

Prospera Energy Inc.
(formerly Georox Resources Inc.)

Financial Statements

December 31, 2018 and 2017

(in Canadian dollars)

Independent Auditor's Report

To the Shareholders of Prospera Energy Inc. (formerly Georox Resources Inc.):

Opinion

We have audited the financial statements of Prospera Energy Inc. (formerly Georox Resources Inc.) (the "Corporation"), which comprise the statements of financial position as at December 31, 2018 and December 31, 2017, and the statements of loss and comprehensive loss, changes in shareholders' deficiency and cash flows for the years then ended, and notes to the financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying financial statements present fairly, in all material respects, the financial position of the Corporation as at December 31, 2018 and December 31, 2017, and its financial performance and its cash flows for the years then ended in accordance with International Financial Reporting Standards.

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 Corporation 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 is sufficient and appropriate to provide a basis for our opinion.

Material Uncertainty Related to Going Concern

We draw attention to Note 2 in the financial statements, which indicates that the Corporation has a working capital deficiency of \$7,648,144, and an accumulated deficit of \$22,414,435. There is a material risk that the Company will be unable to meet its financing obligations including payments of outstanding interest and principal balances on its credit facilities and, as at December 31, 2018, the Company was in breach of all but one of its covenants. As stated in Note 2, these events or conditions, along with other matters as set forth in Note 2, indicate that a material uncertainty exists that may cast significant doubt on the Corporation'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 Management's Discussion and Analysis.

Our opinion on the financial statements does not cover the other information and we do not and will not express any form of assurance conclusion thereon.

In connection with our audits of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audits or otherwise appears to be materially misstated. We obtained Management's Discussion and Analysis prior to the date of this auditor's 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. 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 financial statements in accordance with International Financial Reporting Standards, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, management is responsible for assessing the Corporation'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 Corporation or to cease operations, or has no realistic alternative but to do so.

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

Auditor's Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the 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 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 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 Corporation'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 Corporation'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 Corporation to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

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

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 Elena Ruttan.

Calgary, Alberta

April 30, 2019



Chartered Professional Accountants

PROSPERA ENERGY INC.

(formerly Georox Resources Inc.)

Statements of Financial Position

As at December 31

	Note	2018	2017
ASSETS			
Current assets			
Cash		\$ 177,624	\$ 125,618
Trade and other receivables	6	1,086,382	197,813
Prepaid and other current assets		333,424	3,414
Inventory		89,843	29,884
Total current assets		1,687,273	356,729
Non-current assets			
Property and equipment	8	9,665,253	6,699,220
Total assets		\$ 11,352,526	\$ 7,055,949
SHAREHOLDERS' DEFICIENCY AND LIABILITIES			
Current liabilities			
Trade and other payables	10	\$ 4,420,292	\$ 2,276,006
Credit facilities	11	4,915,125	5,269,776
Derivative liability	11	—	15,391
Total current liabilities		9,335,417	7,561,173
Non-current liabilities			
Provision for decommissioning	12	9,398,844	1,327,194
Total liabilities		18,734,261	8,888,367
Shareholders' deficiency			
Share capital	14(a)	11,539,391	10,243,391
Share purchase warrants	14(b)	96,163	311,126
Contributed surplus		3,411,159	3,120,034
Accumulated other comprehensive income		(14,013)	(14,013)
Deficit		(22,414,435)	(15,492,956)
Total shareholders' deficiency		(7,381,735)	(1,832,418)
Total liabilities and shareholders' deficiency		\$ 11,352,526	\$ 7,055,949

Going Concern (Note 2)

Commitment (Note 22)

Subsequent Events (Note 23)

Approved and authorised by the Board of Directors

Signed "Burkhard Franz", Director

Signed "Lorraine McVean", Director

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

PROSPERA ENERGY INC.

(formerly Georox Resources Inc.)

Statements of Loss and Comprehensive Loss

For the years ended December 31

	Note	2018	2017
Revenues			
Petroleum and natural gas sales	16	\$ 3,094,542	\$ 1,780,057
Royalties		(244,873)	(145,298)
		2,849,669	1,634,759
Expenses			
Operating		2,117,894	1,058,359
General and administrative	17(a)	460,826	654,690
Depletion and depreciation	8	1,903,089	550,238
Impairment	9	5,904,895	471,575
Share-based payments	14(c)	76,162	36,344
		10,462,866	2,771,206
Operating loss		(7,613,197)	(1,136,447)
Finance recovery (expense)	18	121,308	(824,576)
Loss on sale of investment		–	(3,898)
Gain on disposition of property and equipment	8	227,157	–
Gain on de-recognition of debt	19	343,253	–
Loss for the year		(6,921,479)	(1,964,921)
Other comprehensive loss			
Net change in fair value of available for sale financial assets		–	(3,000)
Loss and comprehensive loss		\$ (6,921,479)	\$ (1,967,921)
Loss per share			
	15	\$ (0.18)	\$ (0.08)

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

PROSPERA ENERGY INC.

(formerly Georox Resources Inc.)

Statements of Changes in Shareholders' Deficiency

For the years ended December 31

	Note	2018	2017
Share capital	14(a)		
Balance, January 1		\$ 10,243,391	\$ 10,106,434
Private placement of common shares		991,000	–
Private placement of units		–	116,957
Shares issued for services		–	20,000
Private placement proceeds received in advance	23(a)	366,000	–
Share issue costs		(61,000)	–
Balance, December 31		11,539,391	10,243,391
Share purchase warrants	14(b)		
Balance, January 1		311,126	214,963
Private placement of units		–	96,163
Expiry of share purchase warrants		(214,963)	–
Balance, December 31		96,163	311,126
Contributed surplus			
Balance, January 1		3,120,034	3,083,690
Share-based payments		76,162	36,344
Expiry of share purchase warrants		214,963	–
Balance, December 31		3,411,159	3,120,034
Accumulated other comprehensive income			
Balance, January 1		(14,013)	(11,013)
Net change in fair value of available for sale financial assets		–	(3,000)
Balance, December 31		(14,013)	(14,013)
Deficit			
Balance, January 1		(15,492,956)	(13,528,035)
Loss for the year		(6,921,479)	(1,964,921)
Balance, December 31		(22,414,435)	(15,492,956)
Total shareholders' deficiency		\$ (7,381,735)	\$ (1,832,418)

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

PROSPERA ENERGY INC.

(formerly Georox Resources Inc.)

Statements of Changes in Cash Flows

For the years ended December 31

	Note	2018	2017
Cash flows (used in) provided by operating activities			
Loss for the year		\$ (6,921,479)	\$ (1,964,921)
Add back (deduct) items not affecting cash:			
Depletion, depreciation and impairment	8	5,249,137	1,021,813
Goodwill impairment	7	2,558,847	–
Share-based payments	14(c)	76,162	36,344
Finance expense (recovery)	18	(121,308)	824,576
Deferred fee on credit facilities	11	–	80,467
Loss on sale of investments		–	3,898
Gain on disposition of petroleum and natural gas assets	8	(227,157)	–
Shares issued for services	14(a)	–	20,000
Change in non-cash working capital:			
Trade and other receivables		(888,569)	80,372
Prepaid and other current assets		(156,723)	–
Inventory		(59,959)	4,447
Trade and other payables		1,944,158	103,331
Net cash flows provided by operating activities		1,453,109	210,327
Cash flows provided by (used in) financing activities			
Share issuance proceeds, net of issue costs	14(a)	930,000	213,120
Share issuance proceeds received in advance	23(a)	366,000	–
Advances of credit facilities	11	300,000	417,180
Repayment of credit facilities	11	(310,000)	(30,000)
Interest expense	17	(528,654)	(687,683)
Change in non-cash working capital		45,766	219,869
Net cash flows provided by financing activities		803,112	132,486
Cash flows provided (used in) by investing activities			
Business combinations	7	(2,011,365)	–
Expenditures on petroleum and natural gas assets	8	(844,614)	(450,175)
Proceeds from sale of investment		–	17,087
Change in non-cash working capital		651,764	211,500
Net cash flows used in investing activities		(2,204,215)	(221,588)
Change in cash		52,006	121,225
Cash, beginning of year		125,618	4,393
Cash, end of year		\$ 177,624	\$ 125,618
Cash interest paid		\$ 482,888	\$ 467,814
Cash taxes paid		\$ –	\$ –

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

PROSPERA ENERGY INC.

(formerly Georox Resources Inc.)

Notes to the Financial Statements

For the years ended December 31, 2018 and 2017

1. Nature of Operations

Prospera Energy Inc. (the "Corporation" or "Prospera") was incorporated under the Canada Business Corporations Act on April 14, 2003 as Georox Resources Inc. The Corporation changed its name to Prospera on June 28, 2018. The Corporation is listed on the TSX-Venture Exchange and its primary business is the acquisition of, exploration for, and the development of petroleum and natural gas properties in Canada.

The address of the Corporation's registered office is Suite 700, 1300 – 8th Street SW, Calgary, Alberta, Canada, T2R 1B2.

2. Going Concern

These financial statements have been prepared on a going concern basis, which implies the Corporation will continue to realize its assets and discharge its liabilities in the normal course of business. The Corporation has historically met its day-to-day working capital requirements and funded its capital and operating expenditures through funding received from the proceeds of share issuances and debt.

As of December 31, 2018, the Corporation has a working capital deficiency of \$7,648,144 (December 31, 2017 – \$7,204,444), and an accumulated deficit of \$22,414,435 (December 31, 2017 – \$15,492,956). There is a material risk that the Corporation will be unable to meet its financing obligations including payments of outstanding interest and principal balances on its credit facilities and as at December 31, 2018, the Corporation was in breach of all but one of its covenants (Note 11). Management continually monitors the Corporation's financing requirements. In June 2018 and December 2018, the Corporation acquired an aggregate 35% working interest in producing properties (Note 7) to fund its ongoing operations and assist in the repayment of debt. Management is engaged in discussions with existing shareholders and creditors on proposed transactions and agreements that would reduce anticipated cash outflows and provide the additional financing required to fund capital and operating expenditures, and to meet obligations as they fall due in the 12 months following December 31, 2018.

Management has applied significant judgment in preparing forecasts supporting the going concern assumption. Specifically, management has made assumptions regarding projected oil sales volumes and pricing, scheduling of payments arising from various obligations as at December 31, 2018, the availability of additional financing, and the timing and extent of capital and operating expenditures. As such, there is a material uncertainty related to these events and conditions that may cast significant doubt on the Corporation's ability to continue as a going concern.

The Corporation entered into a Quitclaim (the "Quitclaim") with its lender (Note 11) which provided for the transfer of title in the petroleum and natural gas assets and interests owned by the Corporation as satisfaction for all indebtedness and obligations to the lender. In conjunction with the Quitclaim, the Corporation also entered into a Forbearance Agreement that stated that the lender would refrain from enforcing the Quitclaim or any of the following rights until July 31, 2018:

- Terminate the Amended Credit Facilities;
- Cease to make available or extend any such Amended Credit Facilities;
- Accelerate payment of the Amended Credit Facilities; or,
- Appoint a receiver to manage the Corporation's assets.

Subsequent to December 31, 2018, the Corporation and its lender signed an amending agreement with respect to the credit facilities (Note 23(c)).

The financial statements have been prepared on a basis which asserts that the Corporation will continue to have the ability to realize its assets and discharge its liabilities and commitments in a planned manner with consideration to expected possible outcomes. Conversely, if the assumption made by management is not appropriate and the Corporation is unable to meet its obligations as they fall due, the preparation of these financial statements on a going concern basis may not be appropriate and adjustments to the carrying amounts of the Corporation's assets, liabilities, revenues, expenses, and balance sheet adjustments may be necessary. Such adjustments could be material.

3. Basis of Presentation

(a) Statement of compliance

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

The financial statements were approved and authorized for issuance by the Corporation's Board of Directors on April 30, 2019.

(b) Basis of measurement

The financial statements have been prepared in accordance with IFRS on a historical cost basis except as otherwise noted.

PROSPERA ENERGY INC.

(formerly Georox Resources Inc.)

Notes to the Financial Statements

For the years ended December 31, 2018 and 2017

(c) Presentation and functional currency

These financial statements are presented in Canadian dollars (unless stated otherwise), which is also the Corporation's functional currency.

(d) Use of judgments and estimates

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

The accounting policies subject to such judgments and the key sources of estimation uncertainty that the Corporation believes could have the most significant impact on the reported results and financial position are as follows:

Critical accounting judgments

- Cash-generating units

The Corporation's assets are aggregated into cash-generating units ("CGUs") based on an assessment of the unit's ability to generate independent cash in-flows. The determination of the Corporation's CGUs was based on management's judgment in regards to shared infrastructure, geographical proximity, petroleum type and similar exposure to market risk and materiality. The allocation of assets into CGU's requires significant judgment and interpretations with respect to the way in which management monitors operations. The Corporation has six petroleum and natural gas CGUs: Pouce Coupe and Red Earth in the province of Alberta and Cuthbert, Hearts Hill, Luseland and Silverdale in the province of Saskatchewan.

- Business combinations

Management uses judgment to determine whether a transaction constitutes a business combination or asset acquisition is based on the criteria in IFRS 3 Business Combinations.

- Impairment

Judgments are required to assess when impairment indicators are evident and impairment testing is required.

- Current and deferred taxes

Tax interpretations, regulations and legislation in the various jurisdictions in which the Corporation operates are subject to change. As such, current and deferred taxes are subject to measurement uncertainty. Management uses judgment to assess deferred tax assets at the end of the reporting period to determine the likelihood that they will be realized from future taxable earnings.

- Contingencies

By their nature, contingencies will only be resolved when one or more future events occur or fail to occur. The assessment of contingencies inherently involves the exercise of significant judgment and estimates of the outcome of future events. Although the Corporation believes it has title to its oil and natural gas properties, it cannot control or completely protect itself against the risk of title disputes or challenges.

Key sources of estimation uncertainty

- Valuation of accounts receivable

Expected credit losses are reviewed by the Corporation on a monthly basis. The Corporation calculates the expected credit losses on accounts receivable using a provision matrix which is based on the Corporation's historical credit loss experience for accounts receivable to estimate the lifetime expected credit losses. Management makes these assessments after taking into consideration the customer's payment history, their credit worthiness and the current economic environment in which the customer operates to assess impairment. The Corporation's historical bad debt expenses have not been significant and are usually limited to specific customer circumstances. However, given the cyclical nature of the oil and natural gas industry along with the current economic operating environment, a customer's ability to fulfil its payment obligations can change suddenly and without notice.

- Reserves

The estimate of petroleum and natural gas reserves is integral to the calculation of the amount of depletion charged to the statement of loss and comprehensive loss and is also a key determinant in assessing whether the carrying value of any of the Corporation's petroleum and natural gas assets has been impaired. Changes in reported reserves can impact asset carrying values and the decommissioning provision due to changes in expected future cash flows.

PROSPERA ENERGY INC.

(formerly Georox Resources Inc.)

Notes to the Financial Statements

For the years ended December 31, 2018 and 2017

The Corporation's reserves are evaluated and reported on by independent reserve engineers at least annually in accordance with Canadian Securities Administrators' National Instrument 51-101. 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.

- **Business combinations**

In a business combination, management makes estimates of the fair value of assets acquired and liabilities assumed which includes assessing the value of petroleum and natural gas assets based upon the estimation of recoverable quantities of proved and probable reserves acquired, forecast benchmark commodity prices and discount rates. These estimates impact the potential for recognizing goodwill or a bargain purchase gain, future depletion and impairment.

- **Carrying value of non-financial assets**

If any indication exists that an asset or CGU may be impaired, the Corporation estimates the recoverable amount. The recoverable amounts of individual assets and cash-generating units have been determined based on the higher of value-in-use and fair value less costs to dispose.

These calculations require the use of estimates and assumptions, such as estimates of proved plus probable reserves, future production rates, oil and natural gas prices, future costs and other relevant assumptions, all of which are subject to change. A material adjustment to the carrying value of the Corporation's non-financial assets may be required as a result of changes to these estimates and assumptions.

- **Depletion and depreciation**

Amounts recorded for depletion and depreciation and amounts used for impairment calculations are based on estimates of total proved and probable petroleum and natural gas reserves and future development capital. By their nature, the estimates of reserves, including the estimates of future prices, costs and future cash flows, are subject to measurement uncertainty. Accordingly, the impact to the financial statements in future periods could be material.

- **Provision for decommissioning**

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

- **Deferred taxes**

Deferred taxes are based on estimates as to the timing of the reversal of temporary and taxable differences, substantively enacted tax rates and the likelihood of assets being realized.

- **Stock options and share purchase warrants**

Stock options and share purchase warrants are valued using the Black-Scholes pricing model. Estimates and assumptions for inputs to the model, including the expected volatility of the Corporation's shares and the expected life of the options and share purchase warrants, are subject to significant uncertainties and judgment. Expected volatility is estimated using a historical trading period for the Corporation's shares that matches the life of the related stock options or share purchase warrants.

4. Significant Accounting Policies

(a) Joint arrangements

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

(b) Cash

Cash consist of cash deposits held in Canadian banks.

(c) Inventory

Inventory is stated at the lower of cost and net realizable value. The cost of producing oil and natural gas is accounted for on a weighted average basis. These costs include all costs incurred in the normal course of business in bringing each product to its present location and condition. The cost of oil and natural gas is the producing cost, including royalties and the appropriate proportion of depletion and depreciation and overheads. Net realizable value of oil and natural gas is based on

PROSPERA ENERGY INC.

(formerly Georox Resources Inc.)

Notes to the Financial Statements

For the years ended December 31, 2018 and 2017

estimated selling price in the ordinary course of business less any expected selling costs.

(d) Property and equipment

Petroleum and natural gas assets

All costs directly associated with the development of petroleum and natural gas reserves are capitalized on an area-by-area basis. Development costs include expenditures for areas where technical feasibility and commercial viability has been determined. These costs include proved property acquisitions, development drilling and completion, gathering and infrastructure, decommissioning costs and transfers of exploration and evaluation assets.

Costs incurred subsequent to the determination of technical feasibility and commercial viability, costs of replacing parts of petroleum and natural gas assets and workovers of petroleum and natural gas assets are recognized as assets only if they increase the economic benefits of the assets to which they relate. All other expenditures are recognized in the statement of loss and comprehensive loss when incurred. The carrying amounts of previous inspections or any replaced or sold components are derecognized. The costs of day-to-day servicing of petroleum and natural gas assets are recognized in the statement of loss and comprehensive loss as incurred.

Petroleum and natural gas assets are depleted using the unit-of-production method by reference to the ratio of production in the period to the related proved and probable reserves, taking into account estimated future development costs. Production and reserves of natural gas are converted to equivalent barrels of crude oil on the basis of six thousand cubic feet of gas to one barrel of oil. Changes to estimates used in prior periods, such as proved and probable reserves, that affect the unit-of-production calculations do not give rise to prior period adjustments and are dealt with on a prospective basis.

Processing facilities and well equipment are depleted using the unit-of-production method along with the related reserves when the assets are designed to have a life similar to the reserves of the related wells with little to no residual value.

Administrative assets, consisting of office furniture and equipment are depreciated on a declining balance basis over their estimated useful lives at rates ranging from 20% to 30% per annum.

For divestitures of petroleum and natural gas assets, a gain or loss is recognized in the statement of loss and comprehensive loss. Exchanges of properties are measured at fair value, unless the transaction lacks commercial substance or fair value cannot be reliably measured in which case the cost of the acquired asset is measured at the carrying value of asset given up. Where the exchange is measured at fair value, a gain or loss is recognized in the statement of loss and comprehensive loss.

Impairment

At the end of each reporting period, the Corporation reviews petroleum and natural gas assets for circumstances that indicate the assets may be impaired. Assets are grouped together into CGUs for the purpose of impairment testing. If any such indication of impairment exists, the Corporation makes an estimate of its recoverable amount. A CGU's recoverable amount is the higher of its fair value less costs to dispose and its value in use.

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 of the time value of money and the risks specific to the asset. Value in use is generally computed by reference to the present value of future cash flows expected to be derived from the production of proved and probable reserves.

Fair value less cost to dispose is determined as the amount that would be obtained from the sale of a CGU in an arm's length transaction between knowledgeable and willing parties. The fair value less cost to dispose of oil and gas assets is generally determined as the net present value of the estimated future cash flows expected to arise from the continued use of the CGU, including any expansion prospects, and its eventual disposal, using assumptions that an independent market participant may take into account. These cash flows are discounted by an appropriate discount rate which would be applied by such a market participant to arrive at a net present value of the CGU.

When the recoverable amount is less than the carrying amount, the asset or CGU is impaired. For impairment losses identified on a CGU, the loss is first allocated to reduce the carrying amount of goodwill, should it exist, then allocated on a pro rata basis to the assets within the CGU. Impairment losses are recognized in the statement of loss and comprehensive loss.

At the end of each subsequent reporting period these impairments are assessed for indicators of reversal. Where an impairment loss subsequently reverses, the carrying amount of the asset or CGU is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss have been recognized for the asset or CGU in prior periods. A reversal of an impairment loss is recognized in the statement of loss and comprehensive loss.

PROSPERA ENERGY INC.

(formerly Georox Resources Inc.)

Notes to the Financial Statements

For the years ended December 31, 2018 and 2017

(e) Goodwill

The Corporation records goodwill relating to a business combination when the purchase price exceeds the fair value of the net identifiable assets and liabilities of the acquired business. Goodwill is reported at cost less any impairment and is not amortized. Goodwill is evaluated when facts and circumstances indicate that it is impaired, or at least on an annual basis.

To test for impairment, goodwill is allocated to the related CGU expected to benefit from the acquisition. Goodwill is tested by comparing the carrying amount of the CGU to the recoverable amount. Fair value less costs to dispose is derived by estimating the discounted after-tax future net cash flows as described in the property and equipment impairment test, plus the fair market value of undeveloped land, seismic and inventory. Value in use is assessed using the present value of the expected future cash flows. Any excess of the carrying amount over the recoverable amount is recorded as impairment. Goodwill impairments are not reversed.

(f) Provision for decommissioning

The Corporation recognizes a provision for decommissioning in the period in which a well is drilled or acquired and a reasonable estimate of the future costs associated with removal, site restoration and asset retirement can be made. The estimated decommissioning liability is recorded with a corresponding increase in the carrying amount of the related asset.

The provision for decommissioning is measured at the present value of management's best estimate of the expenditures required to settle the present obligation at the statement of financial position date. Subsequent to the initial measurement, the provision is adjusted at the end of each period 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 accretion expense whereas increases/decreases due to changes in the estimated future cash flows are capitalized. Actual costs incurred upon settlement of decommissioning liabilities are charged against the provision to the extent a liability was established.

(g) Taxes

Taxes on earnings for the periods presented are comprised of current and deferred tax. Taxes are recognized in the statement of loss and comprehensive loss except to the extent that it relates to items recognized directly in equity, in which case it is recognized in equity.

Current tax expense is the expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted at period end, adjusted for amendments to tax payable with regards to previous years.

Deferred tax is recorded, using the statement of financial position method, on temporary differences between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes. However, deferred tax is not recorded on taxable temporary differences arising on the initial recognition of goodwill or on the initial recognition of assets and liabilities in a transaction other than a business combination that affect neither accounting nor taxable profit or loss. Deferred tax is also not recorded on differences relating to investments in subsidiaries and jointly controlled entities to the extent that they will probably not reverse in the foreseeable future. The amount of deferred tax provided is based on the expected manner of realization or settlement of the carrying amount of assets and liabilities, using tax rates enacted or substantively enacted at the statement of financial position date.

A deferred tax asset is recognized only to the extent that it is probable that future taxable profits will be available against which the asset can be utilized. The carrying amount of deferred tax assets is reviewed at each reporting date and reduced to the extent that it is no longer probable that sufficient future taxable profit will be available to allow all or part of the deferred tax asset to be utilized. Unrecognized deferred tax assets are reassessed at each reporting date and are recognized to the extent that it has become probable that future taxable profit will allow the deferred tax asset to be recovered.

Deferred tax assets and liabilities are offset when there is a legally enforceable right to offset current tax assets against current tax liabilities and when they relate to taxes levied by the same taxation authority and the Corporation intends to settle its current tax assets and liabilities on a net basis.

(h) Financial instruments

As of January 1, 2018, the Corporation classifies its financial instruments in the following measurement categories:

- Subsequently measured at fair value (either through profit or loss ("FVTPL") or other comprehensive income ("FVOCI"); or
- Subsequently measured at amortized cost.

The classification depends on the Corporation's business model for managing the financial instruments and the contractual terms of the cash flows. There was no change in the categorization of the Corporation's financial instruments upon the adoption of IFRS 9 Financial Instruments.

PROSPERA ENERGY INC.

(formerly Georox Resources Inc.)

Notes to the Financial Statements

For the years ended December 31, 2018 and 2017

Non-derivative financial instruments

Non-derivative financial instruments comprise cash, trade and other receivables, trade and other payables and credit facilities. Non-derivative financial instruments are recognized initially at fair value plus, for instruments not at FVTPL, any directly attributable transaction costs. Transaction costs of financial assets measured at FVTPL are expensed in the statement of loss and comprehensive loss. Subsequent to initial recognition, non-derivative financial instruments are measured as described below:

- **Financial assets at FVTPL**

Financial assets at FVTPL are measured at fair value, and changes therein are recognized in the statement of loss and comprehensive loss. A financial asset is classified at FVTPL unless it is measured at amortized cost or classified as FVOCI. However an entity may make an irrevocable election at initial recognition for particular investments in equity instruments that would otherwise be measured at FVTPL to present subsequent changes in FVOCI with no reclassification of realized gains or losses in the statement of loss and comprehensive loss upon derecognition of the equity instruments.

- **Financial liabilities at FVTPL**

The Corporation classifies the contingent liability as FVTPL. A financial liability is initially classified as measured at amortized cost or FVTPL. A financial liability is classified as measured at FVTPL if it is held-for-trading, a derivative, or designated as FVTPL on initial recognition. The classification of a financial liability is irrevocable.

Financial liabilities at FVTPL (other than financial liabilities designated at FVTPL) are measured at fair value with changes in fair value, along with any interest expense, recognized in the statement of loss and comprehensive loss. Other financial liabilities are initially measured at fair value less directly attributable transaction costs and are subsequently measured at amortized cost using the effective interest method. Interest expense and foreign exchange gains and losses are recognized in the statement of loss and comprehensive loss. Any gain or loss on derecognition is also recognized in the statement of loss and comprehensive loss.

A financial liability is derecognized when the obligation is discharged, cancelled or expired. When an existing financial liability is replaced by another from the same counterparty with substantially different terms, or the terms of an existing liability are substantially modified, it is treated as a derecognition of the original liability and the recognition of a new liability. When the terms of an existing financial liability are altered, but the changes are considered non-substantial, it is accounted for as a modification to the existing financial liability. Where a liability is substantially modified it is considered to be extinguished and a gain or loss is recognized in the statement of loss and comprehensive loss based on the difference between the carrying amount of the liability derecognized and the fair value of the revised liability. Where a liability is modified in a non-substantial way, the amortized cost of the liability is remeasured based on the new cash flows and a gain or loss is recorded in the statement of loss and comprehensive loss.

- **Financial assets at FVOCI**

Financial assets at FVOCI are measured at fair value, and changes therein are recognized in other comprehensive income. A financial asset is classified as FVOCI if it is held within a business model whose objective is achieved by both collecting contractual cash flows and selling financial assets and 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.

- **Financial instruments at amortized cost**

The Corporation classifies cash, trade and other receivables, trade and other payables and credit facilities as financial instruments at amortized cost. These financial instruments are measured at amortized cost using the effective interest method, less any impairment losses. Any gain or loss arising on de-recognition is recognized directly in the statement of loss and comprehensive loss. Impairment losses are presented as separate line item in the statement of loss and comprehensive loss.

Derivative financial instruments

The Corporation has not entered into any financial derivative contracts.

(i) Impairment of financial instruments

As of January 1, 2018, the Corporation assesses, on a forward looking basis, the expected credit losses associated with financial instruments carried at amortized cost. The impairment methodology applied depends on whether there has been a

PROSPERA ENERGY INC.

(formerly Georox Resources Inc.)

Notes to the Financial Statements

For the years ended December 31, 2018 and 2017

significant increase in credit risk. For trade and other receivables, the Corporation applied the simplified approach permitted by IFRS 9 Financial Instruments ("IFRS 9").

The Corporation adopted IFRS 9 on January 1, 2018 using the modified retrospective approach, but has elected not to restate comparative information. As a result, the comparative information provided continues to be accounted for in accordance with the Corporation's previous accounting policy:

Trade and other receivables are assessed for impairment individually, if significant, and collectively if the assets share similar credit risk characteristics. If an impairment is required, the carrying amount of trade and other receivables is reduced through the use of an allowance account. When a receivable is considered uncollectible, it is written off against the allowance account. Subsequent recoveries of amounts previously written off are credited against the allowance account. Net adjustments to the allowance account are recorded in the statement loss and comprehensive loss.

(j) Share capital

Common and preferred shares are classified as equity. Incremental costs directly attributable to the issuance of common shares are recognized as a deduction from equity.

(k) Share purchase warrants

The Corporation may issue share purchase warrants as part of a unit issuance comprised of a share and warrant or as a share issue cost. Share purchase warrants are classified as equity instruments. Consideration received on the sale of a share and share purchase warrant classified as equity is allocated, within equity, to the respective equity accounts on a reasonable basis. The fair value of share purchase warrants is measured at the date of issuance using the Black-Scholes pricing model taking into account the terms and conditions upon which the share purchase warrants were issued. Share purchase warrants are classified as equity instruments are not subsequently re-measured for changes in fair value.

(l) Share-based payments

The Corporation follows the fair value method of accounting for stock options. The fair value of each stock option is calculated on the grant date using the Black-Scholes pricing model and is charged to income over the vesting period of the stock option, with a corresponding increase recorded in contributed surplus. Forfeitures are accounted for at grant date and adjusted based on actual vesting. Upon exercise of stock options, the consideration received plus the amount previously recorded in contributed surplus is recorded as an increase to share capital.

(m) Deferred share units

The Corporation has a deferred share unit ("DSU") plan, whereby DSUs are issued to the Corporation's Board of Directors. Each DSU is a notional unit equal in value to one common share, which entitles the holder to a cash payment upon redemption. DSUs can only be converted to cash upon the holder ceasing to be a director of the Corporation. The expense associated with the DSU plan is determined based on the market price of the Corporation's common shares on the grant date. The expense is recognized in the statement of loss and comprehensive loss in the quarter in which the units are granted with a corresponding liability recorded in trade and other payables. At period end dates, the DSU liability is adjusted based on the market price of the Corporation's common shares on the period end date.

(n) Per share amounts

The Corporation presents basic and diluted per share data for its common shares. Basic per share amounts are calculated by dividing the profit (loss) attributable to common shareholders of the Corporation by the weighted average number of common shares outstanding during the period. Diluted per share amounts are determined by adjusting earnings attributable to common shareholders and the weighted average number of common shares outstanding, adjusted, for the effects of all dilutive potential common shares.

(o) Revenue recognition

The Corporation recognizes revenue from the sale of petroleum and natural gas when control of the product transfers to the buyer and collection is reasonably assured. This is generally at the point in time when the customer obtains legal title to the product which is when it is physically transferred to the pipeline or other transportation method agreed upon and the Corporation has the present right to payment. Sales of oil and natural gas are based on variable pricing based on benchmark commodity prices and other variable factors including quality, location and other factors.

(p) Changes in accounting standards

Adoption of IFRS 9 Financial Instruments

On January 1, 2018, the Corporation adopted IFRS 9 using the modified retrospective approach which replaces International

PROSPERA ENERGY INC.

(formerly Georox Resources Inc.)

Notes to the Financial Statements

For the years ended December 31, 2018 and 2017

Accounting Standard ("IAS") 39 Financial Instruments: Recognition and Measurement ("IAS 39") and includes new requirements for the classification and measurement of financial assets, a new credit loss impairment model and new model to be used for hedge accounting for risk management contracts. The Corporation does not currently have any risk management contracts. The adoption of IFRS 9 did not have a material impact on the Corporation's financial statements and management applied the provision matrix practical expedient as part of the adoption of the standard.

The additional disclosures required by IFRS 9 are detailed in Note 6.

IFRS 9 contains three principal classification categories for financial assets: measured at amortized cost, FVOCI, and FVTPL. The previous IAS 39 categories of held to maturity, loans and receivables and available for sale are eliminated. IFRS 9 bases the classification of financial assets on the contractual cash flow characteristics and the Corporation's business model for managing the financial asset. Additionally, embedded derivatives are not separated if the host contract is a financial asset within the scope of IFRS 9. Instead, the entire hybrid contract is assessed for classification and measurement. IFRS 9 largely retains the existing requirements in IAS 39 for the classification of financial liabilities. The differences between the two standards did not impact the Corporation at the time of transition.

The following table shows the original measurement categories under IAS 39 and the new measurement categories under IFRS 9 for each class of the Corporation's financial assets and financial liabilities as at January 1, 2018.

Financial instrument	Measurement Category ^{(1) (2)}	
	IAS 39	IFRS 9
Cash	FVTPL	Amortized cost
Trade and other receivables	Loans and receivables at amortized cost	Amortized cost
Trade and other payables	Financial liabilities at amortized cost	Amortized cost
Credit facilities	Financial liabilities at amortized cost	Amortized cost
Derivative liability	FVTPL	FVTPL

⁽¹⁾ There were no adjustments to the carrying amounts of financial instruments as a result of the classification change from IAS 39 to IFRS 9.

⁽²⁾ The Corporation has no contract assets or debt investments measured at FVOCI.

Adoption of IFRS 15 Revenue from Contracts with Customers

On January 1, 2018, the Corporation adopted IFRS 15 Revenue from Contracts with Customers ("IFRS 15") using the modified retrospective method of adoption. The adoption of IFRS 15 did not have a material impact on the Corporation's financial statements. As part of the adoption of the standard, the Corporation applied the practical expedient to not restate contracts that are completed contracts as the beginning of the earliest period presented. The Corporation also applied the practical expedient to recognize revenue in the amount to which the Corporation has the right to invoice. As such, no disclosure is included relating to the amount of transaction price allocated to remaining performance obligations and when these amounts are expected to be recognized as revenue. Contract modifications with the Corporation's customers could change the scope of the contract, the price of the contract, or both. A contract modification exists when the parties to the contract approve the modification either in writing, orally, or both based on the parties' customary business practices. Contract modifications are accounted for either as a separate contract when there is an additional product at a stand-alone selling price, or as part of the existing contract, through either a cumulative catch-up adjustment or prospectively over the remaining term of the contract depending on the nature of the modification and whether the remaining products are distinct. The additional disclosures required by IFRS 15 are detailed in Note 16.

For the comparative year, prior to the adoption of IFRS 15, the Corporation's revenue accounting policy was:

Revenue from the sale of oil and natural gas is recognized based on volumes delivered to customers at contractual delivery points and rates. The costs associated with the delivery, including operating and maintenance costs, transportation, and production-based royalty expenses, are recognized in the same period in which the related revenue is earned and recorded.

(q) New and amended standards not yet adopted

The Corporation has reviewed new and amended accounting pronouncements that have been issued but are not yet effective and determined that the following may have an impact on the Corporation:

IFRS 16 Leases

In January 2016, the IASB issued IFRS 16 Leases ("IFRS 16") which replaces the previous leases standard, IAS 17 Leases. IFRS 16 eliminates the classification of leases as either operating leases or finance leases as is required by IAS 17 and, instead, introduces a single lessee accounting model.

IFRS 16 will result in almost all leases being recognized in the statement of financial position, as the distinction between operating and finance leases is removed. Under IFRS 16, an asset (the right-to-use the leased item) and a financial liability

PROSPERA ENERGY INC.

(formerly Georox Resources Inc.)

Notes to the Financial Statements

For the years ended December 31, 2018 and 2017

are recognized. On initial adoption, the Corporation anticipates that it will elect to use the following practical expedients permitted under the standard:

- Apply a single discount rate to a portfolio of leases with similar characteristics;
- Account for leases with a remaining term of less than 12 months as at January 1, 2019 as short-term leases;
- Account for lease payments as an expense and not recognize a right-of-use asset if the underlying asset is of low dollar value; and
- The use of hindsight in determining the lease term where the contract contains terms to extend or terminate the lease.

IFRS 16 is effective for periods beginning on or after January 1, 2019. The Corporation does not expect any material adjustments to its financial statements, however, the full extent of the impact has not been finalized.

IFRS 3 Business Combinations and IFRS 11 Joint Arrangements

IFRS 3 Business Combinations ("IFRS 3") and IFRS 11 Joint Arrangements ("IFRS 11") were amended in December 2017. IFRS 3 was amended to clarify that when a party to a joint arrangement obtains control of a business that is a joint operation, it re-measures previously held interests in that business. IFRS 11 was amended to clarify that when a party that participates in, but does not have joint control of, a joint operation obtains joint control of the joint operation in which the activity of the joint operation constitutes a business as defined in IFRS 3, the previously held interests in the joint operation are not remeasured. The amendments are effective for annual reporting periods beginning on or after January 1, 2019.

IFRS 3 Business Combinations

IFRS 3 was further amended in October 2018 to clarify the definition of a business. The amendments narrow the definition of a business and permit a simplified assessment of whether an acquired set of activities and assets is a group of assets rather than a business. The amendments are effective for annual reporting periods beginning on or after January 1, 2020 with earlier adoption permitted.

There are no other standards or interpretations issued, but not yet effective, that the Corporation anticipates may have a material effect on the consolidated financial statements once adopted.

5. Determination of Fair Values

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

a) Financial instruments

The fair values of cash, trade and other receivables, trade and other payables and credit facilities approximated their carrying amount at December 31, 2018 and 2017 due to their short term to maturity.

The Corporation determines the fair value of financial instruments according to the following hierarchy based on the amount of observable inputs used to value the instrument.

Level 1– Quoted prices are available in active markets for identical assets or liabilities as of the reporting date. Active markets are those in which transactions occur in sufficient frequency and volume to provide pricing information on an ongoing basis.

Level 2 – Pricing inputs are other than quoted prices in active markets included in Level 1. Prices are either directly or indirectly observable as of the reporting date. Level 2 valuations are based on inputs, including quoted forward rates for interest rate, time value and volatility factors, which can be substantially observed or corroborated in the marketplace.

Level 3 – Valuations in this level are those with inputs for the asset or liability that are not based on observable market data. The Corporation does not hold any Level 3 financial instruments.

Assessment of the significance of a particular input to the fair value measurement requires judgment and may affect the placement within the fair value hierarchy level.

PROSPERA ENERGY INC.

(formerly Georox Resources Inc.)

Notes to the Financial Statements

For the years ended December 31, 2018 and 2017

b) Share purchase warrants and stock options

The Corporation uses the Black-Scholes pricing model to estimate the fair value of share purchase warrants and stock options issued, modified or granted. The Black-Scholes pricing model was based on the following assumptions:

	2018	2017	
	Stock Options (Note 14(c))	Stock Options (Note 14(c))	Share Purchase Warrants (Note 14(b))
Expected volatility	140%	187%	268%
Risk-free rate	2.21%	1.54%	1.28%
Expected life	2 years	2.6 years	1.8 years
Expected dividend yield	0%	0%	0%
Forfeiture rate	0%	3%	0%

6. Trade and Other Receivables

The Corporation's trade and other receivables are exposed to the risk of financial loss if the counterparty fails to meet its contractual obligations. The Corporation's trade and other receivables include amounts due from the sale of petroleum and natural gas. The Corporation's maximum exposure to credit risk at December 31, 2018 is in respect of \$1,086,382 (December 31, 2017 – \$197,813) of trade and other receivables.

The Corporation's trade and other receivables at December 31 consist of:

	2018	2017
Trade receivables	\$ 1,086,382	\$ 174,941
Goods and Services Tax receivable and other	—	22,842
	<u>\$ 1,086,382</u>	<u>\$ 197,813</u>

Four main customers that represent 92% of petroleum and natural gas sales reported for the year ended December 31, 2018 comprise \$337,135 of trade receivables at December 31, 2018 (2017 – two main customers; 85% of sales; \$120,982 of trade receivables). See Note 16.

The Corporation's trade receivables relating to petroleum and natural gas sales are aged at December 31 as follows:

	2018	2017
0 to 60 days	\$ 817,632	\$ 46,204
61 to 90 days	97,761	4,327
Over 90 days	<u>170,989</u>	<u>124,410</u>
	<u>\$ 1,086,382</u>	<u>\$ 174,941</u>

7. Business Combinations

a) 20% Working Interest

On June 11, 2018 the Corporation completed the acquisition of a 20% working interest in producing properties located in Southwest Saskatchewan for cash consideration of \$900,000 plus \$173,865 of adjustments for prepaid lease rentals paid by the vendor between the effective and closing dates.

The Corporation was the lead on the transaction, but is supported by an arm's-length private Corporation participant who was responsible for 80% of the purchase price. The Corporation assigned 80% of its rights and obligations under the Agreement to the Participant and in exchange is the operator of the acquired assets for a minimum period of 18 months from the date of closing and holds a 20% working interests in the Assets. The Corporation has an option to acquire 10% of the Assets for \$1,250,000 until December 11, 2019. A value of \$nil was assigned to this option.

PROSPERA ENERGY INC.

(formerly Georox Resources Inc.)

Notes to the Financial Statements

For the years ended December 31, 2018 and 2017

The acquisition was accounted for as a business combination using the acquisition method of accounting as follows:

Fair value of net assets acquired:	
Petroleum and natural gas assets	\$ 1,370,087
Prepaid lease rentals	173,286
Goodwill (Note 9)	1,259,139
Provision for decommissioning	(1,728,647)
	<u>\$ 1,073,865</u>
Consideration:	
Cash	<u>\$ 1,073,865</u>

The preliminary estimates of fair value were made by management at the time of the closing of the acquisition based on available information at that time. Subsequently, the Corporation received an updated estimation of the fair value of its oil and natural gas reserves reported on by independent engineers which formed the basis for the final fair value of property and equipment. As a result, the Corporation adjusted the preliminary fair value of net assets acquired upon the finalization of fair values and consideration.

The estimated value of the petroleum and natural gas assets acquired was determined using an independent reserve evaluation of total proved and probable petroleum and natural gas reserves discounted at 15%. The fair value of the provision for decommissioning was determined using estimates of the timing and future costs associated with plugging, abandonment and site remediation costs of the petroleum and natural gas assets acquired, discounted at a credit-adjusted rate (12%) in accordance with IFRS 3 Business Combinations and IFRS 13 Fair Value Measurement.

Goodwill results from the corresponding asset recorded upon the recognition of the liability associated with the decommissioning of the acquired assets of which \$876,371 has been attributed to the Cuthbert CGU and \$382,768 to the Hearts Hill CGU. See Note 9.

On June 12, 2018, the day immediately following the acquisition date, the provision for decommissioning was re-measured using a long-term risk free rate based on the expected timing of cash flows, in accordance with IAS 37 Provisions, Contingent Liabilities, and Contingent Assets. The result was a \$2,677,829 increase in the provision for decommissioning associated with the acquired petroleum and natural gas assets and the recognition of a \$2,677,829 measurement adjustment as a change in estimate of the provision for decommissioning.

During 2018, the Corporation incurred \$52,925 of costs related to the acquisition which are included in general and administrative expenses in the statement of loss and comprehensive loss.

Since June 11, 2018, the acquisition contributed \$1,428,391 of petroleum and natural gas sales and \$30,359 of operating income (petroleum and natural gas sales less royalties and operating expenses). Had the acquisition occurred on January 1, 2018, the Corporation estimates that total reported petroleum and natural gas sales would have increased by approximately \$1,543,500 to \$4,638,042 and total reported operating income would have increased by approximately \$629,100 to \$1,360,875. The pro forma information is not necessarily representative of future revenue and operations.

b) 15% Working Interest

On December 21, 2018 the Corporation completed the acquisition of an additional 15% working interest in the producing properties acquired from the arms-length private corporate participant who was responsible for 80% of the acquisition described above in Note 7(a). Consideration for the 15% working interest was \$937,500 of cash consideration.

The acquisition was accounted for as a business combination using the acquisition method of accounting as follows:

Fair value of net assets acquired:	
Petroleum and natural gas assets	\$ 1,003,500
Goodwill (Note 9)	1,299,708
Provision for decommissioning	(1,365,708)
	<u>\$ 937,500</u>
Consideration:	
Cash	<u>\$ 937,500</u>

The estimated value of the petroleum and natural gas assets acquired was determined using an independent reserve evaluation of total proved and probable petroleum and natural gas reserves discounted at 15%. The fair value of the provision

PROSPERA ENERGY INC.

(formerly Georox Resources Inc.)

Notes to the Financial Statements

For the years ended December 31, 2018 and 2017

for decommissioning was determined using estimates of the timing and future costs associated with plugging, abandonment and site remediation costs of the petroleum and natural gas assets acquired, discounted at a credit-adjusted rate (12%) in accordance with IFRS 3 Business Combinations and IFRS 13 Fair Value Measurement.

Goodwill results from the corresponding asset recorded upon the recognition of the liability associated with the decommissioning of the acquired assets of which \$828,394 has been attributed to the Cuthbert CGU and \$471,314 to the Hearts Hill CGU. See Note 9.

On December 21, 2018, the day immediately following the acquisition date, the provision for decommissioning was re-measured using a long-term risk free rate based on the expected timing of cash flows, in accordance with IAS 37 Provisions, Contingent Liabilities, and Contingent Assets. The result was a \$2,023,452 increase in the provision for decommissioning associated with the acquired petroleum and natural gas assets and the recognition of a \$2,023,452 measurement adjustment as a change in estimate of the provision for decommissioning.

During 2018, the Corporation incurred \$11,892 of costs related to the acquisition which are included in general and administrative expenses in the statement of loss and comprehensive loss.

Since December 21, 2018, the acquisition contributed \$11,547 of petroleum and natural gas sales and \$1,556 of operating income (petroleum and natural gas sales less royalties and operating expenses). Had the acquisition occurred on January 1, 2018, the Corporation estimates that total reported petroleum and natural gas sales would have increased by approximately \$665,600 to \$3,760,142 and total reported operating income would have increased by approximately \$147,700 to \$879,475. The pro forma information is not necessarily representative of future revenue and operations.

8. Property and Equipment

	Petroleum and natural gas assets	Administrative assets	TOTAL
Cost	\$	\$	\$
December 31, 2016	12,872,312	16,061	12,888,373
Additions	450,175	—	450,175
Decommissioning revisions (Note 12)	(11,963)	—	(11,963)
Balance, December 31, 2017	13,310,524	16,061	13,326,585
Business combinations (Note 7)	2,373,587	—	2,373,587
Additions	844,614	—	844,614
Disposition	(235,083)	—	(235,083)
Decommissioning revisions (Note 12)	4,999,936	—	4,999,936
Balance, December 31, 2018	21,293,578	16,061	21,309,639
Accumulated depletion, depreciation and impairment			
December 31, 2016	5,954,188	16,061	5,970,249
Depletion and depreciation	550,238	—	550,238
Impairment (Note 9)	106,878	—	106,878
Balance, December 31, 2017	6,611,304	16,061	6,627,365
Depletion and depreciation	1,903,089	—	1,903,089
Impairment (Note 9)	3,346,048	—	3,346,048
Disposition	(232,116)	—	(232,116)
Balance, December 31, 2018	11,628,325	16,061	11,644,386
Net carrying amount			
December 31, 2017	6,699,220	—	6,699,220
December 31, 2018	9,665,253	—	9,665,253

Future development costs

The December 31, 2018 depletion expense calculation included \$3.41 million (December 31, 2017 – \$3.48 million) for estimated future development costs associated with the Corporation's proved and probable reserves.

PROSPERA ENERGY INC.

(formerly Georox Resources Inc.)

Notes to the Financial Statements

For the years ended December 31, 2018 and 2017

Disposition

On August 13, 2018, the Corporation completed a sale of certain wells in the Silverdale area for proceeds of \$125,000. The proceeds for the sale were paid directly to the Corporation's primary lender.

A summary of the property disposition is provided below:

Carrying amount of net assets sold:		
Petroleum and natural gas assets	\$	2,967
Provision for decommissioning (Note 12)		(105,124)
Gain on property disposition		227,157
	\$	125,000
Consideration:		
Paid directly to the Corporation's primary lender (Note 11)	\$	125,000

9. Impairment

During the years ended December 31, 2018 and 2017, the Corporation recognized the following impairment losses:

	2018	2017
Exploration and evaluation assets	\$ —	\$ 364,697
Petroleum and natural gas assets (Note 8)	3,346,048	106,878
Goodwill (Note 7)	2,558,847	—
	<u>\$ 5,904,895</u>	<u>\$ 471,575</u>

Exploration and evaluation assets

As at December 31, 2017, the Corporation recognized \$364,697 of impairment losses for its Meekwap property as the Corporation does not intend to pursue further exploration or development of this area.

Petroleum and natural gas assets

At December 31, 2018 and 2017, the Corporation identified certain business risks related to its petroleum and natural gas assets such as a decline in forward commodity prices. As a result, the Corporation tested its petroleum and natural gas CGUs for impairment at December 31, 2018 and 2017. As at December 31, 2018, the estimate of the fair value less costs to dispose of the Corporation's Cuthbert, Hearts Hill and Luseland CGUs was less than the respective carrying values resulting in the recognition of a \$3,346,048 impairment loss, of which \$1,374,718 is attributed to the Cuthbert CGU, \$1,261,877 to the Hearts Hill CGU and \$709,453 to the Luseland CGU. During 2017, the Corporation recognized an impairment loss of \$106,878 in respect of the Silverdale CGU.

The Corporation determined the recoverable amounts for its CGUs based on fair value less costs to dispose using discounted future cash flows prepared by independent reserve engineers. In determining the recoverable amount, the Corporation considered recent transactions within the industry, long-term views of commodity prices, externally evaluated reserve volumes, and discount rates specific to the CGUs. The calculation of the recoverable amount is sensitive to the assumptions regarding production volumes, discount rates, operating cost structures and commodity prices. The fair value less costs to dispose estimates are categorized as Level 3 according to the IFRS 13 fair value hierarchy. In computing the December 31, 2018 recoverable amounts, future cash flows were adjusted for risks specific to the CGUs, reduced by a cost to dispose of 2% and discounted using a discount rate of 15% (2017 – 2% cost to dispose; 15% discount rate).

Changes in any of the key judgments, such as a downward revision in reserves, a decrease in forecast benchmark commodity prices, changes in foreign exchange rates, an increase in royalties or an increase in operating costs would decrease the recoverable amounts of assets and any impairment charges would affect net loss. A five percent increase in the assumed discount rate would result in approximately \$171,000 of additional impairment loss for the Cuthbert CGU and \$85,000 of additional impairment for the Hearts Hill CGU in 2018 and no impairment for the other CGUs (2017 – \$2,000 of additional impairment loss for Silverdale CGU and no impairment for the other CGUs).

PROSPERA ENERGY INC.

(formerly Georox Resources Inc.)

Notes to the Financial Statements

For the years ended December 31, 2018 and 2017

The following table provides the forecast benchmark commodity prices used in the December 31, 2018 and 2017 impairment calculations:

	December 31, 2018			December 31, 2017		
	Light Oil Cdn\$/bbl	Heavy Oil Cdn\$/bbl	Natural Gas Cdn\$/mcf	Light Oil Cdn\$/bbl	Heavy Oil Cdn\$/bbl	Natural Gas Cdn\$/mcf
2018	n/a	n/a	n/a	65.44	51.05	2.85
2019	63.30	48.70	1.85	74.51	59.61	3.11
2020	74.30	58.70	2.20	78.24	64.94	3.65
2021	78.50	65.20	2.55	82.45	68.43	3.8
2022	83.40	69.20	3.05	84.10	69.80	3.95
2023	85.10	70.60	3.20	—	—	—
Escalation rate thereafter	+ 2% per year	+ 2% per year	+ 2% per year	+ 2% per year	+ 2% per year	+ 2% per year

Goodwill

The recoverable amount of goodwill at December 31, 2018 was determined as the fair value less costs to dispose using a discounted cash flow method and was assessed at the CGU level. The Corporation's key assumptions used in determining the fair value less costs to dispose include discounted net present value of the estimated future cash flows expected to arise from the continued use of the CGU using a 15% discount rate. The impairment test of goodwill at December 31, 2018 concluded that the estimated recoverable amount was less than the carrying amount and the Corporation recognized \$2,558,847 of goodwill impairment of which \$1,704,765 is attributed to the Cuthbert CGU and \$854,082 to the Hearts Hill CGU.

10. Trade and Other Payables

	2018	2017
Trade payables	\$ 4,148,575	\$ 1,599,643
Accrued liabilities and other payables	213,778	661,166
Goods and Services Tax payable	57,939	15,197
	<u>\$ 4,420,292</u>	<u>\$ 2,276,006</u>

Trade payables are non-interest bearing and are normally settled on 30 day terms.

11. Credit Facilities

The following table presents the continuity of the Corporation's credit facilities:

	Debt	Derivative liability	Total
Balance, December 31, 2016	\$ 4,671,063	\$ 29,781	\$ 4,700,844
Amounts advanced under Credit Facility B	417,180	—	417,180
Cash repayments	(30,000)	—	(30,000)
Accretion	131,066	—	131,066
Unpaid deferred fee added to Credit Facility A	80,467	—	80,467
Revaluation of derivative liability	—	(14,390)	(14,390)
Balance, December 31, 2017	5,269,776	15,391	5,285,167
Amounts advanced under Credit Facility B	300,000	—	300,000
Cash repayments	(310,000)	—	(310,000)
Disposition proceeds (Note 8)	(125,000)	—	(125,000)
Reversal of accretion (Note 18)	(219,651)	—	(219,651)
Expiry of share purchase warrants (Note 14(b))	—	(15,391)	(15,391)
Balance, December 31, 2018	\$ 4,915,125	\$ —	\$ 4,915,125

As at December 31, 2018, \$4,537,945 (December 31, 2017 - \$4,662,922) was outstanding in relation to Credit Facility A and \$377,180 (December 31, 2017 - \$387,180) was outstanding in relation to Credit Facility B.

PROSPERA ENERGY INC.

(formerly Georox Resources Inc.)

Notes to the Financial Statements

For the years ended December 31, 2018 and 2017

On September 8, 2017, the Corporation entered into a Forbearance Agreement and a Quitclaim with the lender (Note 2).

On March 27, 2018, the Corporation amended Credit Facility B to add additional security of a promissory note for \$125,000 and to increase the sum of the first supplemental debenture to \$7,500,000 from \$4,000,000. The amount available under Credit Facility B has increased to \$725,000 (from \$600,000) and was to be used for the purpose of funding a waterflood project and paying outstanding property taxes at the Corporation's Red Earth property.

Credit Facilities A and B (collectively, the "Amended Credit Facilities") are secured by promissory notes for \$4,622,945 and \$600,000, a \$25,000,000 fixed and floating charge debenture, a general security agreement on the assets of the Corporation and a \$4,000,000 debenture from the Corporation providing a security interest in all present and after-acquired personal property, a fixed charge on all the oil and gas assets and a floating charge over all other present and after-acquired real property.

Participation fee

Per the terms of the Amended Credit Facilities, the lender may be entitled to a participation fee on the 2018 net revenues (defined as total revenues less royalties) up to a cumulative amount of \$500,000.

Covenants

The Corporation is subject to the following covenants under the Amended Credit Facilities:

- A 1.0:1.0 current ratio;
- A Secured Debt to Trailing Cash Flow at or below 3.0 : 1.0;
- A corporate Licensee Liability Rating ("LLR") of 1.5 or greater; and,
- Maintain monthly sales production of 140 barrels of oil equivalent per day ("boepd").

Credit Facility A bears interest at 10% per annum, increasing to 19% per annum in the event of default. Credit Facility B bears interest at 12% per annum, increasing to 19% per annum in the event of default. Principal repayments on Credit Facility A of \$50,000 per month shall begin on the last day of the month following the repayment of Credit Facility B.

The Amended Credit Facilities were due on July 31, 2018. At December 31, 2018, the Corporation was in breach of all the covenants except for maintaining an LLR of 1.5 or greater. As at December 31, 2018, previously accrued default interest, participation and monitoring fees were forgiven by the lender (Note 18).

Subsequent to December 31, 2018, the Corporation and its lender signed an amending agreement with respect to the Amended Credit Facilities (Note 23(c)).

12. Provision for Decommissioning

The Corporation's provision for decommissioning as at December 31, 2018 and 2017 is based on the following estimates and assumptions:

- Total inflation-adjusted undiscounted future cash flows of \$11,730,546 (2017 – \$1,559,175)
- Annual inflation rate of 2% (2017 – 2%)
- Settlement of the liability occurring in approximately 2 to 16 years (2017 – 2 to 18 years)
- Risk free discount rate of 1.90% to 2.15% (2017 – 1.66% to 2.22%)

	2018	2017
Balance, beginning of year	\$ 1,327,194	\$ 1,319,704
Business combinations (Note 7)	3,094,355	–
Additions and revisions	4,999,936	(12,727)
Disposition (Note 8)	(105,124)	–
Accretion	82,483	20,217
Balance, end of year	\$ 9,398,844	\$ 1,327,194

PROSPERA ENERGY INC.

(formerly Georox Resources Inc.)

Notes to the Financial Statements

For the years ended December 31, 2018 and 2017

13. Taxes

The reconciliation of the Corporation's tax provision computed at the combined Canadian federal and provincial statutory rate of 27% (2017 – 26.5%) to the reported tax provision (recovery) is as follows:

	2018	2017
Loss for the year	\$ (6,291,479)	\$ (1,964,921)
Expected tax recovery	(1,868,799)	(520,704)
Non-deductible expenses	20,786	10,017
Change in deferred tax benefits not recognized	1,848,013	510,687
Deferred tax provision (recovery)	\$ –	\$ –

The combined statutory tax rate increased from 26.5% to 27% due to an increase in certain provincial corporate tax rates on January 1, 2018.

Unrecognized deductible temporary differences

Deferred tax assets have not been recognized for the following deductible temporary differences as it is not probable that future taxable profit will be available against which the Corporation can utilize the benefits:

	2018	2017
Property and equipment	\$ 1,886,145	\$ 3,783,458
Provision for decommissioning	9,398,844	1,327,194
Non-capital losses	6,372,006	5,838,839
Net capital losses	1,136,800	1,136,800
Credit facilities	–	235,066
Share issue costs and other	594,400	231,995
Unrecognized deductible temporary differences	\$ 19,388,195	\$ 12,553,352

As at December 31, 2018, the Corporation has approximately \$6.4 million (2017 – \$5.8 million) of non-capital losses available to reduce future taxable income. The non-capital losses expire at various times between 2027 and 2038.

As at December 31, 2018 and 2017, the Corporation has approximately \$1.1 million of net capital losses which can be applied against future capital gains. These losses do not expire.

14. Share Capital

a) Common shares

Authorized

The Corporation is authorized to issue an unlimited number of common shares.

Issued

	Number	Amount
Balance, December 31, 2016	22,973,895	\$ 10,106,434
Private placement (i)	3,044,570	116,957
Issued for services (ii)	353,846	20,000
Balance, December 31, 2017	26,372,311	10,243,391
Private placement (iii)(iv)	19,820,000	991,000
Private placement proceeds received in advance (Note 23(a))	–	366,000
Share issue costs (iv)	–	(61,000)
Balance, December 31, 2018	46,192,311	\$ 11,539,391

PROSPERA ENERGY INC.

(formerly Georox Resources Inc.)

Notes to the Financial Statements

For the years ended December 31, 2018 and 2017

- (i) On July 27, 2017, the Corporation completed a non-brokered private placement of 3,044,570 common shares at a price of \$0.07 per unit for gross proceeds of \$213,270. Each unit is comprised of one common share and a half-warrant. Each whole warrant is exercisable at \$0.14 per share until May 22, 2019. The fair value of the 1,522,285 share purchase warrants was estimated at \$96,163 using the Black-Scholes pricing model (Note 5(b)).
- (ii) During 2017, the Corporation issued 200,000 common shares at a value of \$10,000 and 153,846 common shares at a value of \$10,000 for services rendered to the Corporation by a consultant. The value of the shares was measured at the fair value of the services rendered.
- (iii) On May 28, 2018, the Corporation completed a non-brokered private placement of 19,700,000 common shares at a price of \$0.05 per share for gross proceeds of \$985,000. A director of the Corporation subscribed for 2,000,000 of the common shares.
- (iv) In connection with the May 28, 2018 non-brokered private placement, the Corporation incurred \$61,000 of share issue costs comprised of \$55,000 of finders' fees paid in cash and 120,000 common shares valued at \$0.05 per share.

b) Share purchase warrants

A continuity of the Corporation's share purchase warrants outstanding is as follows:

	Weighted Average Exercise Price	Number of Share Purchase Warrants	Amount
Balance, December 31, 2016	\$ 0.12	7,698,333	\$ 214,963
Unit private placement (Note 14(a)(i))	0.14	1,522,285	96,163
Balance, December 31, 2017	0.12	9,220,618	311,126
Expired	0.12	(7,698,333)	(214,963)
Balance, December 31, 2018	\$ 0.14	1,522,285	\$ 96,163

All share purchase warrants outstanding at December 31, 2018 are exercisable at \$0.14 per share until May 22, 2019.

c) Stock options

The Corporation's stock option plan provides for the granting of options to directors, officers, employees and consultants. Under the terms of the option plan, options issued will not exceed 10% of the issued and outstanding shares from time to time. The aggregate number of common shares reserved for issuance to any one director, officer or employee in any 12-month period shall not exceed 5% of the Corporation's issued and outstanding common shares at the date of grant, and the aggregate number of common shares reserved for issuance pursuant to options granted to any one consultant in any 12-month period may not exceed 2% of the Corporation's issued and outstanding common shares at the date of the grant. Stock options are non-assignable, non-transferrable and non-tradable and shall be exercisable for a term not to exceed five years from the date of the grant. The exercise price of stock options shall be fixed by the Corporation's Board of Directors on the basis of the market price of the Corporation's shares on the grant date.

A continuity of the Corporation's stock options outstanding is as follows:

	Number	Weighted- Average Exercise Price
Balance, December 31, 2016	1,200,000	\$ 0.14
Granted	350,000	0.07
Expired	(100,000)	(0.10)
Forfeited	(100,000)	(0.10)
Balance, December 31, 2017	1,350,000	0.09
Granted	1,000,000	0.05
Balance, December 31, 2018	2,350,000	\$ 0.07

On December 15, 2017, the Corporation granted 350,000 stock options to directors exercisable at \$0.07 per share, of which 150,000 expire on December 15, 2019 and 200,000 expire on December 15, 2020. The options vest as to 1/3 immediately,

PROSPERA ENERGY INC.

(formerly Georox Resources Inc.)

Notes to the Financial Statements

For the years ended December 31, 2018 and 2017

1/3 on June 30, 2018 and 1/3 on December 31, 2018. The fair value of the stock options was estimated at \$15,888 (\$0.045 per option) using the Black-Scholes pricing model (Note 5(b)) and was recognized as share-based payments expense over the vesting periods, of which \$126 was recorded in 2017 and \$15,762 was recorded in 2018.

On November 20, 2018, the Corporation granted 1,000,000 stock options exercisable at \$0.05 per share to certain consultants. The stock options vest immediately and expire on November 20, 2020. The fair value of the options was estimated at \$60,400 (\$0.06 per option) using the Black-Scholes pricing model (Note 5(b)) and recognized as share-based payments expense on the grant date.

The following table summarizes information about the stock options outstanding and exercisable as at December 31, 2018:

Expiry date	Number of Stock Options Outstanding	Number of Stock Options Exercisable	Exercise Price	Weighted-Average Contractual Life Remaining (Years)
June 9, 2019	200,000	200,000	\$ 0.10	0.44
December 15, 2019	150,000	150,000	\$ 0.07	0.96
November 20, 2020	1,000,000	1,000,000	\$ 0.05	1.89
December 15, 2020	200,000	200,000	\$ 0.07	1.96
October 6, 2021	800,000	800,000	\$ 0.09	2.77
	2,350,000	2,350,000		2.01

15. Per Share Amounts

	2018	2017
Loss for the year	\$ (6,921,479)	\$ (1,964,921)
Number of common shares, January 1	26,372,311	22,973,895
Effect of common shares issued	11,783,397	1,461,784
Basis weighted average number of common shares	38,155,708	24,435,679
Basic and diluted loss per share	\$ (0.18)	\$ (0.08)

All share purchase warrants and stock options were excluded from the diluted per share amounts as their effect is anti-dilutive in loss periods.

16. Petroleum and Natural Gas Sales

The following table represents the Corporation's petroleum and natural gas sales disaggregated by commodity:

	2018	2017
Petroleum	\$ 3,079,508	\$ 1,750,028
Natural gas	15,034	30,029
	\$ 3,094,542	\$ 1,780,057

The Corporation sells its petroleum and natural production pursuant to variable-price contracts which generally have a term of one year or less. The transaction price for variable priced contracts is based on the commodity index price and may include adjustments for quality, location or other factors depending on the contract terms. The Corporation delivers variable or fixed volumes of crude oil and variable volumes of natural gas to the respective counterparty throughout the contract period. Sales revenue is recognized when production is delivered to the contract counterparty. The transaction price that is used in determining the amount of sales revenue to recognize is subject to variability due to fluctuations in commodity prices over the contract period. Volumes delivered to the contract counterparty are limited to the Corporation's ability to transfer production. Sales revenue is recognized at a point in time when a customer obtains legal title to the product, which is when volumes are physically transferred to the contract counterparty. The amount of sales revenue recognized is based on the transaction price. Transaction price variability, discussed above, is recognized in the same period as the Corporation is not constrained in meeting its performance obligations.

During 2018, all of the Corporation's petroleum and natural gas sales were generated in Saskatchewan and Alberta and the production was sold primarily to four major customers. The Corporation's petroleum sales result from variable price contracts whereby the transaction price is predominantly based on the WTI index price in the transaction month with variable adjustments

PROSPERA ENERGY INC.

(formerly Georox Resources Inc.)

Notes to the Financial Statements

For the years ended December 31, 2018 and 2017

for quality, location and or other factors. The transaction price for all natural gas sales is based on the AECO benchmark price. Sales revenues are typically collected on the 25th day of the month following production.

The Corporation's four major customers represented 92% of petroleum and natural gas revenue for the year ended December 31, 2018 (2017 – two major customers represented 85%) and \$337,135 of trade receivables (2017 – \$120,982 two major customers). See Note 6.

17. Personnel Expenses

a) Salaries, benefits and consulting fees

The Corporation's statement of loss and comprehensive loss is prepared primarily by nature of expense, with the exception of \$48,708 of salaries and benefits and \$113,000 of consulting fees for management personnel which are included in general and administrative expenses for the year ended December 31, 2018 (2017 – \$30,000 of salaries and benefits and \$96,000 of consulting fees).

b) Key management compensation

Key management personnel include executive officers and non-executive directors. Executive officers are paid a salary and participate in the Corporation's stock option program. The executive officers include the Chief Executive Officer and Chief Financial Officer. Non-executive directors also participate in the Corporation's stock option program. Key management compensation is comprised of the following:

	2018	2017
Consulting fees	\$ 113,000	\$ 96,000
Salaries and benefits	48,708	30,000
Share-based payments	76,162	30,321
Deferred share units	18,875	22,250
	<u>\$ 256,745</u>	<u>\$ 178,571</u>

During 2018, 295,513 deferred share units ("DSUs") (2017 – 370,280) were granted to directors. The fair value DSUs granted in 2018 was \$18,875 (2017 – \$22,250) based on the market price of the Corporation's shares on the dates of grant, which is included in general and administrative expense.

	Number of DSUs	Amount
Balance, December 31, 2016	562,961	\$ 56,000
Granted	370,280	22,250
Revaluation	–	25,779
Balance, December 31, 2017	933,241	104,029
Granted	295,513	18,875
Cancelled	(244,885)	(5,750)
Revaluation	–	(72,880)
Balance, December 31, 2018	983,869	\$ 44,274

As at December 31, 2018, the Corporation had 983,869 DSUs outstanding (December 31, 2017 – 933,241) for which the aggregate fair value of \$44,274 (2017 – \$104,029) is included in trade and other payables.

PROSPERA ENERGY INC.

(formerly Georox Resources Inc.)

Notes to the Financial Statements

For the years ended December 31, 2018 and 2017

18. Finance (Expense) Recovery

	2018	2017
Interest expense	\$ (528,654)	\$ (687,683)
Accretion of credit facilities (Note 11)	—	(131,066)
Derivative revaluation (Note 11)	15,391	14,390
Forgiveness of interest, participation and monitoring fees	497,403	—
Reversal of accretion (Note 11)	219,651	—
Accretion of provision for decommissioning (Note 12)	(82,483)	(20,217)
	<u>\$ 121,308</u>	<u>\$ (824,576)</u>

In connection with the confirmation of amounts outstanding under the Corporation's credit facilities as at December 31, 2018, the Corporation recognized a \$717,054 recovery of finance expenses related to the lender's forgiveness of previously accrued default interest, participation and monitoring fees in the amount of \$497,403 and the \$219,651 reversal of previously recorded accretion on the outstanding debt amount (Note 11).

19. De-recognition of Debt

In November 2018, the Corporation settled a long standing dispute with an operator of its Red Earth properties, pursuant to which the Corporation accrued a contingency amount in trade and other payables in its 2017 financial statements. Following the receipt of notice on November 26, 2018 that the operator's writ enforcement and security agreement in respect of the Corporation's Red Earth properties were discharged, the Corporation recognized a \$343,253 gain on de-recognition of debt.

20. Related Party Transactions

- During 2018, \$117,255 (2017 – \$68,480) was expensed for legal services provided by a law firm of which a director of the Corporation is a partner. Included in trade and other payables at December 31, 2018 is \$123,044 (2017 – \$72,817) owing to this law firm.
- During 2018, management, consulting and engineering fees of \$113,000 (2017 – \$96,000), included in general and administrative expenses, were charged by an officer of the Corporation and by a Corporation controlled by an officer. Included in trade and other payables at December 31, 2018 is \$64,800 (2017 – \$14,000) owing to this officer.

The above transactions with related parties are in the normal course of business.

21. Financial Risk Management and Capital Management

The Corporation's activities expose it to a variety of financial risks arising from its financial assets and liabilities. The Corporation manages its exposure to financial risks by operating in a manner that minimizes its exposure to the extent practical. The main financial risks affecting the Corporation are:

a) Credit risk

The Corporation is exposed to credit risk in relation to its cash and trade and other receivables. Cash is held with highly-rated Canadian banks. Therefore, the Corporation does not believe these financial instruments are subject to material credit risk. The Corporation's trade and other receivables include amounts due from the sale of petroleum and natural gas. See Note 6.

b) Liquidity risk

The Corporation's approach to managing liquidity risk is to ensure that it will have sufficient liquidity to meet its financial liabilities when they become due. Management mitigates liquidity risk by maintaining banking and other borrowing facilities, continuously monitoring forecast and actual cash flows and actively seeking equity financing to assist with projected cash outflows. As at December 31, 2018, the Corporation has a working capital deficiency of \$7,648,144 and an accumulated deficit of \$22,414,435. The Corporation's ability to continue as a going concern (Note 2) is dependent on the successful completion of the waterflood program in the Red Earth CGU, successful closing of the January 2019 private placement (Note 23(a)), successful renegotiation of its credit facilities (Notes 11 and 23(c)), accessing additional financing and achieving profitable operations.

The Corporation's financial liabilities as at December 31, 2018 total \$9,335,417, comprised of \$4,420,292 of trade and other payables and \$4,915,125 of credit facilities, all of which are classified as current liabilities.

PROSPERA ENERGY INC.

(formerly Georox Resources Inc.)

Notes to the Financial Statements

For the years ended December 31, 2018 and 2017

c) Market risk

Interest rate risk

Interest rate risk is the risk that the fair value of future cash flows of a financial instrument will fluctuate with changes in market interest rates. The Corporation is not exposed to interest rate fluctuations at December 31, 2018 as there are no investments of excess cash in short-term money market investments and credit facilities are at fixed rates of interest.

Foreign currency risk

Management believes the foreign currency risk arising from currency exchange rate fluctuations related to financial instruments held in foreign currencies is negligible as the Corporation held no foreign denominated financial instruments as at December 31, 2018 and 2017.

Commodity price risk

The nature of the Corporation's operations results in exposure to commodity price fluctuations. The Corporation closely monitors commodity prices to determine the appropriate course of action to be taken. The Corporation does not hedge commodity price risk and has no physical forward price or financial derivatives sales contracts as at December 31, 2018 and 2017 or the years then ended.

For the year ended December 31, 2018, if production remained constant and the commodity prices earned by the Corporation changed by 10%, the Corporation's reported loss would vary by approximately \$285,000 (2017 – approximately \$178,000).

d) Capital management

The Corporation's policy is to maintain a strong capital base for the objectives of maintaining financial flexibility, to sustain the development of the Corporation's current capital projects and for future development of the Corporation. The Corporation monitors its working capital and expected capital spending and raises additional equity by the issue of share capital to manage its development plans. The Corporation has no externally imposed capital requirements apart from the banking covenants on the Corporation's credit facilities (Note 11). The Corporation continues to assess additional petroleum and natural gas projects and plans to raise additional debt or equity amounts as needed to fund acquisitions and to maintain sufficient working capital to meet administrative expenditures. The Corporation considers its capital structure to be working capital and shareholders deficiency. Management reviews its capital management approach on an ongoing basis and believes that this approach, given the relative size of the Corporation, is reasonable. There were no changes in the Corporation's approach to capital management during 2018. The Corporation's working capital deficiency at December 31, 2018 was \$7,648,144 (December 31, 2017 – \$7,204,444). The Corporation's shareholders' deficiency at December 31, 2018 was \$7,381,735 (2017 – \$1,832,418).

22. Commitment

The Corporation has a lease for office premises in the amount of \$2,456 per month until June 30, 2019.

23. Subsequent Events

a) Private placement

On January 29, 2019, the Corporation closed a non-brokered private placement for the issuance of 7,560,000 units at \$0.05 per unit for gross proceeds of \$378,000. Each unit is comprised of one common share and one warrant. Share purchase warrants are exercisable at \$0.12 per share until January 25, 2020. \$366,000 of proceeds were received prior to December 31, 2018. Officers and directors subscribed for 6,000,000 units.

b) Property disposition

On March 18, 2019, the Corporation signed a purchase and sale agreement for the disposition of its Silverdale CGU for \$330,000 of cash consideration. The disposition is expected to close on April 30, 2019.

c) Credit facilities

On April 30, 2019, the Corporation and its lender signed an amending agreement (the "Second Amending Agreement") with respect to the Amended Credit Facilities (Note 11). A summary of the amended terms are as follows:

- The maturity date of the Amended Credit Facilities shall be April 30, 2020;
- The interest rate on the Amended Credit Facilities shall reduce to 9.5% per annum effective upon the Corporation making a \$400,000 lump sum principal repayment funded from the sale proceeds of the Silverdale CGU (Note 23(b)) with any shortfall made up from the Corporation's working capital;

PROSPERA ENERGY INC.

(formerly Georox Resources Inc.)

Notes to the Financial Statements

For the years ended December 31, 2018 and 2017

- Upon the receipt of the \$400,000 lump sum principal repayment, the lender will provide \$400,000 of debt forgiveness such that the reduction of the principal amount owing under the Credit Facilities will be \$800,000;
- The interest rate shall be further reduced to 9% per annum upon the receipt of a second lump sum principal repayment in the amount of \$250,000 by no later than August 31, 2019;
- Upon the receipt of the \$250,000 lump sum principal repayment, the lender will provide \$250,000 of debt forgiveness such that the reduction of the principal amount owing under the Credit Facilities will be \$500,000;
- The Corporation shall make a \$500,000 lump sum principal repayment on October 31, 2019 or by December 31, 2019 as assessed by the lender;
- 100% of the net proceeds from the sale of any CGUs and 100% of the net proceeds from the issuance of debt shall be used to repay amounts owing under the Amended Credit Facilities;
- Monthly aggregate payments of \$100,000, inclusive of monthly interest, shall commence on April 30, 2019 and continue on the last day of each month thereafter;
- The Forbearance and Quitclaim shall remain in effect until April 30, 2020;
- Prepayment shall be permitted at any time with no penalty;
- In the event of default, the interest rate shall be 12% per annum;
- The Corporation shall be subject to the following amended covenants:
 - A 0.3:1.0 current ratio;
 - A Trailing Cash Flow (EBITDA) for the most recent quarter annualized) of not less than \$300,000;
 - A corporate LLR of 1.5 or greater; and,
 - Monthly sales production from Alberta properties of 55 boepd, reduced to 40 boepd in the event of the sale of the Corporation's Pouce Coupe CGU.