Consolidated Financial Statements of

CEQUENCE ENERGY LTD.

December 31, 2018 and 2017

Deloitte LLP
700, 850 2 Street SW
Calgary, AB T2P 0R8
Canada

Tel: 403-267-1700
Fax: 587-774-5379
www.deloitte.ca

Independent Auditor's Report

To the Shareholders and the Board of Directors of
Cequence Energy Ltd.

Opinion

We have audited the consolidated financial statements of Cequence Energy Ltd. (the "Company"), which comprise the consolidated balance sheets as at December 31, 2018 and 2017, and the consolidated statements of comprehensive loss, changes in equity and cash flows for the years then ended, and notes to the consolidated financial statements, including a summary of significant accounting policies (collectively referred to as the "financial statements").

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

Basis for Opinion

We conducted our audit in accordance with Canadian generally accepted auditing standards ("Canadian GAAS"). Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Statements* section of our report. We are independent of the Company in accordance with the ethical requirements that are relevant to our audit of the 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.

Other Information

Management is responsible for the other information. The other information comprises:

- Management's Discussion and Analysis
- The information, other than the financial statements and our auditor's report thereon, in the Annual Report.

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 audit of the financial statements, our responsibility is to read the other information identified above and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit, 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 in this auditor's report. We have nothing to report in this regard.

The Annual Report is expected to be made available to us after the date of the auditor's report. If, based on the work we will perform on this other information, we conclude that there is a material misstatement of this other information, we are required to report that fact to those charged with governance.

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 IFRS, 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 Company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Company or to cease operations, or has no realistic alternative but to do so.

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

Auditor's Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the 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 GAAS 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 GAAS, 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 Company's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Company's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Company to cease to continue as a going concern.

- Evaluate the overall presentation, structure and content of the 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 audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

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

The engagement partner on the audit resulting in this independent auditor’s report is Cody Duce.

Deloitte LLP

Chartered Professional Accountants

Calgary, Alberta

March 12, 2019

CEQUENCE ENERGY LTD.

Consolidated Balance Sheets
(Expressed in thousands of Canadian dollars)

	December 31, 2018 $	December 31, 2017 $
ASSETS		
CURRENT		
Cash	**14,496**	10,971
Accounts receivable (Note 7)	**10,324**	14,739
Deposits and prepaid expenses	**633**	514
Commodity contracts (Note 19)	**3,580**	1,274
	29,033	27,498
Property and equipment (Note 4)	**254,607**	257,230
	283,640	284,728
LIABILITIES		
CURRENT		
Accounts payable and accrued liabilities (Note 8)	**35,736**	33,106
Share-based payment liability (Note 16)	**38**	153
Provisions (Note 13)	**1,782**	1,466
Commodity contracts (Note 19)	**-**	998
Senior notes (Note 6)	**-**	59,341
	37,556	95,064
Term loan (Note 6)	**60,000**	-
Provisions (Note 13)	**33,773**	37,012
	131,329	132,076
COMMITMENTS (Note 18)		
SHAREHOLDERS' EQUITY		
Shareholders' capital (Note 15)	**642,123**	633,846
Warrants (Note 15)	**737**	1,300
Contributed surplus	**32,720**	31,076
Deficit	**(523,269)**	(513,570)
	152,311	152,652
	283,640	284,728

APPROVED BY THE BOARD

"Donald Archibald" Donald Archibald, Director

"Brian Felesky" Brian Felesky, Director

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

CEQUENCE ENERGY LTD.

Consolidated Statements of Comprehensive Loss
(Expressed in thousands of Canadian dollars except per share amounts)

	Year ended December 31, 2018 $	2017 $
REVENUE AND OTHER INCOME		
Production revenue (Note 9)	**56,227**	57,886
Other income (Note 10)	**4,207**	215
Gain on derivative financial instruments (Note 19)	**2,028**	9,739
	62,462	67,840
EXPENSES		
Operating costs	**24,080**	27,584
Transportation	**7,160**	5,571
Depletion and depreciation (Note 4)	**27,480**	24,606
Impairment (Note 4)	**-**	96,200
General and administrative (Note 12)	**5,267**	4,408
Finance costs (Note 11)	**7,874**	7,805
Share-based payment (Note 16)	**300**	1,028
	72,161	167,202
LOSS BEFORE INCOME TAXES	**(9,699)**	(99,362)
INCOME TAXES (Note 14)	**-**	-
NET LOSS AND COMPREHENSIVE LOSS	**(9,699)**	(99,362)
Loss per share (Note 17)		
Basic and diluted	**($0.61)**	($8.09)

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

CEQUENCE ENERGY LTD.

Consolidated Statements of Changes in Equity
(Expressed in thousands of Canadian dollars)

	Year ended December 31, 2018 $	2017 $
SHAREHOLDERS' EQUITY		
Shareholders' capital		
Balance, beginning of year	**633,846**	633,848
Proceeds on issuance of flow-through shares (Note 15)	**8,593**	-
Share issue costs (Note 15)	**(316)**	(2)
Balance, end of year	**642,123**	633,846
Warrants		
Balance, beginning of year	**1,300**	1,300
Warrants granted on refinancing of senior notes (Note 6 & 15)	**737**	-
Warrants expired (Note 15)	**(1,300)**	-
Balance, end of year	**737**	1,300
Contributed surplus		
Balance, beginning of year	**31,076**	30,085
Share-based payment expense (Note 16)	**344**	991
Warrants expired (Note 15)	**1,300**	-
Balance, end of year	**32,720**	31,076
Deficit		
Balance, beginning of year	**(513,570)**	(414,208)
Net loss	**(9,699)**	(99,362)
Balance, end of year	**(523,269)**	(513,570)
TOTAL SHAREHOLDERS' EQUITY	**152,311**	152,652

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

CEQUENCE ENERGY LTD.

Consolidated Statements of Cash Flows
(Expressed in thousands of Canadian dollars)

	Year ended December 31, 2018 $	2017 $
CASH FLOWS RELATED TO THE FOLLOWING ACTIVITIES:		
OPERATING		
Net loss	**(9,699)**	(99,362)
Adjustments for non-cash items:		
Depletion and depreciation expense (Note 4)	**27,480**	24,606
Impairment (Note 4)	**-**	96,200
Accretion expense on provisions (Note 11)	**803**	870
Share-based payment (Note 16)	**300**	1,028
Amortization of transaction costs (Note 11)	**371**	443
Refinancing expense – warrants (Note 11)	**737**	-
Accretion expense on senior notes (Note 11)	**288**	341
Unrealized gain on derivative financial instruments (Note 19)	**(3,303)**	(4,927)
Loss (gain) on sale of property and equipment (Note 10)	**(3,890)**	130
Abandonment costs incurred (Note 13)	**(3,756)**	(1,079)
Net change in non-cash working capital (Note 20)	**2,427**	1,634
Cash flow from operating activities	**11,758**	19,884
INVESTING		
Property and equipment expenditures (Note 4)	**(23,800)**	(25,857)
Property acquisitions (Note 4)	**-**	7
Proceeds from sale of property and equipment (Note 4)	**2,863**	4,270
Net change in non-cash working capital (Note 20)	**4,499**	(4,883)
Cash flow used in investing activities	**(16,438)**	(26,463)
FINANCING		
Cash settlement of share-based payments (Note 16)	**(72)**	(226)
Issue of common shares (Note 15)	**8,593**	-
Share issue costs (Note 15)	**(316)**	(2)
Net change in non-cash working capital (Note 20)	**-**	-
Cash flow from (used in) financing activities	**8,205**	(228)
NET INCREASE (DECREASE) IN CASH	**3,525**	(6,807)
CASH, BEGINNING OF YEAR	**10,971**	17,778
CASH, END OF YEAR	**14,496**	10,971

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

1. NATURE AND DESCRIPTION OF THE COMPANY

Cequence Energy Ltd. (the "Company" or "Cequence") is incorporated under the laws of Alberta with common shares that are widely held and listed on the Toronto Stock Exchange. Cequence is engaged in the acquisition, exploration and production of petroleum and natural gas reserves in Western Canada. The registered office of the Company is located at Suite 1400, 215 – 9th Avenue. SW, Calgary, Alberta, T2P 1K3.

These consolidated financial statements ("consolidated financial statements") include all assets, liabilities, revenues and expenses of Cequence and its wholly-owned subsidiary, 1175043 Alberta Ltd.

2. SIGNIFICANT ACCOUNTING POLICIES

Statement of compliance and authorization

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

The consolidated financial statements were authorized for issue by the Company's Board of Directors on March 12, 2019.

Basis of presentation

The consolidated financial statements have been prepared using historical costs, except for financial instruments carried at fair value. All financial information is presented in Canadian dollars, which is also the Company's functional currency. The accounting policies set out below have been applied consistently in all material respects.

Basis of consolidation

The consolidated financial statements include the accounts of the Company and its consolidated subsidiaries, which are the entities over which the Company has control. Control exists when the Company has the power to govern the financial and operating policies of an entity so as to obtain benefit from its activities. All intercompany transactions and balances are eliminated on consolidation.

Business combinations

The acquisition method of accounting is used to account for acquisitions of subsidiaries and assets that meet the definition of a business under IFRS. The cost of an acquisition is measured as the fair value of the assets given, equity instruments issued and liabilities incurred or assumed at the date of exchange. Acquisition-related costs are recognized in comprehensive loss as incurred. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date. The excess of the cost of acquisition over the fair value of the identifiable assets and liabilities acquired and contingent liabilities for which a provision is provided is recorded as goodwill. If the cost of acquisition is less than the fair value of the net assets of the subsidiary acquired, the difference is recognized as a bargain purchase gain in comprehensive loss. Results of subsidiaries are included in the consolidated statement of comprehensive loss from the closing date of acquisition.

Property and equipment and exploration and evaluation assets

Recognition and measurement

Exploration and evaluation expenditures

Pre-license costs, geological and geophysical costs are recognized in comprehensive loss as incurred.

Exploration and evaluation ("E&E") costs, including the costs of acquiring licenses, drilling exploratory wells and other directly attributable costs, are initially capitalized as E&E assets to the extent that they do not relate to a field with proven reserves attributed. The costs are accumulated in cost centers by field or exploration area pending determination of technical feasibility and commercial viability.

The Company enters into E&E farm-in arrangements to fund a portion of the partner's (farmor's) exploration and/or future development expenditures ("carried interests"), these expenditures are reflected in the consolidated financial statements when the exploration and development work progresses. For E&E farm-out arrangements where the farmee correspondingly undertakes to fund carried interests as part of the consideration no gain or loss is recognized by the Company.

E&E assets are assessed for impairment if sufficient data exists to determine technical feasibility and commercial viability, or if facts and circumstances suggest that the carrying amount exceeds the recoverable amount.

The technical feasibility and commercial viability of extracting a mineral resource is considered to be determinable when proven reserves are determined to exist and are capable of economic production. A review of each exploration field is carried out, at least annually, to ascertain whether proven reserves have been discovered that are capable of economic production. Upon determination of proven reserves, E&E assets attributable to those reserves are first tested for impairment and then reclassified from E&E assets to development and production assets included in property and equipment.

Development and production costs

Items of property and equipment, which include oil and gas development and production assets, are measured at cost less accumulated depletion and depreciation and accumulated impairment losses, net of any reversals.

Development and production assets are grouped into Cash Generating Units ("CGUs") for impairment testing. CGUs are defined as the smallest identifiable group of assets that generates cash inflows that are largely independent of the cash inflows from other assets or groups of assets. The Company evaluates the geography, geology, production profile and infrastructure of its assets in determining its CGUs. Based on this assessment, Cequence's CGUs are generally composed of significant development areas. The Company reviews the composition of its CGUs at each reporting date to assess whether any changes are required in light of new facts and circumstances.

When significant parts of an item of property and equipment, including oil and natural gas interests, have different useful lives, they are accounted for as separate items (major components).

Gains and losses on disposal of an item of property and equipment, including oil and natural gas interests, are determined by comparing the proceeds from disposal with the carrying amount of the related property and equipment and are recognized net within "other expense (income)".

Impairment

The carrying amounts of all assets, other than financial assets and deferred tax assets, are reviewed at each reporting date to determine whether there is indication of an impairment loss. If any such indication exists, the asset's recoverable amount is estimated.

For any asset that does not generate largely independent cash flows, the recoverable amount is determined for the CGU to which the asset belongs. If the carrying amount of an asset (or CGU) exceeds its recoverable amount, the asset (or CGU) is written down.

The recoverability of the carrying amount of an E&E asset is dependent on successful development and commercial exploitation, or alternatively, sale of the respective area of interest. Where a potential impairment is indicated, an assessment is performed for each field or area to which the E&E expenditure is attributed. To the extent that capitalized expenditures are not expected to be recovered, the excess of the carrying amount over the recoverable amount is recognized immediately in comprehensive loss.

The recoverable amount of a development and production asset (or CGU) or other intangible asset (or CGU) is determined as the higher of its value in use and fair value less cost to sell. Value in use is determined by estimating future cash flows after taking into account the risks specific to the asset (or group of assets within a CGU) and discounting them to their present value using a pre-tax discount rate that reflects the current market assessment of the time value of money. In determining fair value less cost to sell, an appropriate valuation model is used. These calculations are corroborated by external valuation metrics or other available fair value indicators wherever possible.

Where the carrying amount of a development and production asset (or CGU) or other intangibles asset (or CGU) exceeds its recoverable amount, the excess is recognized immediately in comprehensive loss.

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 only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or depletion, if no impairment loss had been recognized.

Subsequent costs

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

Depletion and depreciation

The net carrying value of development and production assets plus future development costs on proved plus probable reserves is depleted using the unit of production method based on proved and probable reserves, as determined by independent engineers, on an area by area basis. For the purpose of this calculation, production and reserves of petroleum and natural gas are converted to a common unit of measurement on the basis of their relative energy content, where six thousand cubic feet of natural gas equates to one barrel of oil. Costs are only depleted once production in a given area begins.

Cequence depletes separately, where applicable, any significant components within development and production assets, such as fields, processing facilities and pipelines, which are significant in relation to the total cost of a development and production asset and have a different useful life than such assets.

Provisions

Provisions are recognized when the Company has a present obligation as a result of a past event that can be estimated with reasonable certainty and are measured at the amount that the Company would rationally pay to be relieved of the present obligation. To the extent that provisions are estimated using a present value technique, such amounts are determined by discounting the expected future cash flows at a risk-free pre-tax rate and adjusting the liability for the risks specific to the liability.

Decommissioning liabilities

The Company records the present value of the estimated cost of legal and constructive obligations to restore operating locations in the period in which the obligation arises. The nature of restoration activities includes the removal of facilities, abandonment of wells and restoration of affected areas. Provision is made for the estimated cost of restoration and capitalized in the relevant asset category.

Decommissioning liabilities are measured at the present value of management's best estimate of the expenditure required to settle the present obligation at the balance sheet date. Subsequent to the initial measurement, the obligations are adjusted at the end of each period to reflect the passage of time and changes in the estimated future cash flows underlying the obligation as well as changes to the discount rate. The increase in the provision due to the passage of time is recognized as finance cost whereas increases or decreases due to changes in the estimated future cash flows or changes in the discount rate are capitalized. Actual costs incurred upon settlement of the decommissioning liabilities are charged against the decommissioning liabilities.

Onerous contracts

Present obligations arising under onerous contracts are recognized and measured as provisions. An onerous contract is considered to exist where the Company has a contract under which the unavoidable costs of meeting the obligations under the contract exceed the economic benefits expected to be received from the contract.

Jointly controlled assets

A significant portion of the Company's oil and natural gas activities involve jointly controlled assets and any related liabilities incurred. The consolidated financial statements include the Company's share of these jointly controlled assets and liabilities and a proportionate share of the relevant revenues and related costs, classified according to their nature. Joint control exists for contractual arrangements whereby the Company has less than a 100 percent working interest, all of the partners have control of the arrangement collectively, and spending on the project requires unanimous consent of all parties that collectively control the arrangement and share the associated risks. The Company does not have joint arrangements that are individually material to the Company.

Share-based payments

The Company has a stock option plan and issues stock options to directors, officers, employees and other service providers. Compensation costs attributable to stock options granted are measured at fair value at the date of grant and are expensed over the vesting period, using a graded vesting schedule, with a corresponding increase in contributed surplus. When stock options are exercised, the cash proceeds together with the amount previously recorded as contributed surplus are recorded as share capital. The Company incorporates an estimated forfeiture rate for stock options that will not vest, and subsequently adjusts for actual forfeitures as they occur.

The Company issues Restricted Share Units ("RSU") under the RSU Plan to directors, officers and other service providers. RSUs are accounted as cash-settled share-based payments and are originally measured at the grant date fair value and subsequently remeasured each period end until the vesting date when the RSUs are settled in cash. Share-based payment expense on the RSUs is charged to net earnings or loss in the period they vest with a corresponding adjustment to share-based payment liability. The Company incorporates an estimated forfeiture rate for RSUs that will not vest, and subsequently adjusts for actual forfeitures as they occur.

Flow-through shares

The Company, from time to time, issues flow-through shares to finance a portion of its capital expenditure program. Pursuant to the terms of the flow-through share agreements, the tax deductions associated with the expenditures are renounced to the subscribers. The difference between the value ascribed to flow-through shares issued and the value, if any, that would have been received for common shares at the date of issuance of the flow-through shares is initially recognized as a liability on the consolidated balance sheet. When the expenditures are renounced and incurred, the liability is drawn down, a deferred income tax liability is recorded equal to the estimated amount of deferred income tax payable by the Company as a result of the renunciation, and the difference is recognized as income tax expense.

Earnings per share

Basic per share amounts are computed by dividing the net loss by the weighted average number of common shares outstanding during the period. Diluted per share amounts are calculated giving effect to the potential dilution that would occur if stock options, RSUs and warrants were exercised. The dilutive effect of stock options, RSUs and warrants is calculated with the assumption that proceeds received from the exercise of options, RSUs and warrants for which the exercise price is less than the market price plus the unamortized portion of share-based payments are used to repurchase common shares at the average market price for the period.

Taxation

Income tax expense represents the sum of the tax currently payable and deferred tax.

Current tax

The tax currently payable is based on taxable income for the year. Taxable income differs from income as reported in the consolidated statement of comprehensive loss because of items of income or expense that are taxable or deductible in other years and items that are never taxable or deductible. The Company's liability for current tax is calculated using tax rates that have been enacted or substantively enacted by the end of the reporting period.

Deferred tax

Deferred tax is recognized on temporary differences between the carrying amounts of assets and liabilities in the financial statements and the corresponding tax bases used in the computation of taxable income.

Deferred tax assets are generally recognized for all deductible temporary differences to the extent that it is probable that taxable profits will be available against which such deductible temporary differences can be utilized. Such deferred tax assets and liabilities are not recognized if the temporary difference arises from goodwill or from the initial recognition (other than in a business combination) of other assets and liabilities in a transaction that affects neither taxable income nor the accounting income.

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

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply in the period in which the liability is settled or the asset realized, based on tax rates (and tax laws) that have been enacted or substantively enacted by the end of the reporting period. The measurement of deferred tax liabilities and assets reflects the tax consequences that would follow from the manner in which the Company expects, at the end of the reporting period, to recover or settle the carrying amount of its assets and liabilities.

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

Current and deferred tax for the period

Current and deferred tax are recognized as an expense or income in comprehensive loss, except when they relate to items that are recognized outside profit or loss (whether in other comprehensive income or directly in equity), in which case the tax is also recognized outside profit or loss, or where they arise from the initial accounting for a business combination. In the case of a business combination, the tax effect is included in the accounting for the business combination.

Significant accounting judgments, estimates and assumptions

The preparation of the consolidated financial statements in conformity with IFRS requires management to make judgments, estimates and assumptions that affect the reported amount of assets, liabilities, and contingent liabilities at the date of the consolidated financial statements and reported amounts of revenues and expenses during the reporting period. Estimates and judgments are continuously evaluated and are based on management’s experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

In particular, information about significant areas of estimation uncertainty considered by management in preparing the consolidated financial statements are described as follows:

- Estimates of recoverable quantities of proved and probable reserves include assumptions regarding commodity prices, exchange rates, discount rates, future development costs and production and transportation costs for future cash flows. It also requires interpretation of geological and geophysical models in order to make an assessment of the size, shape, depth and quality of reservoirs, and their anticipated recoveries. The economic, geological and technical factors used to estimate reserves may change from period to period. Changes in reported reserves can impact asset carrying values, the provision for decommissioning liabilities and the recognition of deferred tax assets, due to changes in expected future cash flows. Reserve estimates are prepared in accordance with the Canadian Oil and Gas Evaluation Handbook and are reviewed by third party reservoir engineers.

- The amounts recorded for depletion and depreciation of property and equipment, the provision for decommissioning liabilities, and the valuation of property and equipment are based on estimates of proved and probable reserves, production rates, future petroleum and natural gas prices, future costs and the remaining lives and period of future benefit of the related assets.

- The Company makes judgments in determining its CGUs and evaluates the geography, geology, production profile and infrastructure of its assets in making such determinations, which are based on estimates of reserves. Based on this assessment, Cequence's CGUs are generally composed of significant development areas. The Company reviews the composition of its CGUs at each reporting date to assess whether any changes are required in light of new facts and circumstances.

- Costs associated with acquiring oil and natural gas licenses and exploratory drilling are accumulated as E&E assets pending determination of technical feasibility and commercial viability. Establishment of technical feasibility and commercial viability is subject to judgement which management has determined to be based on the allocation of commercial reserves to the exploration area. Upon determination of commercial reserves, E&E assets attributable to those reserves are first tested for impairment and then reclassified from E&E assets to development and production assets included in property and equipment.

- The amount recorded as decommissioning liabilities is based on current legal and constructive requirements, technology, price levels and expected plans for remediation. Actual costs and cash outflows can differ from estimates because of changes in laws and regulations, public expectations, market conditions, discovery and analysis of site conditions and changes in technology.

- The amounts recorded for deferred income tax assets and deferred tax expense (recovery) are based on estimates of the probability of the Company utilizing certain tax pools and assets which, in turn, is dependent on estimates of proved and probable reserves, production rates, future petroleum and natural gas prices, and changes in legislation, tax rates and interpretations by taxation authorities.

- The fair value of derivative contracts is estimated, wherever possible, based on quoted market prices, and if not available, on estimates from third-party brokers. Another significant assumption used by the Company in determining the fair value of derivatives is market data or assumptions that market participants would use when pricing the asset or liability, including assumptions about risk. The actual settlement of derivatives could differ materially from the value recorded and could impact future results.

The above judgments, estimates and assumptions relate primarily to unsettled transactions and events as of the date of the consolidated financial statements. Actual results could differ from these estimates and the differences could be material.

3. CHANGES IN ACCOUNTING POLICIES

IFRS 15 "Revenue from contracts with customers"

Cequence adopted IFRS 15 with a date of initial application of January 1, 2018. IFRS 15 replaces existing revenue recognition guidance and provides a single, principles-based five-step model to be applied to all contracts with customers. Cequence used the modified retrospective approach to adopt the new standard, applying the standard retrospectively only to contracts that were not completed contracts on January 1, 2018. Under the transitional provision, the cumulative effect of initially applying IFRS 15 is recognized on the date of initial application as an adjustment to deficit. As a result of applying the requirements of IFRS 15, including the application of certain practical expedients such as the right to invoice method of measuring the Company's progress towards complete satisfaction of its performance obligations, there was no change or adjustments to the Company's consolidated financial statements as a result of the adoption of IFRS 15. Additional disclosure requirements required by IFRS 15 are detailed in Note 9.

Cequence recognizes revenue at a point in time when control of the product has been transferred to the customer and performance obligations have been satisfied. This is generally met when the customer obtains legal title to the product and physical delivery at a delivery point has taken place. Revenue is measured based on the consideration specified in the contracts the Company has with its customers.

Cequence evaluates its arrangements with 3rd parties and partners to determine if the Company acts as the principal or as an agent. In making this evaluation, management considers if it obtains control of the product delivered, which is indicated by the Company having the primary responsibility for the delivery of the product, having the ability to establish prices or having inventory risk. If Cequence acts in the capacity of an agent rather than as a principal in a transaction, then the revenue is recognized on a net-basis, only reflecting the fee, if any, realized by the party from the transaction.

Interest income is recognized as it accrues, using the effective interest method.

IFRS 9 "Financial Instruments"

On January 1, 2018, Cequence adopted IFRS 9 as issued by the IASB. IFRS 9 includes a new classification and measurement approach for financial assets and liabilities, and a new expected loss impairment model for financial assets including credit losses. The adoption of IFRS 9 did not have a material impact on Cequence's consolidated financial statements. Additional disclosures related to Cequence's financial assets are included in Note 19. Cequence has revised the description of its accounting policy for financial instruments to reflect the new classifications approach as follows:

Financial Instruments

A financial instrument is any contract that gives rise to a financial asset of one entity and a financial liability or equity instrument of another entity. Financial assets and financial liabilities are recognized on the consolidated balance sheet at the time the Company becomes a party to the contractual provisions. Upon initial recognition, financial instruments are measured at fair value. Measurement in subsequent periods is dependent on the classification of the financial instrument.

The Company has made the following classifications:

- Fair value through profit or loss: Financial instruments under this classification include cash and commodity contract assets and liabilities.
- Amortized cost: Financial instruments under this classification included accounts receivable, deposits, demand credit facilities, Term Loan, Senior Notes, accounts payable and accrued liabilities.

IFRS 9 also introduces a new model for the measurement of impairment of financial assets based on expected credit losses which replaces the incurred losses impairment model applied under IAS 39. Under this new model, Cequence's accounts receivable are considered collectible within one year or less; therefore, these financial assets are not considered to have a significant financing component and a lifetime ECL is measured at the date of initial recognition of the accounts receivable.

For accounts receivable, the Company assesses the lifetime ECL applicable to its commodity product sales receivables and joint venture receivables at initial recognition and re-assesses the provision at each reporting date. The majority of the Company's accounts receivable are due from joint venture partners in the oil and gas industry and from marketers of the Company's petroleum and natural gas production. In making an assessment as to whether Cequence's financial assets are credit impaired, the Company considers historical bad debts, the counterparties financial condition, credit rating and total financial exposure. The carrying amounts of receivables are reduced by the amount of the ECL through an allowance account and losses are recognized within general and administrative expense in comprehensive loss.

The Company considers all amounts greater than 90 days past due. These past due accounts are considered to be collectible, except as provided in the allowance for doubtful accounts. When determining whether past due accounts are uncollectible, the Company factors in the past credit history of the counterparties.

Transaction costs related to financial instruments classified as fair value through profit or loss are expensed as incurred. All other transaction costs related to new financial instruments are recorded as part of the instrument and are amortized using the effective interest method.

Contracts that are entered into for the purpose of the receipt or delivery of a non-financial item in accordance with the Company's expected purchase, sale or usage requirements (such as physical delivery commodity contracts) do not qualify as financial instruments and thus, are accounted for in accordance with other applicable standards and are not recorded as assets or liabilities.

Embedded derivatives are separated from the host contract and accounted for separately if the economic characteristics and risks of the host contract and the embedded derivative are not closely related, a separate instrument with the same terms as the embedded derivative would meet the definition of a derivative, and the combined instrument is not measured at fair value through profit or loss. Changes in the fair value of separable embedded derivatives are recognized immediately in comprehensive loss.

IFRS establishes a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The three levels of the fair value hierarchy are described below:

Level 1: Values based on quoted prices in active markets that are accessible at the measurement date for identical assets or liabilities.

Level 2: Values based on quoted prices in markets that are not active or model inputs that are observable either directly or indirectly for substantially the full term of the asset or liability.

Level 3: Values based on prices or valuation techniques that require inputs that are both unobservable and significant to the overall fair value measurement.

When the inputs used to measure fair value fall within different levels of the hierarchy, the level within which the fair value measurement is categorized is based on the lowest level input that is significant to the fair value measure in its entirety.

(All figures expressed in thousands except per share amounts unless otherwise noted)

IFRS 16 "Leases"

IFRS 16 'Leases' was issued by the IASB in January 2016. IFRS 16 replaces the existing standard IAS 17 and requires the recognition of most leases on the balance sheet. IFRS 16 effectively removes the classification of leases as either finance or operating leases and treats all leases as finance leases for lessees with exemptions for short-term leases where the term is twelve months or less and for leases of low value items. The accounting treatment for lessors remains the same. IFRS 16 is effective January 1, 2019, with earlier application permitted. The Company is in the process of assessing the impact of the adoption of this standard on the Company's consolidated financial statements.

4. PROPERTY AND EQUIPMENT

Cost:	
Balance at December 31, 2016	925,094
Additions	25,857
Decommissioning obligation additions and change in estimates	1,302
Acquisitions	(7)
Disposals	(23,311)
Balance at December 31, 2017	928,935
Additions	**23,800**
Decommissioning obligation additions and change in estimates	**2,179**
Acquisitions	**-**
Disposals	**(39,997)**
Balance at December 31, 2018	**914,917**
Depletion, depreciation and impairment:	
Balance at December 31, 2016	(569,036)
Depletion and depreciation	(24,606)
Impairment loss	(96,200)
Disposals	18,137
Balance at December 31, 2017	(671,705)
Depletion and depreciation	**(27,480)**
Disposals	**38,875**
Balance at December 31, 2018	**(660,310)**
Carrying amounts:	
At December 31, 2017	257,230
At December 31, 2018	**254,607**

Costs subject to depletion include $859,026 of estimated future capital costs (December 31, 2017 – $840,601).

The Company's credit facilities are secured by a demand debenture with a first floating charge over all assets of the Company (see note 5).

(All figures expressed in thousands except per share amounts unless otherwise noted)

Sale of assets

During the year ended December 31, 2018, the Company completed sales of certain oil and gas properties, including associated decommissioning obligation liabilities, for proceeds of $2,863 (2017 - $4,270), subject to final adjustments. The sales resulted in a gain recognized in other income in the statement of comprehensive loss of $3,890 (2017 - $130 loss).

Impairment

June 30, 2017

The Company reviewed each CGU comprising its property and equipment at June 30, 2017 for indicators of impairment and determined that indicators were present, related to the further reduction in the Company's enterprise value and decreases to future crude oil and natural gas prices used to estimate the value in use and fair value less cost to sell of each of the Company's CGUs.

As a result, impairment tests were carried out at June 30, 2017. The recoverable amounts of each of the Company's CGUs at June 30, 2017 were estimated as their fair value less cost to sell, based on the net present value of discounted future cash flows from oil and gas reserves as estimated by the Company's independent reserves evaluator at December 31, 2016 updated for management's best estimate of current price forecasts and consideration to acquisition metrics of recent transactions completed on similar assets to those contained within the relevant CGU. The Company also included the fair value of undeveloped land based on an internal evaluation with consideration of recent land sales. The fair value less costs of disposal values used to determine the recoverable amounts are classified as Level 3 fair value measurements as certain key assumptions are not based on observable market data but, rather, management's best estimates.

The Company used an after-tax 11% discount rate for the June 30, 2017 impairment tests which took into account the risks specific to the CGUs and current market assessment of the time value of money.

The estimated recoverable amounts used in the June 30, 2017 impairment tests were $7,425 for the Northeast British Columbia CGU, $2,497 for the Peace River Arch CGU and $255,999 for the Deep Basin CGU.

Results of the Company's impairment test at June 30, 2017 are as follows:

	2017
Northeast British Columbia	**-**
Peace River Arch	**2,200**
Deep Basin	**94,000**
Total Impairment	**96,200**

As at June 30, 2017, a one percent increase in the discount rate applied to the Company's future estimated cash flows would result in an additional impairment of $22,286, whereas a ten percent decrease in forward commodity prices would result in additional impairment of $106,947 recognized in comprehensive loss for the year ended December 31, 2017.

(All figures expressed in thousands except per share amounts unless otherwise noted)

December 31, 2017

The Company reviewed each CGU comprising its property and equipment at December 31, 2017 for indicators of impairment and determined that indicators were present, related to the further reduction in the Company's enterprise value and decreases to future crude oil and natural gas prices used to estimate the value in use and fair value less cost to sell of each of the Company's CGUs. As a result, impairment tests were carried out at December 31, 2017. Based on the impairment tests performed, the Company determined that the recoverable amounts of each of the Company's CGUs exceeded its carrying value and accordingly, no impairment expense was recorded.

December 31, 2018

The Company identified impairment indicators at December 31, 2018 related to the Company's market capitalization being less than the carrying amount of its net assets and the continued commodity price downturn.

As a result, impairment tests were carried out at December 31, 2018. The recoverable amounts of each of the Company's CGUs at December 31, 2018 were estimated as their fair value less cost to sell, based on the net present value of discounted future cash flows from oil and gas reserves as estimated by the Company's independent reserves evaluator at December 31, 2018 and consideration to acquisition metrics of recent transactions completed on similar assets to those contained within the relevant CGU. The Company also included the fair value of undeveloped land based on an internal evaluation with consideration to recent land sales. The fair value less costs of disposal values used to determine the recoverable amounts are classified as Level 3 fair value measurements as certain key assumptions are not based on observable market data but, rather, management's best estimates. The Company used an after-tax 12% discount rate for the December 31, 2018 impairment tests which took into account the risks specific to the CGUs and current market assessment of the time value of money.

Based on the impairment tests performed at December 31, 2018, the Company determined that the recoverable amounts of each of the Company's CGUs exceeded its carrying value and accordingly, no impairment expense was recorded. The determination of impairment is sensitive to changes in key judgments, including reserve or resource revisions, changes in forward commodity prices and exchange rates, and changes in costs and timing of development. Changes in these key judgments would impact the recoverable amount of the Company's CGUs, therefore resulting in additional impairment charges or recoveries.

The benchmark escalated prices on which the December 31, 2018 impairment tests are based are as follows:

	Natural Gas	**Condensate**	**Crude Oil**
	AECO Spot ($/mmbtu)	Edmonton Pentanes Plus ($/bbl)	Edmonton Par ($/bbl)
2019	1.85	67.67	63.33
2020	2.29	79.22	75.32
2021	2.67	83.54	79.75
2022	2.90	85.49	81.48
2023	3.14	87.80	83.54
2024	3.23	90.30	86.06
2025	3.34	93.33	89.09
2026	3.41	96.86	92.62
2027	3.48	98.81	94.57
2028	3.54	100.80	96.56

Prices increase at a rate of approximately 2.0 percent per year for natural gas, condensate and crude oil after 2028. Adjustments were made to the benchmark prices, for purposes of the impairment tests, to reflect varied delivery points and quality differentials in the products delivered.

5. DEMAND CREDIT FACILITIES

As at December 31, 2018, the Company has an extendible revolving term credit facility (the "Credit Facility") of $7,000 (December 31, 2017 - $12,000) with one Canadian chartered bank and has drawn $nil (December 31, 2017 - $nil) under the facility. The Company has letters of credit outstanding of $1,590 (December 31, 2017 - $1,540).

Prime loans and U.S. Base Rate Loans on the facility bear interest at the bank prime rate or U.S. Base Rate, respectively, plus 1.0 percent to 3.5 percent on a sliding scale, depending on the Company's debt to adjusted EBITDA ratio (ranging from being less than or equal to 1.0:1.0 to greater than 3.5:1.0). Banker's Acceptances, Libor Loans and letters of credit on the facility bear interest at the Banker's Acceptance rate, Libor rate or letter of credit rate, as applicable, plus 2.0 percent to 4.5 percent based on the same sliding scale as above. The credit facility is secured by a general assignment of book debts and a $250,000 demand debenture with a first floating charge over all assets of the Company. The Company is permitted to hedge up to 67 percent of its production under the lending agreement.

The Company has a covenant that requires Senior Debt to EBITDA, as defined in the bank agreement, to be less than 3:0 to 1:0. Senior Debt is defined as the sum of Consolidated Debt less the period end balance of the Term Loan. Consolidated Debt is defined as the sum of the Company's period end balance of the Credit Facility and Term Loan. The Company was in compliance with the lender's covenants at December 31, 2018 and December 31, 2017.

The Credit Facility has a term date of May 31, 2019. The term date may be extended beyond the initial term, if requested by the Company and accepted by the lenders. If the senior credit facility does not continue to revolve, amounts borrowed under the facility must be repaid on the term date. The Credit Facility is reviewed on a semi-annual basis with the lender holding the right to request an additional review as may be required. The next scheduled review is to take place in May 2019.

6. SENIOR NOTES AND TERM LOAN

Senior Notes

On October 3, 2013, Cequence issued $60,000 of unsecured five-year term notes ("Senior Notes") at par with a 9% coupon per annum for gross proceeds net of transaction costs of $57,974. The Senior Notes are unsecured and are subordinate to Cequence's credit facilities. The Senior Notes were issued pursuant to a trust indenture with a Canadian trust company, which provides for an additional $60,000 of unsecured senior notes at a future date, subject to approval of both the lender and the Company on terms to be confirmed at the time of issuance.

On July 27, 2018, Cequence entered into a second lien secured loan agreement with the Senior Note lender to refinance the Senior Notes as further described below under Term Loan.

The Senior Notes were subject to the same financial covenants as the Company credit facilities as well as other non-financial covenants and restrictive covenants, including restrictions over asset sales, restricted payments and the incurrence of additional indebtedness. The Company was in compliance with the Senior Notes covenants at July 27, 2018 prior to refinancing and December 31, 2017.

(All figures expressed in thousands except per share amounts unless otherwise noted)

Term Loan

On July 27, 2018, Cequence entered into a second lien secured loan agreement with the Senior Note lender for a $60,000 loan facility due October 3, 2022 (the "Term Loan") to refinance the existing Senior Notes which were due on October 3, 2018. Finance costs include $962 of legal, advisory and other professional fees related to refinancing the existing Senior Notes (Note 11).

Interest will be paid quarterly at the rate of 5% per annum if the 12-month trailing Funds Flow from Operations is equal to or less than $40 million; and 10% per annum if the 12-month trailing Funds Flow from Operations is greater than $40 million. Funds Flow from Operations is defined as cash flow from operating activities before decommissioning liability expenditures and net change in non-cash working capital.

Cequence has granted the lender second lien security over all of the Company's assets (with the exception of its Simonette joint venture property) through a $100,000 demand debenture, which will rank junior in priority to the security securing the obligations under the Company's Credit Facility pursuant to an intercreditor agreement. The Term Loan is subject to a cross default clause and the same financial covenants as the Company's Credit Facility as well as certain other non-financial covenants and restrictive covenants, including restrictions over asset sales, restricted payments, the incurrence of additional indebtedness and other transactions outside of the ordinary course of business.

As part of the refinancing Cequence issued 1,841 share purchase warrants entitling the lender to purchase common shares of the Company at a price of $2.00 per common share which are exercisable for four years from the date of issuance. Based on a Black-Scholes option pricing model, the fair value of the warrants was calculated as $737 and recorded to finance costs in the statement of comprehensive loss (note 11).

A summary of the inputs used to value the warrants is as follows:

Risk-free interest rate	**2.21%**
Expected life	**4 years**
Expected volatility	**85%**
Expected dividend rate	**0%**

At any time prior to the maturity of October 3, 2022, the Company has the option to make voluntary prepayments without penalty towards the Term Loan. Subject to restrictions in the intercreditor agreement, there are mandatory repayments related to asset sales and the incurrence of unsecured debt.

On December 17, 2018, the Term Loan and 1,841 share purchase warrants (the "Warrants") were purchased from the lender by an individual who, in subsequent transactions, sold interests in the Term Loan and Warrants to a small group of persons, including two of the Company's directors who at December 31, 2018 hold $11.5 million of the outstanding Term Loan. Interest expense of $49 was incurred and owing at December 31, 2018 to the two directors. There have been no changes to the terms and conditions of the Term Loan.

(All figures expressed in thousands except per share amounts unless otherwise noted)

7. ACCOUNTS RECEIVABLE

	December 31, 2018	December 31, 2017
Trade receivables	**3,035**	6,572
Allowance for doubtful accounts	**(760)**	(659)
Net trade receivables	**2,275**	5,913
Accrued receivables	**7,884**	8,609
Other receivables	**165**	217
Total accounts receivable	**10,324**	14,739

8. ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

	December 31, 2018	December 31, 2017
Accounts payable	**10,750**	9,549
Accrued liabilities	**24,986**	23,557
Total accounts payable and accrued liabilities	**35,736**	33,106

9. PRODUCTION REVENUE

Cequence sells its oil, natural gas, and natural gas liquids production pursuant to variable price contracts. The transaction price for variable priced contracts is based on a benchmark commodity price, adjusted for quality, location or other factors, whereby each component of the pricing formula (apart from the benchmark commodity price) can be either fixed or variable, depending on the contract terms. Revenues are typically collected on the 25th day of the month following the prior month's production, with revenue being recorded once the product is delivered to a contractually agreed upon delivery point.

The following table presents Cequence's production disaggregated by revenue source:

	Year ended December 31,	
	2018	2017
Natural gas	**26,327**	33,121
Crude oil and condensate	**30,389**	25,056
Natural gas liquids	**3,480**	2,847
Royalties	**(3,969)**	(3,138)
Total production revenue	**56,227**	57,886

(All figures expressed in thousands except per share amounts unless otherwise noted)

10. OTHER INCOME

	Year ended December 31, 2018	2017
Gain (loss) on sale of property and equipment	**3,890**	(130)
Interest income	**126**	102
Other	**191**	243
Total other income	**4,207**	215

11. FINANCE COSTS

	Year ended December 31, 2018	2017
Interest expense on demand credit facilities	**121**	331
Interest expense on Senior Notes and Term Loan	**4,592**	5,820
Refinancing expense – warrants (Note 6)	**737**	-
Refinancing expense – legal, advisory and professional fees on the Term Loan (Note 6)	**962**	-
Amortization of transaction costs	**371**	443
Accretion expense on Senior Notes	**288**	341
Accretion expense on provisions	**803**	870
Total finance costs	**7,874**	7,805

12. COMPENSATION COSTS AND KEY MANAGEMENT PERSONNEL EXPENSES

Total wages, salaries, benefits, severances, and other personnel costs included in comprehensive loss for the year ended December 31, 2018 were $2,873 (2017 - $2,968).

The aggregate expense of key management personnel, defined as the Company's Chief Executive Officer, Executive Vice President, Chief Financial Officer, Interim Chief Financial Officer and the Company's Board of Directors, was as follows:

	Year ended December 31, 2018	2017
Wages, salaries, benefits and other personnel costs	**738**	906
Share-based payments (i)	**258**	532
Total remuneration	**996**	1,438

(i) Represents the total fair value of share-based payment awards granted to officers and directors in the year of grant, as determined using a Black-Scholes option pricing model (see note 16).

(All figures expressed in thousands except per share amounts unless otherwise noted)

13. PROVISIONS

Decommissioning liabilities

The following table summarizes the changes in decommissioning liabilities for the years ended December 31, 2018 and 2017:

	2018	2017
Balance, beginning of year	**38,478**	38,161
Property dispositions (Note 4)	**(2,149)**	(776)
Accretion expense	**803**	870
Liabilities incurred	**192**	371
Abandonment costs incurred	**(3,756)**	(1,079)
Revisions in estimated cash flows	**1,870**	(185)
Revisions due to change in discount rates	**117**	1,116
Balance, end of year	**35,555**	38,478
Current	**1,782**	1,466
Non-current	**33,773**	37,012
	35,555	38,478

The Company's decommissioning liabilities result from its ownership in oil and natural gas assets including well sites, facilities and gathering systems. The total estimated, undiscounted cash flows, inflated at 2 percent, required to settle the obligations are $55,390 (December 31, 2017 - $63,742). These cash flows have been discounted using a risk-free interest rate of 2.15 percent (December 31, 2017 – 2.20 percent) based on Government of Canada long-term benchmark bonds. The Company expects these obligations to be settled in approximately 1 to 50 years (December 31, 2017 – 1 to 50 years). As at December 31, 2018 and 2017, no funds have been set aside to settle these liabilities.

14. INCOME TAXES

The following table sets forth the components of the Company's deferred income tax asset:

	December 31, 2018	December 31, 2017
Excess of net book value of assets and liabilities over related tax pools	**(95,180)**	(97,137)
Non-capital loss carry-forwards	**85,774**	87,955
Scientific research and development expenses and investment tax credits	**9,056**	9,056
Other tax assets	**350**	126
Total net deferred income tax asset	**-**	-

(All figures expressed in thousands except per share amounts unless otherwise noted)

At December 31, 2018, Cequence has total tax pools of $608,780 (December 31, 2017 - $616,660) including non-capital loss carry-forwards, investment tax credit carry-forwards and Scientific Research and Experimental Development ("SRED") expenses available to reduce future years' income for tax purposes. Deferred income tax assets have been recognized to the extent that estimated future taxable profits are sufficient to realize the deferred income tax assets in the allowable timeframes. The ongoing period of low commodity prices has created uncertainty regarding the future realization of the Company's deferred tax assets. As a result, a deferred income tax asset of $106,309 has not been recognized (December 31, 2017 – $109,081). The SRED expenses of approximately $22,704 available for carry-forward do not expire (December 31, 2017 - $22,704). The non-capital loss carry-forwards expire in 6 to 20 years and the investment tax credit carry-forwards expire in 2 to 6 years.

Income tax expense differs from that which would be expected from applying the effective Canadian federal and provincial tax rates of 27 percent (2017 – 27 percent) to loss before income taxes as follows:

	Year ended December 31,	
	2018	2017
Expected income tax recovery	**(2,619)**	(26,828)
Effect of share-based payments	**81**	278
Change in previously estimated tax pools	**2,775**	(424)
Effect of renunciation of flow-through shares (Note 15)	**2,320**	-
Change in unrecorded deferred income tax asset	**(2,772)**	27,107
Other	**215**	(133)
Deferred income tax expense	**-**	-
Current income tax	**-**	-
Income tax expense	**-**	-

Movements in deferred income tax balances are as follows:

	Balance, Dec. 31, 2017	Recognized in comprehensive loss	Recognized in liabilities	Recognized in equity	Balance, Dec. 31, 2018
Property and equipment and provisions	(96,931)	**2,718**	**-**	**-**	**(94,213)**
Unrealized (gain) loss on financial instruments	(75)	**(892)**	**-**	**-**	**(967)**
Senior notes and term loan	(131)	**329**	**-**	**-**	**198**
Non-capital losses	87,955	**(2,181)**	**-**	**-**	**85,774**
SRED expenses and investment tax credits	9,056	**-**	**-**	**-**	**9,056**
Other	126	**26**	**-**	**-**	**152**
Total	-	**-**	**-**	**-**	**-**

	Balance, Dec. 31, 2016	Recognized in comprehensive loss	Recognized in liabilities	Recognized in equity	Balance, Dec. 31, 2017
Property and equipment and provisions	(90,959)	(5,972)	-	-	(96,931)
Unrealized (gain) loss on financial instruments	1,255	(1,330)	-	-	(75)
Senior notes	(190)	59	-	-	(131)
Non-capital losses	80,456	7,499	-	-	87,955
SRED expenses and investment tax credits	9,056	-	-	-	9,056
Other	382	(256)	-	-	126
Total	-	-	-	-	-

15. SHARE CAPITAL

Cequence has an unlimited number of common voting shares and common non-voting shares with no par value authorized.

On October 22, 2018, the Company's shareholders approved a share consolidation on the basis of one post-consolidation common share for every 20 pre-consolidation common shares. These consolidated financial statements and all information relating to issued and outstanding common shares, stock options, warrants and restricted share units, have been restated to reflect the share consolidation for all periods presented.

	Year ended December 31, 2018		Year ended December 31, 2017	
Issued common voting shares	**Number (000's)**	**Stated Value $**	Number (000's)	Stated Value $
Balance, beginning of year	**12,277**	**633,846**	12,277	633,848
Flow-through common shares	**12,276**	**8,593**	-	-
	24,553	**642,439**	12,277	633,848
Share issue costs	**-**	**(316)**	-	(2)
Balance, end of year	**24,553**	**642,123**	12,277	633,846
Warrants				
Balance, beginning of year	**150**	**1,300**	150	1,300
Granted on refinancing of Senior Notes	**1,841**	**737**	-	-
Expired	**(150)**	**(1,300)**	-	-
Balance, end of year	**1,841**	**737**	150	1,300

On July 27, 2018, Cequence filed a Rights Offering Circular for holders of common shares on August 9, 2018 (the "record date") to subscribe for up to 12,276,394 common shares (245,527,883 pre-consolidation common shares) on a Canadian development expenses ("CDE") "flow-through" basis at a price of $0.70 per share ($0.035 per share pre-consolidation) (the "Rights Offering) for gross proceeds of up to $8,593. The Rights Offering was fully subscribed for and closed on September 13, 2018.

(All figures expressed in thousands except per share amounts unless otherwise noted)

An obligation related to flow-through shares has not been recorded as the flow-through shares were not issued at a premium to the fair value of the Company's common shares. In accordance with the terms of the agreement and pursuant to certain provisions of the Income Tax Act (Canada), the Company is required to incur on a best efforts basis and renounce to the holders of the flow-through common shares, for income tax purposes, development expenditures of $8,593 prior to December 31, 2018. The Company has until December 31, 2019 to incur the development expenditures. As at December 31, 2018, the Company has incurred $8,593 in development expenditures.

16. SHARE-BASED PAYMENT PLANS

Stock options

The Company has a stock option plan for directors, officers, employees and consultants of the Company and its subsidiaries. The number of common shares granted with respect to options may not exceed a rolling maximum of 10 percent of the Company's outstanding common shares. Options typically vest over a three year period, expire five years from the date of grant and are settled by issuing shares of the Company.

During the year ended December 31, 2018, the Company issued 980 stock options (2017 – 251) at an exercise price of $0.72 (2017 - $6.40) to employees, officers and directors. The options have a five year life and one third vest annually commencing one year following the grant date.

A summary of the inputs used to value stock options is as follows:

	2018	2017
Risk-free interest rate	**2.27%**	1.12%
Expected life of options	**5 years**	5 years
Expected volatility	**77%**	60%
Expected dividend rate	**0%**	0%
Expected forfeiture rate	**10%**	15%
Weighted average fair value	**$0.48**	$3.40

Expected volatility is determined based on the historical volatility of the Company's shares.

A summary of the status of the Company's stock option plan and changes during the years ended December 31, 2018 and 2017 is as follows:

	2018		2017	
	Number of Options (000's)	**Weighted Average Exercise Price $**	Number of Options (000's)	Weighted Average Exercise Price $
Outstanding, beginning of year	**661**	**11.22**	550	17.11
Granted	**980**	**0.72**	251	6.40
Cancelled/Forfeited	**(112)**	**9.12**	(5)	26.60
Expired	**(53)**	**33.61**	(135)	25.61
Outstanding, end of year	**1,476**	**3.61**	661	11.22

(All figures expressed in thousands except per share amounts unless otherwise noted)

The following table summarizes information about stock options outstanding at December 31, 2018:

Options Outstanding			Options Exercisable	
Exercise Price $	Number of Options (000's)	Contractual Life Remaining (years)	Number of Options (000's)	Exercise Price $
0.72	980	4.89	-	-
5.80	22	2.74	15	5.80
6.40	204	3.06	68	6.40
6.60	212	2.53	142	6.60
16.20	28	1.44	28	16.20
44.40	30	0.64	30	44.40
	1,476	4.11	283	11.46

During the year ended December 31, 2018, $344 (2017 - $991) in share-based payment expense related to equity-settled stock options has been recognized in comprehensive loss.

Restricted Share Units

The Company has a RSU plan for directors, officers, employees and consultants of the Company and its subsidiaries. An RSU is a conditional grant to receive a Cequence common share, or the cash equivalent, as determined by the Company, upon vesting of the RSUs and in accordance with the terms of the RSU plan and grant agreement. The value of one RSU is notionally equivalent to one Cequence common share. RSUs vest over a three year period and management plans to settle the RSUs in cash on the respective vesting date.

A summary of the status of the Company's RSU plan and changes for the years ended December 31, 2018 and 2017 is as follows:

Number of RSUs (000's)	**2018**	2017
Outstanding, beginning of year	**133**	150
Granted	**393**	35
Cancelled/Forfeited	**(19)**	(1)
Settled	**(63)**	(51)
Outstanding, end of year	**444**	133

During the year ended December 31, 2018, the Company recognized ($44) (2017 - $37) in share-based payment expense related to the cash-settled RSUs in comprehensive loss.

17. LOSS PER SHARE

Loss per share has been calculated based on the weighted average number of common shares outstanding during the period and reflects the share consolidation as described in more detail in Note 15. For the years ended December 31, 2018 and 2017, the Company has excluded all dilutive instruments as their inclusion would be anti-dilutive. The following table reconciles the denominators used for the basic and diluted loss per share calculations:

(All figures expressed in thousands except per share amounts unless otherwise noted)

	Year ended December 31, 2018	2017
Basic weighted average shares	**15,942**	12,277
Effect of dilutive instruments	**-**	-
Diluted weighted average shares	**15,942**	12,277

18. COMMITMENTS

	2019	2020	2021	2022	2023+	Total
Office leases	262	-	-	-	-	262
Pipeline transportation	6,535	6,535	6,535	6,118	26,016	51,739
Gas processing	4,154	4,166	4,154	4,154	30,471	47,099
Total	10,951	10,701	10,689	10,272	56,487	99,100

Cequence has a take or pay agreement with the operator of the Simonette facility. The volume commitment under the take or pay is 42 mmcf/d until April 30, 2030.

The Company has firm transportation on a major pipeline system for 35 mmcf/d for the period December 17, 2017 to March 30, 2026.

The Company has a contract to ship 10,850 GJ/d of natural gas on the TransCanada mainline system from the Empress receipt point to the Dawn hub in Ontario subject to regulatory approval with the National Energy Board and financial assurances. The term of the contract began on April 1, 2018, is 10 years in duration and has early termination rights that can be exercised following the initial five years of service. The toll for this service is $0.77 per GJ/d. As part of this commitment, the Company entered into a five year contract to transport AECO gas to Empress at an annual cost of approximately $750.

During the year ended December 31, 2018, the Company recognized $264 (2017 – $250) of expense related to office leases, included with general and administrative expense.

19. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT

The Company’s financial instruments, including derivative financial instruments, recognized in the consolidated balance sheets consist of cash, accounts receivable, deposits, commodity contracts, demand credit facilities, Senior Notes, Term Loan and accounts payable and accrued liabilities.

The Company's cash, accounts receivable, deposits, demand credit facilities and accounts payable and accrued liabilities approximate their carrying values due to their short terms to maturity and the floating interest rate on the Company's debt. The Senior Notes and Term Loan bear interest at rates available to Cequence and accordingly the fair value approximates the carrying value excluding deferred financing costs.

The Company’s fair value hierarchy for those assets and liabilities measured at fair value comprises cash measured at level 1 and commodity contracts measured at level 2 under the Company’s fair value hierarchy as of December 31, 2018. The fair value of commodity contracts is determined by discounting the remaining contracted petroleum and natural gas volumes by the difference between the contracted price and published forward price curves as at the balance sheet date.

(All figures expressed in thousands except per share amounts unless otherwise noted)

The nature of these financial instruments and the Company's operations expose the Company to market risk, credit risk and liquidity risk. The Company manages its exposure to these risks by operating in a manner that minimizes these risks. Senior management employs risk management strategies and policies to ensure that any exposure to risk is in compliance with the Company's business objectives and risk tolerance levels. The Board of Directors has overall responsibility for the establishment and oversight of the Company's risk management framework. The Board has established policies in setting risk limits and controls and monitors these risks in relation to market conditions.

MARKET RISK

Market risk is the risk that changes in market prices, such as foreign exchange rates, commodity prices, and interest rates will affect the Company's comprehensive loss to the extent the Company has outstanding financial instruments. The objective of the Company is to mitigate market risk exposures within acceptable limits, while maximizing returns.

Commodity price risk

The nature of the Company's operations results in exposure to fluctuations in commodity prices. Management continuously monitors commodity prices and initiates instruments to manage exposure to these risks when it deems appropriate. As a means of managing commodity price volatility, the Company enters into various derivative financial instrument agreements and physical contracts. The fair values of the derivative financial instruments are based on mark-to-market assessments and estimates of fair value and are recorded on the consolidated balance sheet as either an asset or liability with the change in fair value recognized in comprehensive loss.

During the year ended December 31, 2018, the Company entered into several commodity derivative financial instrument contracts. The following information presents all outstanding positions for commodity derivative financial instruments at December 31, 2018:

Term	Product	Type	Volume	Price	Basis
January 1, 2019 to March 31, 2019	Gas	Swap	7,500 gj/day	$4.92	Dawn
April 1, 2019 to June 30, 2019	Gas	Swap	5,000 gj/day	$3.20	Dawn
July 1, 2019 to September 30, 2019	Gas	Swap	2,500 gj/day	$3.04	Dawn
January 1, 2019 to December 31, 2019	Oil	Swap	400 bbl/day	$85.29	WTI

For the year ended December 31, 2018, realized loss from commodity derivative contracts recognized in comprehensive loss were $1,275 (2017 - $4,812 gain).

The fair value of the commodity contracts outstanding at December 31, 2018 was a current asset of $3,580 (December 31, 2017 – current asset of $1,274 and current liability of $998).

For the year ended December 31, 2018, the Company recorded an unrealized gain of $3,303 from derivative commodity contracts (2017 - $4,927 unrealized gain).

As at December 31, 2018, a change in gas price of $0.50/gj and oil price of $1.00/bbl results in a change in the fair value of the commodity contracts of $680 and $146 (2017 - $563 and $109) respectively and a commensurate increase to comprehensive loss.

Subsequent to December 31, 2018, the Company entered into the following commodity derivative financial instrument contracts:

Term	Product	Type	Volume	Price	Basis
April 1, 2019 to October 31, 2019	Gas	Swap	5,000 gj/day	$1.37	AECO

(All figures expressed in thousands except per share amounts unless otherwise noted)

Foreign exchange risk

The Company is exposed to foreign currency fluctuations as crude oil and natural gas prices are referenced to U.S. dollar denominated prices. As at December 31, 2018, the Company had no forward, foreign exchange contracts in place, nor any significant working capital items denominated in foreign currencies (2017 – nil).

Interest rate risk

The Company is exposed to interest rate risk to the extent that changes in market interest rates impact its borrowings under the floating rate credit facilities. The floating rate debt is subject to interest rate cash flow risk, as the required cash flows to service the debt will fluctuate as a result of changes in market rates. The Company has no interest rate swaps or financial contracts in place as at or during the year ended December 31, 2018 (2017 - nil).

As at December 31, 2018, a 1 percent change in interest rates on the Company's outstanding credit facilities, with all other variables constant, would result in a change in comprehensive loss of $nil (2017 - $nil).

CREDIT RISK

Credit risk is the risk of financial loss to the Company if a counterparty to a financial instrument fails to meet its contractual obligation. The Company is exposed to credit risk with respect to its cash, accounts receivable and commodity contract assets.

The Company's cash and commodity contract assets is held with a large established financial institution. The majority of the Company's accounts receivable are due from marketers of the Company's petroleum and natural gas production which are typically collected on the 25th day of the month following the prior month's production and from joint venture partners in the oil and gas industry. The Company mitigates its credit risk by entering into contracts with established counterparties that have strong credit ratings and reviewing its exposure to individual counterparties on a regular basis.

As at December 31, 2018, the accounts receivable balance was $10,324 (December 31, 2017 - $14,739) of which $1,248 (December 31, 2017 - $956) was past due. The Company considers all amounts greater than 90 days past due. These past due accounts are considered to be collectible, except as provided in the allowance for doubtful accounts. When determining whether past due accounts are uncollectible, the Company factors in the past credit history of the counterparties. The following table provides an aging analysis of the Company's accounts receivables:

Current	30-60 days	60-90 days	90+days	Total
8,200	**545**	**331**	**1,248**	**10,324**

At December 31, 2018, the Company has an allowance for doubtful accounts of $760 (December 31, 2017 – $659). As at December 31, 2018, 34.7 percent (December 31, 2017 – 35.0) of the total receivables balance is due from marketers of the Company's oil and natural gas production. A reconciliation of the Company's allowance for doubtful accounts is as follows:

	Year ended December 31,	
	2018	2017
Balance, beginning of year	**659**	647
Amounts collected	**3**	(78)
Additional provision	**98**	90
Balance, end of year	**760**	659

(All figures expressed in thousands except per share amounts unless otherwise noted)

As at December 31, 2018, the maximum exposure to credit risk was $28,400 (December 31, 2017 - $26,984) being the carrying value of the Company's cash, accounts receivable and commodity contract assets.

LIQUIDITY RISK

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they are due. The nature of the oil and gas industry is capital intensive and the Company maintains and monitors a certain level of cash flow to finance operating and capital expenditures. Refer to note 21 for disclosure related to the management of capital.

The expected timing of cash flows relating to financial liabilities as at December 31, 2018 is as follows:

	< 1 Year	1 – 2 Years	2 – 5 Years	Thereafter
Term Loan	-	-	60,000	-
Accounts payable and accrued liabilities	35,736	-	-	-
	35,736	-	60,000	-

20. CHANGES IN NON-CASH WORKING CAPITAL

	Year ended December 31, **2018**	2017
Accounts receivable	**4,415**	(594)
Deposits and prepaid expenses	**(119)**	363
Accounts payable and accrued liabilities	**2,630**	(3,018)
Net change in non-cash working capital	**6,926**	(3,249)
Allocated to:		
Operating activities	**2,427**	1,634
Investing activities	**4,499**	(4,883)
	6,926	(3,249)

21. CAPITAL MANAGEMENT

Cequence's objectives are to maintain a flexible capital structure in order to meet its financial obligations, execute on strategic opportunities throughout the business cycle and respond to changes in economic conditions. The Company's capital comprises shareholders' equity, demand credit facilities, Term Loan and working capital. Cequence manages the capital structure and makes adjustments in light of economic conditions and the risk characteristics of the underlying assets.

In order to maintain or adjust the capital structure, Cequence may issue new common shares, issue new debt or replace existing debt, adjust capital expenditures and acquire or dispose of assets. The Company evaluates its capital structure based on net debt to cash flow from operating activities and the current credit available to Cequence compared to its budgeted capital expenditures.

At December 31, 2018, Cequence has a $60,000 Term Loan due on October 3, 2022 and a $7,000 Credit Facility that has a term date of May 31, 2019. The Company has letters of credit outstanding of $1,590. The Company's Credit Facility is based on the lenders' review of the Company's oil and natural gas reserves with the next scheduled review expected to be completed in May 2019. The Credit Facility has a covenant that requires Senior Debt to twelve month trailing EBITDA, as defined in the bank agreement, to be less than 3:0 to 1:0. The Company was in compliance with the lender's covenant at December 31, 2018 with a ratio of 0.1 times (December 31, 2017 – 0.1 times).

The Company continues to review its options to improve its financial leverage including alternative financing arrangements, property acquisitions or divestitures, corporate mergers and acquisitions, other recapitalization opportunities, further adjustments to the capital program, use of risk management contracts or the issuance of additional equity.