility of \$17.9 million (“Credit Facility A”) and a corporate credit card of \$0.1 million (“Credit Facility B”). Credit Facility A can be used for general corporate purposes, ongoing operations and capital expenditures within Canada.

Based on discussions with the lender in the fourth quarter, the Company anticipates its credit facilities will increase from \$18 million to \$20 million.

Any borrowing under the credit facilities, with the exception of letters of credit, bears interest at the bank’s prime interest rate and an applicable basis point margin based on the ratio of debt to cash flow measured quarterly. The bank’s prime rate currently is 2.70% per annum and the effective interest rate for the quarter was 4.45%. The credit facilities are secured by a debenture with a first floating charge over all assets of the Company and a general assignment of books debts. Under the terms of the credit facility, the Company has provided a covenant that it will maintain an Adjusted Working Capital Ratio greater than 1.0. The ratio is defined as current assets (excluding unrealized hedging gains and including undrawn Credit Facility A availability) to current liabilities (excluding bank debt outstanding and unrealized hedging losses). The Adjusted Working Capital Ratio at September 30, 2019 was 1.81 and the covenant was met. At September 30, 2019, \$16.97 million (December 31, 2018: \$13.84 million) was drawn on Credit Facility A.

The current commodity price environment has resulted in tighter capital markets. The credit facilities are demand facilities and can be reduced, amended or eliminated by the lender for reasons beyond the Company’s control. Should the credit facilities, in fact, be reduced or eliminated, the Company would need to seek alternative credit facilities or consider the issuance of equity to enhance its liquidity.

12. Right-of-use Assets and Lease Liabilities

a) *Right-of-use assets*

<i>(\$ thousands)</i>	Real Estate		Other		Total
Cost					
Balance, January 1, 2019	\$	198	\$	–	\$ 198
Additions		–		25	25
Balance, September 30, 2019	\$	198	\$	25	\$ 223
Accumulated Depreciation					
Balance, January 1, 2019	\$	–	\$	–	\$ –
Depreciation		78		2	80
Balance, September 30, 2019	\$	78	\$	2	\$ 80
Carrying value					
Balance, January 1, 2019	\$	198	\$	–	\$ 198
Additions, net of depreciation		(78)		23	(55)
Balance, September 30, 2019	\$	120	\$	23	\$ 143

The associated right-of-use assets were measured at the amount equal to the lease liabilities on January 1, 2019 with no impact on retained earnings.

b) *Lease liabilities*

A reconciliation of the gross future minimum lease payments on operating lease commitments, as disclosed in Note 19 of the Annual Report for the year ended December 31, 2018, to the lease liabilities as at January 1, 2019 is as follows:

<i>(\$ thousands)</i>	
Operating lease commitments disclosed as at December 31, 2018	\$ 256
Discounted using the incremental borrowing rate as at January 1, 2019	246
(Less): short-term leases recognized on a straight-line basis as expense	(20)
(Less): low-value leases recognized on a straight-line basis as expense	(28)
Lease liability recognized as at January 1, 2019	\$ 198

Maturity analysis - undiscounted cash flows as at September 30, 2019:

Current portion	114
Long term portion	38
Total undiscounted lease liabilities as at September 30, 2019	\$ 152

Lease Liabilities	
Balance, January 1, 2019	198
Additional leases during period	25
Interest expense	7
Lease payments	(84)
Balance, September 30, 2019	\$ 146
Current portion	110
Long term portion	36
Balance, September 30, 2019	\$ 146

Amounts related to lease liabilities recognized in profit or loss are as follows:

Interest expense on lease liabilities	\$ 7
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On adoption of IFRS 16, the Company recognized lease liabilities in relation to leases which had previously been classified as operating leases under the principles of IAS 17, "Leases" ("IAS 17"). Under the principles of the new standard these leases have been measured at the present value of the remaining lease payments, discounted using the Company's incremental borrowing rates at January 1, 2019 estimated at 4.14%. Leases with a remaining term of less than twelve months and low-value leases were excluded. Interest expense related to leases are included in "Interest paid" under Operating Activities on the Statements of Cash Flow.