

SUNSET PACIFIC PETROLEUM LTD.
CONSOLIDATED FINANCIAL STATEMENTS
(expressed in Canadian Dollars)
DECEMBER 31, 2018 AND 2017

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charlton & company
CHARTERED PROFESSIONAL ACCOUNTANTS

INDEPENDENT AUDITORS' REPORT

To: the Shareholders of
Sunset Pacific Petroleum Ltd.

Opinion

We have audited the consolidated financial statements of Sunset Pacific Petroleum Ltd. (the "Company"), which comprise the consolidated statements of financial position as at December 31, 2018 and December 31, 2017, and the consolidated statements of operations and comprehensive loss, changes in shareholders equity and cash flows for the years then ended, and 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 financial position of the Company as at December 31, 2018 and December 31, 2017, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards (IFRSs).

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 Auditor's 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 audit of the consolidated 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 is sufficient and appropriate to provide a basis for our opinion.

Material Uncertainty Related to Going Concern

We draw attention to Note 1 of the consolidated financial statements, which indicates that the Company has an accumulated deficit of \$23,807,582 and a working capital deficiency of \$1,476,394. As stated in Note 1, these events and conditions 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 the Management 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 audit of the consolidated financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the consolidated financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

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 IFRSs, 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.

Auditor's Responsibilities for the Audit of the 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 auditor's 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 consolidated 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 auditor's report to the related disclosures in the 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 auditor's 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.
- Obtain sufficient appropriate audit evidence regarding the consolidated financial information of the entities or business activities within the Group 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 auditor's report is Robert G. Charlton.

Charlton & Company

CHARTERED PROFESSIONAL ACCOUNTANTS

Vancouver, BC

July 3, 2019

SUNSET PACIFIC PETROLEUM LTD.

CONSOLIDATED STATEMENTS OF FINANCIAL POSITION

(Expressed in Canadian dollars)

	<u>ASSETS</u>	
	<u>December 31,</u> <u>2018</u>	<u>December 31,</u> <u>2017</u>
CURRENT		
Cash	\$ 151	\$ 54,000
Sales tax recoverable	13,651	8,032
Prepaid expenses	616	-
	<u>\$ 14,418</u>	<u>\$ 62,032</u>
	<u>LIABILITIES</u>	
CURRENT		
Accounts payable (Note 9)	\$ 362,458	\$ 303,173
Accrued liabilities	467,028	455,446
Loans payable (Note 4)	660,710	409,804
	<u>1,490,196</u>	<u>1,168,423</u>
	<u>SHAREHOLDERS' DEFICIENCY</u>	
SHARE CAPITAL (Note 5)	20,953,987	20,953,987
CONTRIBUTED SURPLUS (Note 5)	1,377,817	1,377,817
DEFICIT	(23,807,852)	(23,438,195)
	<u>(1,475,778)</u>	<u>(1,106,391)</u>
	<u>\$ 14,418</u>	<u>\$ 62,032</u>

NATURE AND CONTINUANCE OF OPERATIONS (Note 1)

COMMITMENTS (Note 9)

CONTINGENT LIABILITIES (Note 9)

APPROVED AND AUTHORIZED FOR ISSUE BY THE BOARD ON July 3, 2019.

"Dennis Luk"

"Belkacem Aissaoui"

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

SUNSET PACIFIC PETROLEUM LTD.

CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE LOSS

FOR THE YEARS ENDED DECEMBER 31, 2018 AND 2017

(Expressed in Canadian dollars)

	<u>2018</u>	<u>2017</u>
EXPENSES		
Consulting fees	\$ 181,870	\$ 224,250
Filing fees and transfer agent	24,236	10,234
Interest expense	57,158	51,462
Office and miscellaneous	42,220	43,399
Professional fees	33,903	43,701
Rent	30,000	30,000
Stock based compensation (Note 5)	-	29,032
Travel, parking and promotion	-	-
Wages and salaries	-	-
	<u>369,387</u>	<u>432,078</u>
LOSS BEFORE OTHER ITEMS	<u>(369,387)</u>	<u>(432,078)</u>
OTHER INCOME (LOSS):		
Write down of oil and gas properties (Note 3)	-	(9,400)
Write off of accounts payable	<u>-</u>	<u>77,692</u>
	<u>-</u>	<u>68,392</u>
LOSS AND COMPREHENSIVE LOSS FOR THE YEAR	<u>\$ (369,387)</u>	<u>\$(363,786)</u>
Basic and diluted loss per common share	<u>\$ (0.01)</u>	<u>\$ (0.01)</u>
Weighted average number of common shares outstanding	<u>73,936,934</u>	<u>72,395,030</u>

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

SUNSET PACIFIC PETROLEUM LTD.

CONSOLIDATED STATEMENTS OF CASH FLOWS

FOR THE YEARS ENDED DECEMBER 31, 2018 AND 2017

(Expressed in Canadian dollars)

	<u>2018</u>	<u>2017</u>
OPERATING ACTIVITIES		
Net loss for the year	\$ (369,387)	\$ (363,786)
Items not involving cash:		
Stock based compensation	-	29,032
Accrued interest on loans payable	49,707	44,335
Write off of accounts payable	-	(77,692)
Write down of oil and gas properties	-	9,400
	<u>(319,680)</u>	<u>(358,711)</u>
Changes in non-cash working capital items:		
Sales tax receivable	(5,619)	(5,811)
Prepaid Expenses	(616)	
Accounts payable	59,285	4,924
Accrued liabilities	<u>11,582</u>	<u>(2,735)</u>
	<u>(255,048)</u>	<u>(362,333)</u>
FINANCING ACTIVITIES		
Proceeds from loans payable	201,199	415,898
Repayment of loans payable	-	(252,000)
Proceeds from issuance of shares	-	252,000
Subscriptions received	<u>-</u>	<u>-</u>
	<u>201,199</u>	<u>415,898</u>
CHANGE IN CASH	(53,849)	53,565
CASH BEGINNING OF YEAR	<u>54,000</u>	<u>435</u>
CASH , END OF YEAR	<u>\$ 151</u>	<u>\$ 54,000</u>
Cash paid for:		
Interest	\$ -	\$ -
Income taxes	\$ -	\$ -
	<u><u>-</u></u>	<u><u>-</u></u>
Cash received for:		
Interest	\$ -	\$ -
	<u><u>-</u></u>	<u><u>-</u></u>

SUPPLEMENTAL CASHFLOW INFORMATION (Note 12)

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

SUNSET PACIFIC PETROLEUM LTD.

CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY

AS AT DECEMBER 31, 2018 AND 2017

(Expressed in Canadian dollars)

Share capital							
Notes	Number of shares	Amount	Reserves	Deficit	Total		
Balance at December 31, 2017	73,936,934	\$ 20,953,987	\$ 1,377,817	\$ (23,438,195)	\$ (1,106,391)		
Comprehensive income:							
Loss for the year	-	-	-	(369,387)	(369,387)		
Stock options granted	-	-	-	-	-		
Warrants Exercised	-	-	-	-	-		
Balance at December 31, 2018	73,936,934	\$ 20,953,987	\$ 1,377,817	\$ (23,807,582)	\$ (1,475,778)		

Share capital							
Notes	Number of shares	Amount	Reserves	Deficit	Total		
Balance at December 31, 2016	70,336,934	\$ 20,701,987	\$ 1,348,785	\$ (23,074,409)	\$ (1,023,637)		
Comprehensive income:							
Loss for the year	-	-	-	(363,786)	(363,786)		
Warrants exercised	3,600,000	252,000	-	-	252,000		
Stock options granted	-	-	29,032	-	29,032		
Balance at December 31, 2017	73,936,934	\$ 20,953,987	\$ 1,377,817	\$ (23,438,195)	\$ (1,106,391)		

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

1. NATURE AND CONTINUANCE OF OPERATIONS

The Company was incorporated under the British Columbia Company Act (subsequently transitioned under the British Columbia Corporations Act) on May 14, 1981 and is registered extra-provincially in Alberta. The Company's registered office is located at 1100 – 736 Granville Street, Vancouver BC, V6C 1G3.

The Company is a junior resource exploration company engaged in the acquisition, exploration, and development of natural resource properties (primarily oil and gas). The Company and its subsidiaries do not have producing resource properties at this time. The Company's business is presently focused on the exploration and evaluation of various oil and gas properties in North Africa and the Middle East.

During the year ended December 31, 2018, the Company incurred a loss of \$369,387 (2017: \$363,786) and has an accumulated deficit of \$23,807,582 (December 31, 2017: \$23,438,195). Cash at December 31, 2018 was \$151 (December 31, 2017: \$54,000). The Company had a working capital deficiency of \$1,476,394 at December 31, 2018 (December 31, 2017: \$1,106,391) all of which indicate the existence of a material uncertainty that may cast substantial doubt about the Company's ability to continue as a going concern.

As a junior exploration stage company, the Company is currently unable to self-finance its operations. The ability of the Company to carry on as a going concern and the ultimate recovery of the Company's investment in its oil and gas properties is dependent upon the discovery, development and sale of oil and gas reserves, the ability to joint venture or sell its resource properties and the ability to raise sufficient capital to finance this operation. The Company continues to seek new capital, and will continue to require additional funds to both finance its administrative expenditures and meet its property commitments. The ultimate outcome of these operations cannot presently be determined because they are contingent on future matters. These financial statements do not include the adjustments to the amounts and classification of assets and liabilities that might be necessary should the Company be unable to continue as a going concern.

2. SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation

Statement of compliance with IFRS

The consolidated financial statements of the Company for the year-ending December 31, 2018 have been prepared in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB") and interpretations of the International Financial Reporting Interpretations Committee ("IFRIC").

These statements were authorized for issuance by the Board of Directors on July 3, 2019.

Basis of measurement

These financial statements have been prepared on an accrual basis and based on historical costs, modified where applicable. The financial statements are presented in Canadian dollars, which is also the functional currency of the Company and its subsidiary.

Use of estimates and judgments

The preparation of financial statements in conformity with IFRS requires management to make estimates, assumptions and judgments that affect the application of policies and reported amounts of assets and liabilities and disclosures of assets and liabilities at the date of the financial statements, along with reported amounts of expenses and net losses during the period. Actual results may differ

2. SIGNIFICANT ACCOUNTING POLICIES (continued)

from these estimates, and as such, estimates and underlying assumptions are reviewed on an ongoing basis. Revisions are recognized in the period in which the estimates are revised and in any future periods affected.

Estimates

Significant assumptions about the future and other sources of estimation uncertainty that management has made at the financial position reporting date that could result in a material adjustment to the carrying value of assets and liabilities, in the event that actual results differ from assumptions made, relate to, but are not limited to, the following:

- The recoverability of oil and gas properties and deferred expenditures incurred on its Canadian projects. The Company's reserve estimates are evaluated annually consistent with NI 51-101 – Standards of Disclosure for Oil and Gas Activities.
- the inputs in accounting for share-based payment transactions in the statement of loss and comprehensive loss (using the Black-Scholes model) including volatility, probable life of options granted, time of exercise of the options and forfeiture rate;

Judgments

Significant accounting judgments that management has made at the financial position reporting date relate to, but are not limited to, the following:

- The recoverability of accounts on the statement of financial position;
- whether a past event has led to a liability that should be recognized in the consolidated statement of financial position or disclosed as a contingent liability;
- the assessment of the Company's ability to continue as a going concern and execute its strategy by funding future working capital requirements.

Basis of consolidation

The consolidated financial statements include the accounts of its wholly owned subsidiary Bighorn Exploration Ltd. (formerly Zarcán Minerals Inc.), a company incorporated under the laws of the Province of British Columbia.

Details of controlled entities are as follows:

	Country of incorporation	Percentage owned*	
		December 31, 2018	December 31, 2017
Bighorn Exploration Ltd. (formerly Zarcán Minerals Inc.)	Canada	100%	100%

*Percentage of voting power is in proportion to ownership.

Inter-company balances and transactions, including unrealized income and expenses arising from inter-company transactions, are eliminated on consolidation.

2. SIGNIFICANT ACCOUNTING POLICIES (continued)

Exploration and evaluation expenditures

Exploration and evaluation expenditures, including the costs of acquiring licenses and exploratory drilling are capitalized as either tangible or intangible exploration and evaluation assets according to the nature of the assets acquired. The costs are accumulated in cost centers by well, field or exploration area pending determination of technical and commercial feasibility.

Exploration and evaluation assets are not subject to depletion as these assets are generally not yet producing.

Impairment

As long as the exploration and evaluation assets remain classified as intangible exploration and evaluation assets, they are subject to technical, commercial, and management review, as well as review for indicators of impairment at each reporting period. If there are indicators of impairment, exploration and evaluation assets are tested for impairment at the cash generating unit level. Exploration and evaluation assets are derecognized when the legal right to explore has expired or when the asset is no longer expected to generate value.

The technical feasibility and commercial viability of extracting a resource is considered to be determinable when proved resources are proven to exist. A review of each exploration license or field is carried out, at least annually, to ascertain whether proved reserves have been discovered. Upon determination of proved reserves, exploration and evaluation assets attributable to those reserves are first tested for impairment and then reclassified from exploration and evaluation assets to a separate category within property and equipment referred to as petroleum and natural gas interests.

Development and production costs

Items of property and equipment referred to as petroleum and natural gas interests, which include petroleum and natural gas development and production assets, are measured at cost less accumulated depletion and depreciation and accumulated impairment losses. Development and production assets are grouped into cash generating units for impairment testing. When significant items of property, plant and equipment, including petroleum and natural gas interests, have different useful lives, they are accounted for as separate items.

Gains and losses on disposal of an item of property and equipment, including petroleum and natural gas interests, are determined by comparing the proceeds from disposal with the carrying amount of the property and equipment and are recognized net within “other income” or “other expenses” in the statement of comprehensive income.

Subsequent costs

Costs incurred subsequent to the determination of technical feasibility and commercial viability and the costs of replacing parts of property and equipment 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 expensed to the statement of comprehensive income 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 a geotechnical area basis. The carrying amount of any replaced or sold component is derecognized. The costs of day-to-day servicing of property and equipment are expensed as incurred.

2. SIGNIFICANT ACCOUNTING POLICIES (continued)

Depletion

The net carrying value of development or production assets is depleted using the units of production method be reference to the units produced in the year as a percentage of the related proved reserves, taking into account estimated future development costs necessary to bring those reserves into production. Future development costs are estimated taking into account the level of development required to produce the reserves.

Reserves are estimated using reserve engineer reports and represent the estimated quantities of crude petroleum, 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 that are determined to be commercially producible. There should be a 90 percent statistical probability that the actual quantity of recoverable reserves will be more than the amount estimated as proved reserves and a 10 percent statistical probability that it will be less. The equivalent statistical probabilities for the probable component of the proved and probable reserves are 50 percent and 50 percent, respectively.

Such reserves may be commercially producible if management has the intention of developing and producing them and such intention is based upon:

- 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 petroleum and natural gas production;
- evidence that necessary production, transmission and transportation facilities are available or can be made available.

Provisions

When the Company has a present legal or constructive obligation as a result of a past event, a provision is recognized only when the obligation is estimated reliably, and it is probable that an outflow of economic benefits will be required to settle the obligation.

Provisions are measured at the present value of the expenditure expected to be required to settle the obligation using a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the obligation. The increase in the obligation due to the passage of time is recognized as finance expense.

Restoration and environmental obligations

The Company recognizes liabilities for statutory, contractual, constructive or legal obligations associated with the retirement of long-term assets, when those obligations result from the acquisition, construction, development or normal operation of the assets. The net present value of future restoration cost estimates arising from the decommissioning of plant and other site preparation work is capitalized to exploration and evaluation assets along with a corresponding increase in the restoration provision in the period incurred. Discount rates using a pre-tax rate that reflect the time value of money are used to calculate the net present value. The restoration asset will be depreciated on the same basis as other mining assets.

2. SIGNIFICANT ACCOUNTING POLICIES (continued)

The Company's estimates of restoration costs could change as a result of changes in regulatory requirements, discount rates and assumptions regarding the amount and timing of the future expenditures. These changes are recorded directly to mining assets with a corresponding entry to the restoration provision. The Company's estimates are reviewed annually for changes in regulatory requirements, discount rates, effects of inflation and changes in estimates.

Changes in the net present value, excluding changes in the Company's estimates of reclamation costs, are charged to profit and loss for the period.

The net present value of restoration costs arising from subsequent site damage that is incurred on an ongoing basis during production are charged to profit or loss in the period incurred. The costs of restoration projects that were included in the provision are recorded against the provision as incurred. The costs to prevent and control environmental impacts at specific properties are capitalized in accordance with the Company's accounting policy for exploration and evaluation assets.

Revenue Recognition

The Company records royalty revenue in accordance with the contract terms once it can be reliably measured and the collection is reasonably assured.

Share base compensation

Where equity-settled share options are awarded to employees, the fair value of the options at the date of grant is charged to the statement of comprehensive loss/income over the vesting period. Performance vesting conditions are taken into account by adjusting the number of equity instruments expected to vest at each reporting date so that, ultimately, the cumulative amount recognized over the vesting period is based on the number of options that eventually vest. Non-vesting conditions and market vesting conditions are factored into the fair value of the options granted. As long as other vesting conditions are satisfied, a charge is made irrespective of whether these vesting conditions are satisfied. The cumulative expense is not adjusted for failure to achieve a market vesting condition or where a non-vesting condition is not satisfied.

Where equity instruments are granted to employees, they are recorded at the fair value of the equity instrument granted at the grant date. The grant date fair value is recognized in comprehensive loss/income over the vesting period, described as the period during which all the vesting conditions are to be satisfied.

Where equity instruments are granted to non-employees, they are recorded at the fair value of the goods or services received in the statement of comprehensive loss/income, unless they are related to the issuance of shares. Amounts related to the issuance of shares are recorded as a reduction of share capital.

When the value of goods or services received in exchange for the share-based payment cannot be reliably estimated, the fair value is measured by use of a valuation model. The expected life used in the model is adjusted, based on management's best estimate, for the effects of non-transferability, exercise restrictions, and behavioral considerations.

All equity-settled share-based payments are reflected in contributed surplus, until exercised. Upon exercise, shares issued from treasury and the amount reflected in contributed surplus is credited to share capital, adjusted for any consideration paid.

2. SIGNIFICANT ACCOUNTING POLICIES (continued)

Where a grant of options is cancelled or settled during the vesting period, excluding forfeitures when vesting conditions are not satisfied, the Company immediately accounts for the cancellation as an acceleration of vesting and recognizes the amount that otherwise would have been recognized for services received over the remainder of the vesting period. Any payment made to the employee on the cancellation is accounted for as the repurchase of an equity interest except to the extent the payment exceeds the fair value of the equity instrumented granted, measured at the repurchase date. Any such excess is recognized as an expense.

Where the terms and conditions of options are modified before they vest, the increase in the fair value of the options, measured immediately before and after the modification, is also charged to the statement of comprehensive loss/income over the remaining vesting period.

Financial instruments

The Company adopted all of the requirements of IFRS 9 Financial Instruments (“IFRS 9”) as of January 1, 2018. IFRS 9 replaces IAS 39 Financial Instruments: Recognition and Measurement (“IAS 39”). IFRS 9 utilizes a revised model for recognition and measurement of financial instruments and a single, forward-looking “expected loss” impairment model. Most of the requirements in IAS 39 for classification and measurement of financial liabilities were carried forward in IFRS 9, so the Company’s accounting policy with respect to financial liabilities is unchanged. As a result of the adoption of IFRS 9, management has changed its accounting policy for financial assets retrospectively, for assets that continued to be recognized at the date of initial application. The change did not impact the carrying value of any financial assets or financial liabilities on the transition date.

(i) Classification

The Company classifies its financial instruments in the following categories: at fair value through profit and loss (“FVTPL”), at fair value through other comprehensive income (loss) (“FVTOCI”) or at amortized cost. The Company determines the classification of financial assets at initial recognition. The classification of debt instruments is driven by the Company’s business model for managing the financial assets and their contractual cash flow characteristics. Equity instruments that are held for trading are classified as FVTPL. For other equity instruments, on the day of acquisition the Company can make an irrevocable election (on an instrument-by-instrument basis) to designate them as at FVTOCI. Financial liabilities are measured at amortized cost, unless they are required to be measured at FVTPL (such as instruments held for trading or derivatives) or if the Company has opted to measure them at FVTPL.

The Company completed a detailed assessment of its financial assets and liabilities as at January 1, 2018. The following table shows the original classification under IAS 39 and the new classification under IFRS 9:

Financial assets/liabilities	Original classification IAS 39	New classification IFRS 9
Cash and cash equivalents	FVTPL	FVTPL
Accounts payable and accrued liabilities	Amortized cost	Amortized cost
Loans payable	Amortized cost	Amortized cost

The Company did not restate prior periods as it recognized the effects of retrospective application to shareholders’ equity at the beginning of the 2018 annual reporting period, which also includes the date

SUNSET PACIFIC PETROLEUM LTD.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2018 AND 2017
(Expressed in Canadian dollars)

of initial application. The adoption of IFRS 9 resulted in no impact to the opening accumulated deficit nor to the opening balance of accumulated other comprehensive income on January 1, 2018.

(ii) Measurement

Financial assets and liabilities at amortized cost are initially recognized at fair value plus or minus transaction costs, respectively, and subsequently carried at amortized cost less any impairment.

Financial assets and liabilities carried at FVTPL are initially recorded at fair value and transaction costs are expensed in the statements of loss. Realized and unrealized gains and losses arising from changes in the fair value of the financial assets and liabilities held at FVTPL are included in the statements of loss in the period in which they arise.

(iii) Impairment of financial assets at amortized cost

The Company recognizes a loss allowance for expected credit losses on financial assets that are measured at amortized cost. At each reporting date, the Company measures the loss allowance for the financial asset at an amount equal to the lifetime expected credit losses if the credit risk on the financial asset has increased significantly since initial recognition. If at the reporting date, the financial asset has not increased significantly since initial recognition, the Company measures the loss allowance for the financial asset at an amount equal to the twelve month expected credit losses. The Company shall recognize in the statements of loss, as an impairment gain or loss, the amount of expected credit losses (or reversal) that is required to adjust the loss allowance at the reporting date to the amount that is required to be recognized.

(iv) Derecognition of financial assets

The Company derecognizes financial assets only when the contractual rights to cash flows from the financial assets expire, or when it transfers the financial assets and substantially all of the associated risks and rewards of ownership to another entity. Gains and losses on derecognition are generally recognized in the statements of loss.

The required disclosures are included in Note 11.

Basic and Diluted Loss Per Share

Loss per common share is calculated using the weighted average number of common shares issued and outstanding during each year. Diluted loss per common share is calculated using the treasury stock method which assumes that stock options are only exercised when the exercise price is below the average market price during the period, and that the Company will use these proceeds to purchase its common shares at their average market price during the period. In the years when the Company reports a net loss, the effect of potential issuances of shares under options would be anti-dilutive and, therefore, basic and diluted losses per share are the same.

Existing stock options and share purchase warrants have not been included in the computation of diluted loss per share as to do so would be anti-dilutive. Accordingly, basic and diluted loss per share are the same for the years presented.

Comprehensive Loss

Comprehensive loss reflects net loss and other comprehensive income (loss) for the period. Other comprehensive income (loss) includes changes in unrealized foreign currency translation amounts arising from self-sustaining foreign operations, unrealized gains and losses on available-for-sale assets and changes in the fair value of derivatives designated as cash flow hedges to the extent they are effective.

2. SIGNIFICANT ACCOUNTING POLICIES (continued)

Income Taxes

The Company accounts for income taxes using the asset and liability method, whereby deferred income tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted or substantially enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the date of enactment or substantive enactment. Deferred income tax assets are recognized to the extent that they are considered more likely than not to be realized. The valuation of deferred income tax assets is adjusted, if necessary, by the use of a valuation allowance to reflect the estimated realizable amount.

Warrants

Proceeds from issuances by the Company of units consisting of shares and warrants are allocated based on the residual method, whereby the carrying amount of the warrants is determined based on any difference between gross proceeds and the estimated fair market value of the shares. If the proceeds from the offering are less than or equal to the estimated fair market value of shares issued, a nil carrying amount is assigned to the warrants.

Impairment of non-financial assets

The Company assesses at each date of the statement of financial position the carrying amounts of non-financial assets to determine whether there is indication that those assets have incurred an impairment loss. If such an indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss. Where it is not possible to estimate the recoverable amount of an individual asset, the Company estimates the recoverable amount of the cash-generating unit to which the assets belong.

Recoverable amount is the greater of the fair value less costs to sell and value in use. In determining fair value less costs to sell, recent market transactions are taken into account, if available. If it is not possible to determine the fair value less costs to sell, the asset's value in use can be used as the recoverable amount. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments for the time value of money and risks specific to the asset.

If the recoverable amount of an asset (or cash generating unit) is estimated to be less than its carrying amount, the carrying amount of the asset (or cash generating unit) is reduced to its recoverable

2. SIGNIFICANT ACCOUNTING POLICIES (continued)

amount. An impairment loss is recognized immediately in the statement of operations and comprehensive loss. Where an impairment loss subsequently reverses, the carrying amount of the asset (or cash generating unit) is increased to the revised estimate of the recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognized for the asset (or cash generating unit) in prior year. A previously recognized impairment loss is reversed only if there has been a change in the assumptions used to determine the asset's recoverable amount since the last impairment loss was recognized.

Future accounting changes

The following new standards and interpretations are not yet effective and have not been applied in preparing these financial statements. The Company is currently evaluating the potential impacts of these new standards and does not anticipate any material changes to the financial statements upon adoption of these new and revised accounting pronouncements.

IFRS 16 – Leases (effective January 1, 2019) introduces new requirements for the classification and measurement of leases.

The Company anticipates that the application of these standards, amendments and interpretations will not have a material impact on the results and financial position of the Company.

3. OIL AND NATURAL GAS PROPERTIES

Royalty Interests – Bougie Trutch and Trutch East

On October 14, 2005 the company acquired a 2.5% overriding royalty in the Bougie Trutch oil and gas project in north eastern British Columbia for \$29,000 paid for by the issuance of 100,000 common shares. A total of 5 halfway wells have been drilled on this property. Production from two wells commenced in February 2007 and the production from the third well started in January 2008. Of the remaining two wells one was capped and the other was abandoned.

On November 30, 2006 the company acquired a 2.5% over-riding royalty in the Trutch East natural gas lease package (15 square miles) for \$250,000. Under the terms of the Trutch East Participation Agreement, the Company will have the right to earn a 2.5% rolling over-riding interest in the 15 sections of Trutch East lands. The property has one producing well. Production commenced in February 2007.

At December 31, 2017, management determined that the carrying amount of the Bougie Trutch project was greater than its recoverable amount of \$Nil. The recoverable amount of the property was its value in use as it was not possible to make a reliable estimate of the project's fair value less costs to sell.

During the year ended December 31, 2017, the Company wrote off \$9,400 (2016: \$9,600) which is included in write down of oil and gas properties on the consolidated statement of operations and comprehensive loss.

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3. OIL AND NATURAL GAS PROPERTIES (continued)

CONSOLIDATED SCHEDULE OF OIL AND GAS PROPERTY COSTS

FOR THE YEARS ENDED DECEMBER 31, 2018 AND 2017

Year Ended December 31, 2017

	Royalty Interests- <u>Trutch</u>
Balance, beginning of year	\$ 9,400
Additions: Lease payments	-
Other items	-
Write down	<u>(9,400)</u>
Balance, end of year	<u>\$ Nil</u>

Year Ended December 31, 2018

	Royalty Interests- <u>Trutch</u>
Balance, beginning of year	\$ Nil
Additions: Lease payments	-
Other items	-
Write down	<u>-</u>
Balance, end of year	<u>\$ Nil</u>

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4. LOAN PAYABLE

	2018	2017
Loan #1	\$ 279,845	\$ 230,139
Loan #2 to #4	192,165	15,965
Subscription loans	188,700	163,700
Total	<u>\$ 660,710</u>	<u>\$ 409,804</u>

During the year ended December 31, 2011, the Company entered into loan agreements with several parties for a total amount of \$333,526. Loan #1 had an original principal amount of \$60,000 and bears interest at 20% per annum compounded monthly and is due on demand. Loans #2 to #4 bears no interest and have no fixed terms of repayment.

During the year ended December 31, 2018, the Company received \$25,000 (2017-\$163,700) for a planned private placement. The private placement was subsequently withdrawn by the exchange and as such the Company is holding the placement funds in the amount of \$188,700 as loans payable with no interest and no fixed terms of repayment.

During the year ended December 31, 2018, the company received new loans totaling \$176,200 (2017 – repaid \$252,000).

During the year ended December 31, 2018, interest expense for the interest bearing loan of \$49,707 (2017- \$44,335) was accrued in loan payable.

5. SHARE CAPITAL

(a) Authorized:

An unlimited number of common shares without par value.

(b) Issued and outstanding:

Please refer to the statement of changes in shareholder's equity

The Company did not close any private placements during the years ended December 31, 2018 and 2017.

5. SHARE CAPITAL (continued)

(c) Stock options

The Company has a stock option plan pursuant to which, the Company may grant options to eligible directors and employees of the Company, up to a maximum of 10% of the total number of outstanding common shares. Options may be issued under the stock option plan at the sole discretion of the Company's Board of Directors. The exercise price will be set by the Company's Board of Directors at the time the option is granted, and cannot be less than the discounted market price. Vesting terms of the option will be determined at the discretion of the Board of Directors. Options may be granted for a maximum of ten years from the date of the grant.

Summary of stock option activity

	Number of Options	Weighted Average Exercise Price \$
Balance, December 31, 2016	6,638,696	0.07
Cancelled	(2,772,856)	0.08
Granted	1,800,000	0.05
Balance, December 31, 2017 & 2018	5,665,840	0.07

The following table provides detailed information about stock options outstanding and exercisable at December 31, 2018

Options Outstanding	Exercise Price	Expiry Date	Weighted Average Remaining Life (years)
1,000,000	\$ 0.07	February 26, 2019*	0.16
800,000	0.105	May 15, 2019 *	0.37
250,000	0.15	October 16, 2019	0.79
1,815,840	0.05	October 11, 2021	2.78
<u>1,800,000</u>	0.05	October 25, 2022	<u>3.82</u>
5,665,840			2.57

* expired unexercised subsequent to year end.

The options granted vested on the grant date. The fair value of each option is estimated on the grant date using the Black-Scholes option valuation model assuming no expected dividends. The assumptions used in calculating fair value are as follows:

	2018	2017
Risk free interest rate	-	1.71%
Expected life (in years)	-	5
Expected volatility	-	135%
Expected dividend yield	-	0%

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5. SHARE CAPITAL (continued)

(c) Options (continued)

On January 18, 2018 the Company announced the grant of incentive stock options to certain directors, officers and consultants of the Company to purchase up to an aggregate of 925,000 common shares of the Company pursuant to the Company's share option plan. The options are exercisable for a period of five years at a price of \$0.05/share. These options are subject to regulatory approval.

Share based compensation recorded during the year ended December 31, 2018 was \$Nil (2017 - \$29,032)

(d) Warrants

Summary of warrant activity:

	Number of Warrants	Weighted Average Exercise Price
Balance, December 31, 2016	39,365,065	\$0.09
Exercised	(3,600,000)	\$0.07
Balance, December 31, 2017 and 2018	35,765,065	\$0.09

A summary of the warrants outstanding as of December 31, 2018 is presented below:

<u>Options Warrants</u>		<u>Exercise Price</u>	<u>Expiry Date</u>	<u>Weighted Average Remaining Life (years)</u>
1,283,333	\$	0.07	March 19, 2019*	0.21
2,666,666		0.17	July 29, 2019	0.58
1,666,666		0.17	August 26, 2019	0.65
350,000		0.15	November 6, 2019	0.85
293,000		0.15	December 19, 2019	0.97
3,814,400		0.10	March 11, 2020	1.19
3,695,000		0.10	June 25, 2020	1.48
1,980,000		0.07	October 30, 2020	1.83
4,016,000		0.07	May 13, 2021	2.36
<u>16,000,000</u>		0.07	October 11, 2021	<u>2.78</u>
35,765,065				1.95

* expired unexercised subsequent to year end.

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6. RELATED PARTY TRANSACTIONS

The Company has identified certain directors and certain senior officers as its key management personnel. The compensation costs for key management personnel for the years ended December 31, 2018 and 2017 are as follows:

	December 31	
	2017	2017
Share-based compensation	\$ -	\$ 20,968
Consulting fees	-	5,000
Travel	-	-
	<u>\$</u>	<u>\$ 25,968</u>

As at December 31, 2018 and 2017, \$32,495 was included in accounts payable for consulting fees owed to the former CEO of the Company. This amount is currently being disputed by the Company.

7. INCOME TAXES

A reconciliation of income taxes at statutory rates with the reported taxes is as follows:

	<u>2018</u>	<u>2017</u>
Statutory tax rate	26.00%	26.00%
Loss before income tax	<u>\$ (369,387)</u>	<u>\$ (363,786)</u>
Expected income tax recovery	(96,041)	(94,584)
Increase (decrease) in income tax recovery resulting from:		
Non deductible item and deductible items	-	9,992
Other adjustments	-	-
Change in unrecognized deferred tax assets	<u>96,041</u>	<u>84,592</u>
	<u>\$ -</u>	<u>\$ -</u>
	2018	2017
Deferred income tax assets		
Non-capital losses	\$ 2,304,441	\$ 2,208,400
Oil and natural gas properties	1,076,410	1,076,410
Property, plant and equipment	6,909	6,909
Share issuance costs	-	-
Total unrecognized deferred income tax assets	<u>\$3,387,760</u>	<u>\$3,291,719</u>

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7. INCOME TAXES (Continued)

The Company has non-capital tax loss carry forwards of approximately \$8,493,847 (2017 - \$8,493,847) that are available to reduce taxable income in future periods. The non-capital losses expire as follow:

<u>Expiry Date</u>	<u>Total</u>
2026	717,597
2027	838,601
2028	644,466
2029	319,504
2030	521,052
2031	1,274,349
2032	495,437
2033	213,850
2034	876,662
2035	898,219
2036	1,368,756
2037	325,354
2038	369,387
Total	8,863,234

The Company has approximately \$4,140,000 (2017: \$4,140,000) of exploration costs which are available for deduction against future income for tax purposes.

Due to the uncertainty surrounding the realization of deferred income tax assets, the Company has not recognized a deferred tax asset.

8. SEGMENTED INFORMATION

The Company operates within a single operating segment, which is the exploration and development of its oil and gas properties located in Tunisia, North Africa.

9. CONTINGENT LIABILITIES

- (a) The Company may be liable for a claim in the amount of \$75,113 for certain legal expenses with respect to a proposed amalgamation with Canada Gas Corp. The amalgamation was not completed and management is disputing the amount and is in the opinion that the amount owed is \$2,315. The Company has accrued \$nil in relation to this claim.
- (b) PricewaterhouseCoopers LLP ("PwC") has filed a Writ of Summons against the company for \$52,125 in uncollected fees plus 6% interest on the outstanding fees, and any cost associated with collecting these fees. On November 18, 2011, judgment was awarded to PwC in the full amount of \$52,125 plus 6% interest on the judgment awarded and costs. On November 25, 2011, the Company filed an Appeal with the Court of Appeal.

The Company has recorded the debt and interest as accounts payable and included the interest in accrued liabilities.

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- (c) Synterra Technologies Ltd. Filed a claim against the Company in the amount of \$18,780 for the consulting services provided. Management has decided to settle the claim by negotiating it with the plaintiff in the amount of \$10,000.

The Company has recorded the debt in accounts payable.

- (d) Ah Twelve Holdings Ltd filed a Notice of Civil Claim against the Company in the amount of \$38,886 for the outstanding rent payments on December 13, 2013. Management has determined that it is probable that an outflow of cash for the above stated amount will be required to settle the obligation. During the year ended December 31, 2017, the Company made payments totaling \$5,000 and additional payments of \$9,000 in 2016 and \$6,000 in 2015.

The Company has recorded the balance of the debt in accounts payable.

10. MANAGEMENT OF CAPITAL

The Company manages its capital structure and makes adjustments to it, based on the funds available to the Company in order to support the acquisition, exploration and development of mineral properties and to maintain the Company in good standing with the various regulatory authorities.

The properties in which the Company currently has an interest in are in the exploration stage, as such, the Company does not recognize revenue from its exploration properties. The Company's historical sources of capital have consisted of the sale of equity securities and interest income. In order for the Company to carry out planned exploration and development and pay for administrative costs, the Company will spend its working capital and raise additional amounts externally as needed.

The Company has policies and procedures in place for employee and officer expenditure authorization limits and capital expenditure authorization. Management reviews its capital management approach on an ongoing basis and believes this approach, given the size of the Company, is reasonable.

11. FINANCIAL INSTRUMENTS

The Company's financial instruments at December 31, 2018 consist of cash, accounts payable and accrued liabilities, and loans payable. Cash is carried at fair value using a level 1 fair value measurement. The carrying value of accounts payable and accrued liabilities, and loans payable approximate their fair value because of their nature and respective maturity dates or durations.

The risk exposure is summarized as follows:

Credit Risk

The Company is not exposed to any significant credit risk on its financial assets. Cash consists of cash on hand have been invested with reputable financial institutions and funds in trust have been held with trustworthy legal firms, from which management believes the risk of loss to be remote.

As at December 31, 2018, the Company had no financial assets that were either past due or impaired.

Liquidity Risk

The Company's approach to managing liquidity is to ensure that it will have sufficient liquidity to settle obligations and liabilities when due. As at December 31, 2018, the Company had a cash of

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\$151 to settle current liabilities of \$1,490,196 which mainly consist of accounts payable and accrued liabilities and loans payable that are considered short term.

Market risk

i) Interest Rate Risk:

The Company's accounts payable and accrued liabilities and loans payable are non-interest bearing.

ii) Foreign Currency Risk:

The Company's functional and reporting currency is the Canadian dollar and is not exposed to foreign currency risk.

iii) Price Risk:

The Company's financial assets and liabilities are not exposed to price risk with respect to commodity prices.

During the year ended December 31, 2018, there were no changes to the Company's risk exposure or to the Company's policies for risk management.

12. SUPPLEMENTAL CASH FLOW INFORMATION

There were no non-cash transactions during the year ended December 31, 2018 and 2017.