# CANACOL ENERGY LTD.

**CONSOLIDATED FINANCIAL STATEMENTS**
**YEAR ENDED DECMBER 31, 2019**

## Management's Report

Management is responsible for the accuracy, integrity and objectivity of the consolidated financial statements of Canacol Energy Ltd. (the "Corporation") within reasonable limits of materiality. The accompanying consolidated financial statements have been prepared by management in accordance with International Financial Reporting Standards and, where appropriate, reflect management's best estimates and judgements. The accompanying consolidated financial statements have been prepared using policies and procedures established by management and fairly reflect the Corporation's financial position, financial performance and cash flows, in accordance with International Financial Reporting Standards. Management has established and maintains a system of internal controls that is designed to provide reasonable assurance that assets are safeguarded from loss or unauthorized use and the financial information is reliable and accurate.

The Corporation's external auditors, KPMG LLP, have audited the consolidated financial statements for the year ended December 31, 2019. Their audit included such tests and procedures, as they considered necessary, to provide reasonable assurance that the financial statements are presented fairly in accordance with International Financial Reporting Standards. The consolidated financial statements for the year ended December 31, 2018 were audited by the Corporation's former external auditors, Deloitte LLP.

The Audit Committee of the Board of Directors has reviewed in detail the consolidated financial statements with management and the external auditors. The Audit Committee has reported its findings to the Board of Directors who have approved the consolidated financial statements.

*(signed) "Charle Gamba"*
Charle Gamba
President and Chief Executive Officer

*(signed) "Jason Bednar"*
Jason Bednar
Chief Financial Officer

March 17, 2020

KPMG

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# INDEPENDENT AUDITORS' REPORT

To the Shareholders of Canacol Energy Ltd.

***Opinion***

We have audited the consolidated financial statements of Canacol Energy Ltd. (the "Company"), which comprise:

- the consolidated statement of financial position as at December 31, 2019;
- the consolidated statement of operations and comprehensive income (loss) for the year then ended;
- the consolidated statement of changes in equity for the year then ended;
- the consolidated statement of cash flows for the year then ended;
- and notes to the consolidated financial statements, including a summary of significant accounting policies.

(Hereinafter referred to as the "financial statements").

In our opinion, the accompanying financial statements present fairly, in all material respects, the consolidated financial position of the Company as at December 31, 2019 and its consolidated financial performance and its consolidated cash flows for the year 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. Our responsibilities under those standards are further described in the "*Auditors' Responsibilities for the Audit of the Financial Statements*" section of our auditors' 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.

***Emphasis of Matter – Modified Retrospective Change in Accounting Policy***

We draw attention to Note 3 to the financial statements which indicates that the Company has changed its accounting policy for leases and has applied that change on a modified retrospective basis.

Our opinion is not modified in respect of this matter.

***Other Matter – Comparative Information***

The financial statements for the year ended December 31, 2018 were audited by another auditor who expressed an unmodified opinion on those financial statements on March 21, 2019.

***Other Information***

Management is responsible for the other information. Other information comprises the information included in Management's Discussion and Analysis filed with the relevant securities commission.

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 and remain alert for indications that the other information appears to be materially misstated.

We obtained the information included in Management's Discussion and Analysis filed with the relevant Canadian Securities Commissions as at the date of this auditors' report. If, based on the work we have performed on this other information, we conclude that there is a material misstatement of this other information, we are required to report that fact in the auditors' report.

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 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.

***Auditors' 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 auditors' report that includes our opinion.

Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with Canadian generally accepted auditing standards will always detect a material misstatement when it exists.

Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of the 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 Company's internal control.

- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.

- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Company's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditors' report to the related disclosures in the financial statements or, if such disclosures are inadequate, KPMG

to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditors' report. However, future events or conditions may cause the Company to cease to continue as a going concern.

- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represents the underlying transactions and events in a manner that achieves fair presentation.
- 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.
- Provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the group Company to express an opinion on the financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

The engagement partner on the audit resulting in this auditors' report is Reinier Deurwaarder.

KPMG LLP

Chartered Professional Accountants

Calgary, Canada
March 17, 2020

## CONSOLIDATED STATEMENTS OF FINANCIAL POSITION

*(in thousands of United States dollars)*

| As at | Note | December 31, 2019 | December 31, 2018 |
|---|---|---|---|
| **ASSETS** | | | |
| **Current assets** | | | |
| Cash and cash equivalents | | **$ 41,239** | $ 51,632 |
| Trade and other receivables | 23 | **69,608** | 62,244 |
| Tax installments and receivables | | **9,533** | 5,966 |
| Assets held for sale | 6 | **7,960** | — |
| Other current assets | 7 | **4,930** | 4,897 |
| | | **133,270** | 124,739 |
| **Non-current assets** | | | |
| Trade and other receivables | 23 | **5,629** | — |
| Exploration and evaluation assets | 4 | **53,867** | 39,555 |
| Property, plant and equipment | 5 | **506,097** | 480,428 |
| Deferred tax assets | 17 | **49,176** | 55,335 |
| Other non-current assets | 7 | **6,023** | 4,946 |
| | | **620,792** | 580,264 |
| **Total assets** | | **$ 754,062** | $ 705,003 |
| **LIABILITIES AND EQUITY** | | | |
| **Current liabilities** | | | |
| Current portion of long-term debt | 10 | **$ 8,182** | $ — |
| Trade and other payables | | **52,591** | 49,279 |
| Lease obligations | 12 | **4,731** | 1,701 |
| Taxes payable | | **6,043** | 6,313 |
| Liabilities held for sale | 6 | **10,591** | — |
| Decommissioning obligations | 11 | **—** | 840 |
| Other current liabilities | 8 | **15,675** | 11,125 |
| | | **97,813** | 69,258 |
| **Non-current liabilities** | | | |
| Long-term debt | 10 | **333,403** | 339,684 |
| Lease obligations | 12 | **22,367** | 19,772 |
| Decommissioning obligations | 11 | **16,398** | 22,850 |
| Deferred tax liabilities | 17 | **24,559** | 32,289 |
| Other non-current liabilities | 8 | **16,776** | 15,713 |
| **Total liabilities** | | **511,316** | 499,566 |
| **Equity** | | | |
| Share capital | 9 | **169,459** | 159,116 |
| Other reserves | | **68,067** | 67,821 |
| Accumulated other comprehensive income | | **335** | 335 |
| Retained earnings (deficit) | 9 | **4,885** | (21,835) |
| **Total equity** | | **242,746** | 205,437 |
| **Total liabilities and equity** | | **$ 754,062** | $ 705,003 |

Commitments and contingencies (note 24)
See accompanying notes to the consolidated financial statements.

**Approved by the Board of Directors**

*(signed) "Michael Hibberd"*
Director

*(signed) "Francisco Diaz"*
Director

## CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE INCOME (LOSS)

*(in thousands of United States dollars, except per share amounts)*

| Year ended December 31, | Note | | 2019 | | 2018 |
|---|---|---|---|---|---|
| **Revenues** | | | | | |
| Natural gas and crude oil revenues, net of royalties | 19 | $ | 240,841 | $ | 219,419 |
| Take-or-pay natural gas income | 19 | | 1,238 | | 2,994 |
| **Total natural gas and crude oil revenues, net of royalties** | | | 242,079 | | 222,413 |
| **Expenses** | | | | | |
| Operating expenses | | | 17,138 | | 28,896 |
| Transportation expenses | | | 22,557 | | 18,262 |
| Pre-license costs and exploration expense | 4 | | 2,973 | | 13,674 |
| General and administrative | | | 28,973 | | 28,195 |
| Stock-based compensation and restricted share units expense | 8, 9 | | 7,921 | | 8,476 |
| Depletion and depreciation | 5 | | 54,283 | | 44,246 |
| Other expenses | 13 | | 10,598 | | 21,474 |
| Loss on settlement of long-term debt | 10 | | — | | 14,417 |
| Impairment recovery | | | — | | (19,126) |
| Settlement expense | 8 | | — | | 20,258 |
| | | | 144,443 | | 178,772 |
| Net finance expense | 14 | | 32,902 | | 34,539 |
| **Income before income taxes** | | | 64,734 | | 9,102 |
| **Income tax expense (recovery)** | | | | | |
| Current | 17 | | 32,058 | | 23,587 |
| Deferred | 17 | | (1,571) | | 7,350 |
| | | | 30,487 | | 30,937 |
| **Net income (loss) and comprehensive income (loss)** | | $ | 34,247 | $ | (21,835) |
| **Net income (loss) per share** | | | | | |
| Basic and diluted | 15 | $ | 0.19 | $ | (0.12) |

See accompanying notes to the consolidated financial statements.

## CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY

*(in thousands of United States dollars)*

| | Share Capital | Other Reserves | Accumulated Other Comprehensive Income | Retained Earnings (Deficit) | Non-Controlling Interest | Total Equity |
|---|---|---|---|---|---|---|
| Balance at December 31, 2017 | $ 707,125 | $ 65,547 | $ 335 | $ (533,847) | $ (18) | $ 239,142 |
| Transfer of deficit to share capital (note 9) | (533,847) | — | — | 533,847 | — | — |
| Distribution of share capital | (20,000) | — | — | — | — | (20,000) |
| Common share repurchases | (1,037) | — | — | — | — | (1,037) |
| Stock options exercised | 6,875 | (2,660) | — | — | — | 4,215 |
| Stock-based compensation | — | 4,934 | — | — | — | 4,934 |
| Sale of non-controlling interest | — | — | — | — | 18 | 18 |
| Net loss | — | — | — | (21,835) | — | (21,835) |
| **Balance at December 31, 2018** | **$ 159,116** | **$ 67,821** | **$ 335** | **$ (21,835)** | **$ —** | **$ 205,437** |
| Balance at January 1, 2019 (note 3) | $ 159,116 | $ 67,821 | $ 335 | $ (22,264) | $ — | $ 205,008 |
| Common share repurchases | (1,443) | — | — | — | — | (1,443) |
| Stock options exercised | 11,786 | (3,152) | — | — | — | 8,634 |
| Stock-based compensation | — | 3,398 | — | — | — | 3,398 |
| Dividends paid (note 16) | — | — | — | (7,098) | — | (7,098) |
| Net income | — | — | — | 34,247 | — | 34,247 |
| **Balance at December 31, 2019** | **$ 169,459** | **$ 68,067** | **$ 335** | **$ 4,885** | **$ —** | **$ 242,746** |

See accompanying notes to the consolidated financial statements.

## CONSOLIDATED STATEMENTS OF CASH FLOWS

*(in thousands of United States dollars)*

| Year ended December 31, | Note | 2019 | 2018 |
|---|---|---|---|
| **Operating activities** | | | |
| Net income (loss) and comprehensive income (loss) | | $ 34,247 | $ (21,835) |
| Non-cash adjustments: | | | |
| Depletion and depreciation | 5 | 54,283 | 44,246 |
| Stock-based compensation and restricted share units expense | 8, 9 | 7,921 | 8,476 |
| Net financing expense | 14 | 32,902 | 34,539 |
| Unrealized foreign exchange loss and other expenses | | 735 | 2,630 |
| Deferred income tax | 17 | (1,571) | 7,350 |
| Realized (gain) loss on financial instruments | 13 | — | 1,645 |
| Unrealized loss on financial instruments | 13 | 78 | 7,086 |
| Exploration impairment | 4 | — | 9,865 |
| Loss on settlement of long-term debt | 10 | — | 14,417 |
| Impairment recovery | 6 | — | (19,126) |
| Settlement expense | 8 | — | 20,258 |
| Other operating activities | 18 | (6,421) | (6,887) |
| Changes in non-cash working capital | 18 | (13,824) | (8,653) |
| | | 108,350 | 94,011 |
| **Investing activities** | | | |
| Expenditures on exploration and evaluation assets | 4 | (36,778) | (42,534) |
| Expenditures on property, plant and equipment | | (66,282) | (68,569) |
| Net proceeds on disposition of property, plant and equipment | 5 | 12,379 | 3,000 |
| Proceeds on assets and liabilities held for sale | 6 | — | 47,349 |
| Finance lease obligation settlement | 12 | — | (21,262) |
| Other investing activities | 18 | (390) | 32,895 |
| Changes in non-cash working capital | 18 | 6,807 | (26,400) |
| | | (84,264) | (75,521) |
| **Financing activities** | | | |
| Net financing expense paid | 14 | (29,505) | (30,982) |
| Lease principal payments | 12 | (5,067) | (6,885) |
| Dividends paid | 16 | (7,098) | — |
| Common share repurchases | 9 | (1,443) | (1,037) |
| Issue of common shares | 9 | 8,634 | 4,215 |
| Draw on long-term debt | 10 | — | 350,000 |
| Financing fees | 10 | — | (11,260) |
| Repayment of long-term debt | 10 | — | (305,000) |
| Prepayment penalty on settlement of long-term debt | 10 | — | (4,980) |
| | | (34,479) | (5,929) |
| Change in cash and cash equivalents | | (10,393) | 12,561 |
| Cash and cash equivalents, beginning of period | | 51,632 | 39,071 |
| **Cash and cash equivalents, end of period** | | $ 41,239 | $ 51,632 |

See accompanying notes to the consolidated financial statements.

## NOTE 1 - GENERAL INFORMATION

Canacol Energy Ltd. and its subsidiaries ("Canacol" or the "Corporation") are primarily engaged in natural gas exploration and development activities in Colombia. The Corporation's head office is located at 2650, 585 - 8th Avenue SW, Calgary, Alberta, T2P 1G1, Canada. The Corporation's shares are traded on the Toronto Stock Exchange ("TSX") under the symbol CNE, the OTCQX in the United States of America under the symbol CNNEF, the Bolsa de Valores de Colombia under the symbol CNEC and the Bolsa Mexicana de Valores under the symbol CNEN.

The Board of Directors approved these consolidated financial statements (the "financial statements") for issuance on March 17, 2020.

## NOTE 2 - BASIS OF PREPARATION

The financial statements have been prepared by management in accordance with the International Financial Reporting Standards ("IFRS").

**Basis of Measurement**

These financial statements have been prepared on a historical cost basis, except for certain financial instruments, restricted share units and hedging contract, which are measured at fair value with changes in fair value recorded in profit or loss ("fair value through profit or loss").

These financial statements have been prepared on a going concern basis.

**Functional and Presentation Currency**

These financial statements are presented in United States dollars, which is both the functional and presentation currency, with the exception of Canadian dollar unit prices ("C$") where indicated.

**Significant Estimates and Management Judgements**

The timely preparation of financial statements in accordance with IFRS requires that management make estimates, assumptions and use judgement regarding the measured amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Such estimates relate primarily to unsettled transactions and events as of the date of the financial statements. Accordingly, actual results may differ from estimated amounts as future confirming events occur. The following discussion relates to amounts determined by management which required significant estimation and/or judgement.

Management judgement is required in determining the functional currency that represents the economic effect of underlying transactions, events and conditions. The United States dollar is selected as the Corporation's functional currency as it is the currency of the primary economic environment in which the Corporation operates; the Corporation's revenues, funds from financing and the majority of its expenditures are denominated in United States dollars.

The Corporation holds an investment in a public company, Arrow Exploration Corp. ("Arrow"), of which two of the board of directors of Arrow are also key members of the Corporation's management. Management has used judgement in determining that the Corporation does not have significant influence over Arrow by considering the Corporation's voting rights and ownership interest of Arrow (note 7).

Significant management judgement is required in determining the provision for deferred income taxes. There are many transactions and calculations for which the ultimate tax determination is uncertain. The Corporation has not recognized a benefit for the net deferred tax asset created from a portion of its non-capital losses and capital losses carried forward due to the uncertainty of realization of such amounts.

The calculation of stock-based compensation expense is subject to uncertainty as it reflects the Corporation's best estimate of whether or not performance will be achieved and obligations incurred. In addition, the key assumptions used for stock-based compensation calculation are based on estimated volatility and estimated forfeiture rates for stock options that will not vest.

Natural gas and crude oil assets are grouped into cash generating units ("CGUs") identified as having largely independent cash flows and are geographically integrated. The determination of the CGUs was based on management's interpretation and judgement. The recoverability of development and production asset carrying values is assessed at the CGU level. The asset composition of a CGU can directly impact the recoverability of the assets included therein.

Amounts recorded for depletion, depreciation, amortization, accretion and provisions for decommissioning obligations are based on their expected lives and other relevant assumptions.

Indicators of impairment or impairment recovery are assessed by management using judgement, considering market conditions and commodity prices. In assessing the recoverability of oil and gas properties, each CGU's carrying value is compared to its recoverable amount, defined as the greater of its fair value less cost to sell and value in use.

In assessing the recoverable amount, the estimated future cash flows are discounted to their present value using a discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. The recoverable amount is generally computed by reference to the present value of the future cash flows expected to be derived from production of proved and probable reserves.

Key input estimates used in the determination of future cash flows from natural gas reserves include the following:

i) Reserves - Assumptions that are valid at the time of reserve estimation may change significantly when new information becomes available. Changes in forward price estimates, production costs or recovery rates may change the economic status of reserves and may ultimately result in reserves being revised.

ii) Commodity prices - Forward price estimates of the natural gas prices are used in the cash flow model. Commodity prices have fluctuated in recent years due to global and regional factors including supply and demand fundamentals, inventory levels, exchange rates, weather, economic and geopolitical factors; however a significant portion of the Corporation's natural gas production is sold based on firm priced contracts, which are not subject to management's estimate.

iii) Discount rate - The discount rate used to calculate the net present value of cash flows is based on estimates of an approximate industry peer group weighted average cost of capital. Changes in the general economic environment could result in significant changes to this estimate.

iv) Decommissioning obligation - The decommissioning obligation is determined based on management's best estimate for future costs for decommissioning activities at the end of the asset's useful life. The timing and amount of costs are subject to change based on local legal and regulatory requirements as well as market conditions.

## NOTE 3 - SIGNIFICANT ACCOUNTING POLICIES

**Principles of Consolidation**

Subsidiaries - Subsidiaries are entities controlled by the Corporation. Control exists when the Corporation is exposed, or has rights, to variable returns from its involvement with the subsidiary and has the ability to affect those returns through its power over the subsidiary. The financial statements of subsidiaries are included in the financial statements from the date that control commences until the date that control ceases.

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 up, equity instruments issued and liabilities incurred or assumed at the date of exchange. 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 the acquisition over the fair value of the identifiable assets acquired and liabilities and contingent liabilities assumed 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 immediately in profit or loss as a gain on acquisition. Acquisition related costs, other than share issue costs, are expensed as period costs in the consolidated statements of operations and comprehensive income (loss).

Jointly-controlled operations and jointly-controlled assets - The Corporation's operating activities involve jointly-controlled assets. The financial statements include the Corporation's share of these jointly-controlled assets and a proportionate share of the relevant revenue and related operating costs.

Joint ventures - The Corporation's investment in the Ecuador IPC was accounted for using the equity method whereby the investment is originally recognized at cost and the Corporation's share of the Ecuador IPC's net income or loss is included in the consolidated statements of operations and comprehensive income (loss). During the year ended December 31, 2018, the Corporation sold its equity investment in the Ecuador IPC (note 6).

Transactions eliminated on consolidation - Intercompany balances and transactions, and any unrealized income and expenses arising from intercompany transactions, are eliminated on consolidation.

**Foreign Currency**

The United States dollar is the functional currency of the Corporation and its subsidiaries. Monetary assets and liabilities denominated in foreign currencies are translated to United States dollars at the period-end exchange rate. Non-monetary assets, liabilities, revenues and expenses are translated at exchange rates at the transaction date. Foreign exchange gains or losses are recognized in the consolidated statements of operations and comprehensive income (loss).

**Financial Instruments**

Non-derivative financial instruments - Non-derivative financial instruments include cash and cash equivalents, restricted cash, trade and other receivables, investments, restricted share units, long-term debt, settlement liability, trade and other payables and other long-term obligations. Non-derivative financial instruments are initially recognized at fair value plus any directly attributable transaction costs, except for financial assets and liabilities at fair value through profit or loss whereby any directly attributable transaction costs are expensed as incurred. Subsequent to initial recognition, non-derivative financial instruments are measured as described below.

Cash and cash equivalents - Cash and cash equivalents is measured similar to other non-derivative financial instruments. Subsequent to initial recognition, this financial instrument is measured at amortized cost.

Restricted cash - Restricted cash relates to cash placed in trust to ensure the payment of its obligations pursuant to exploration, abandonment and credit agreements and as such is classified separately from cash and cash equivalents due to its restricted use. Subsequent to initial recognition, this financial instrument is measured at amortized cost.

Investments - Investments are recorded at fair value through profit or loss. Subsequent to initial recognition, this financial instrument is measured at fair value and changes therein are recognized in the consolidated statements of operations and comprehensive income (loss).

Long-term debt - Long-term debt is recorded at amortized cost, net of directly attributable transaction costs. Subsequent to initial recognition, the directly attributable transaction costs are amortized into the carrying value using the effective interest method over the term of the debt facility through the consolidated statements of operations and comprehensive income (loss).

Settlement liability - Settlement liability is a present legal obligation of the Corporation which is measured at the estimated settlement amount and is subject to accrued interest at 8.74% per annum. The interest and settlement liability is settled on a monthly basis.

Lease obligations - Lease obligations are obligations of the lessee to pay lease payments that consist of principal and interest components according to the lease agreement. Subsequent to initial recognition, the lease obligations are accreted using the interest rate implicit in the lease, if that rate can be readily determined or if not, the Corporation's incremental borrowing rate and is recorded as finance expense to the statement of operations and comprehensive income (loss).

Crude oil payable in kind - Crude oil payable in kind was recorded at fair value through profit or loss. Subsequent to initial recognition, these financial instruments were measured at fair value and changes therein were recognized in the consolidated statements of operations and comprehensive income (loss). During the year ended December 31, 2018, the Corporation sold its interest in certain petroleum assets and corresponding liabilities, resulting in the de-recognition of its crude oil payable in kind.

Other - Other non-derivative financial instruments, such as trade and other receivables, prepaid expenses, taxes receivable, trade and other payables, taxes payable and other long-term obligations are measured at amortized cost, less any impairment losses.

**Property, Plant and Equipment and Exploration and Evaluation Assets**

***Recognition and measurement***

Exploration and evaluation ("E&E") assets - E&E costs, including the costs of acquiring licenses, farming into or acquiring rights to working interest and directly attributable general and administrative costs, initially are capitalized either as tangible or intangible E&E assets according to the nature of the assets acquired. The costs are accumulated in cost centers by well, field or exploration area pending determination of technical feasibility and commercial viability.

When E&E assets are determined to be technically feasible and commercially viable (generally upon assignment of proved and probable reserves), the accumulated costs are transferred to property, plant and equipment ("PP&E"). When E&E assets are determined not to be technically feasible and commercially viable or the Corporation decides not to continue with its activity, the unrecoverable costs are charged to the consolidated statements of operations and comprehensive income (loss) as exploration costs.

E&E assets are allocated into CGUs and assessed for impairment when they are transferred to PP&E or in any circumstances where sufficient data exists to determine technical feasibility and commercial viability, and facts and circumstances suggest that the carrying amount exceeds the recoverable amount.

Development and production ("D&P") assets - Items of property, plant and equipment, which include natural gas and crude oil development and production assets, are measured at cost less accumulated depletion and depreciation and accumulated impairment losses. D&P assets are grouped into CGUs for impairment testing.

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

Gains and losses on disposal of an item of PP&E are determined by comparing the proceeds from disposal, net transaction costs with the carrying amount of PP&E and are recognized net within the consolidated statements of operations and comprehensive income (loss).

Subsequent costs - Costs incurred subsequent to the determination of technical feasibility and commercial viability and the costs of replacing parts of property, plant and equipment are recognized as PP&E only when they increase the future economic benefits embodied in the specific asset to which they relate. All other expenditures are recognized in the consolidated statements of operations and comprehensive income (loss) as incurred. Such capitalized PP&E generally represent costs incurred in developing proved and/or probable reserves and bringing in or enhancing production from such reserves. The carrying amount of any replaced or sold component is de-recognized. The costs of the day-to-day servicing of PP&E are recognized in the consolidated statements of operations and comprehensive income (loss) as incurred.

Depletion and depreciation - The net carrying value of D&P assets is depleted using the units-of-production method by reference to the ratio of production in the period to the related proved plus probable reserves, taking into account estimated future development costs necessary to bring those reserves into production. Future development costs are estimated by taking into account the level of development required to produce the reserves.

Proved and probable reserves are estimated using independent reserve engineer reports and represent the estimated quantities of natural gas, crude oil and natural gas liquids which geological, geophysical and engineering data demonstrate with a specified degree of certainty to be recoverable in future years from known reservoirs and which are considered commercially producible.

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

i) A reasonable assessment of the future economics of such production;

ii) A reasonable expectation that there is a market for all or substantially all the expected natural gas and crude oil production; and

iii) Evidence that the necessary production, transmission and transportation facilities are available or can be made available.

For other PP&E, depreciation is recognized in profit or loss on a straight-line basis over the estimated useful lives of each part of an item of the asset. Land is not depreciated.

The estimated useful lives for other assets for the current and comparative years are as follows:

| | |
|---|---|
| Equipment and other | 2 - 5 years |
| Right-of-Use assets | Over the term of the lease agreements |

Depreciation methods, useful lives and residual values are reviewed at each reporting date.

**Lease Obligations and Right-of-Use Assets**

The Corporation holds leases related to office leases, compressors and information technology equipment. The lease arrangements are assessed based on whether they meet the following definition of a lease under IFRS 16:

i) Identified asset - The Corporation has access to the use of a physically distinct asset and the counterparty does not hold the right to substitute an alternative asset for use;

ii) Right to direct the use of an asset - The Corporation has relevant operational decision-making rights for the use and purpose of the underlying asset; and

iii) Substantially all of the economic rights and benefits - The Corporation obtains sole and exclusive benefit from the use of the asset throughout the duration of the lease term.

Lease arrangements which meet the criteria of a lease are recognized as right-of-use assets and lease obligations at the lease commencement date.

The right-of-use asset is initially measured at cost. Subsequently, it is measured at cost less accumulated depreciation and impairment losses and adjusted for certain re-measurements of the lease obligation. The lease obligation is measured at the present value of the lease payments outstanding at the lease commencement date, discounted using the implicit rate, and when not determinable, the Corporation's incremental borrowing rate.

The lease obligation is re-measured when there is a change in estimated future payments arising from a change in a lease term, index or rate, residual guarantee or purchase option.

The Corporation has applied judgment and estimates when determining the estimated lease payments, including the lease term. The assessment of whether a renewal, extension, termination or purchase option is reasonably certain to be exercised was considered, based on facts and circumstances, and has the potential to significantly impact the amount of right-of-use asset and lease obligation recognized.

The Corporation holds a head lease for an office lease, which is sub-leased to a third party in return for monthly lease income. The Corporation accounts for the head lease and sub-lease arrangements as two separate contracts. The head lease is recognized as a lease obligation and the sub-lessee's share of the head lease is recognized as a net investment. The Corporation recognizes interest income received under finance leases over the lease term in the consolidated statements of operations using the effective interest rate method.

**Assets and Liabilities Held for Sale**

Assets and liabilities held for sale are recognized if the carrying value will be recovered principally through a sale transaction rather than continuing use. The assets and liabilities will be recognized at the lower of the carrying amount or the fair value less cost to sell and any impairment loss or recovery is recognized in the consolidated statements of operations and comprehensive income (loss).

**Impairment loss and recovery**

Financial assets - A financial asset is assessed at each reporting date for being credit-impaired or having significantly increased credit risk since initial recognition; if so determined, an estimated loss allowance is measured at an amount equal to the lifetime expected credit losses ("ECL"). Lifetime ECLs are a probability-weighted estimate of credit losses from all possible default events over the expected life of a financial asset. Credit losses are measured as the PV of all expected cash shortfalls relative to the carrying value of the financial asset. The ECLs are discounted at the effective interest rate.

The Corporation considers reasonable and supportable information that is relevant and available without undue cost or effort when determining credit impairment, significantly increased credit risk and any resulting ECLs. The financial asset is written off when the Corporation has determined the financial asset is credit-impaired with no reasonable expectations of recovering the financial asset in its entirety or a portion thereof.

Non-financial assets - The carrying amounts of the Corporation's non-financial assets, other than E&E assets and deferred income tax assets, are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists, then the recoverable amount of the asset is estimated. E&E assets are assessed for impairment when they are reclassified to PP&E, and also if facts and circumstances suggest that their carrying amount exceeds the recoverable amount. Deferred income tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realized.

For the purpose of impairment testing, assets are grouped together into the smallest group of assets that generates cash inflows from continuing use that are largely independent of the cash inflows of other assets or groups of assets. The recoverable amount of an asset or a CGU is the greater of its value in use and its fair value less costs to sell.

E&E assets are allocated to related CGUs when they are assessed for impairment, both at the time of any triggering facts and circumstances as well as upon their eventual reclassification to D&P assets.

An impairment loss is recognized if the carrying amount of an asset or its CGU exceeds its estimated recoverable amount. Impairment losses recognized in respect of CGUs are allocated first to reduce the carrying amount of any goodwill allocated to the units and then to reduce the carrying amounts of the other assets in the unit (group of units) on a pro-rata basis.

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

All impairment losses are recognized in the consolidated statements of operations and comprehensive income (loss).

**Provisions**

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

Decommissioning obligations - The Corporation's activities give rise to dismantling, decommissioning and site disturbance remediation activities. Provision is made for the estimated cost of site restoration and capitalized in the relevant asset category.

Decommissioning obligations are measured at the PV of management's best estimate of the expenditure required to settle the present obligation at the period-end date. Subsequent to initial measurement, the obligation 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 finance costs whereas increases or decreases due to changes in the estimated future cash flows are capitalized. Actual costs incurred upon settlement of the decommissioning obligations are charged against the provision to the extent the provision was established.

**Inventory**

Inventory consists of crude oil in transit or in storage tanks at the reporting date, and is valued at the lower of cost, using the weighted-average cost method, or net realizable value. Costs include direct and indirect expenditures including depletion and depreciation incurred in bringing the crude oil to its existing condition and location.

**Revenue**

The Corporation's revenues are primarily derived from the production of natural gas. Revenue from contracts with customers is recognized when the Corporation satisfies a performance obligation by physically transferring the product and control to a customer. The Corporation satisfies its performance obligations at the point of delivery of the product and not over a period of time. Revenue is measured based on the consideration specified in contracts with customers.

The Corporation recognizes take-or-pay natural gas income relating to the portion of natural gas sales nominations by the Corporation's off-takers that do not get delivered, typically due to the off-takers' inability to accept such gas when they have no recourse or legal right to delivery at a later date. Certain take-or-pay contracts grant the off-takers the legal right to take delivery at a later date, for a fixed period of time ("make-up rights"). These nominations are paid for at the time and are recorded as deferred income. The Corporation recognizes revenue associated with such make-up rights at the earliest of: a) when the make-up volume is delivered; b) when the make-up rights expires; or c) when it is determined that the likelihood of the off-taker will utilize the make-up right is remote.

Revenue is recorded net of any royalties when the amount of revenue can be reliably measured and the costs incurred in respect of the transaction can be measured reliably.

**Stock-Based Compensation**

The grant date fair value of stock options granted to officers, employees and directors is recognized as stock-based compensation expense with a corresponding increase in contributed surplus over the vesting period. A forfeiture rate is estimated on the grant date and is adjusted to reflect the actual number of awards that vest. The fair value of the stock options granted is estimated using the Black-Scholes option pricing model. Upon exercise of stock options, the fair value of the stock options are transferred from contributed surplus to share capital.

**Restricted Share Units**

The grant date fair value of restricted share units granted to officers, employees and directors is recognized as restricted share units expense with a corresponding increase in restricted share units liability over the vesting period. Subsequent to initial recognition, the restricted share units liability and expense is measured at fair value.

**Finance Income and Expense**s

Net finance income or expense is comprised of interest income, interest expense on borrowings and leases, amortization of upfront fees and accretion of the discount on decommissioning liabilities.

**Income Taxes**

Income tax expense comprises current and deferred income taxes. Income tax expense is recognized in the consolidated statements of operations and comprehensive income (loss) except to the extent that it relates to items recognized directly in equity, in which case it is recognized in equity.

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

Deferred income tax is recognized using the liability method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred income tax is not recognized on the initial recognition of assets or liabilities in a transaction that is not a business combination. In addition, deferred income tax is not recognized for taxable temporary differences arising on the initial recognition of goodwill. Deferred income tax is measured at the tax rates that are expected to be applied to temporary differences when they reverse, based on the laws that have been enacted or substantively enacted by the reporting date.

Deferred income tax assets and liabilities are offset if there is a legally enforceable right to offset, and they relate to income taxes levied by the same tax authority on the same taxable entity, or on different tax entities, but they intend to settle current tax liabilities and assets on a net basis or their tax assets and liabilities will be realized simultaneously.

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

**Net Income (Loss) per Share**

Basic net income (loss) per share is calculated by dividing the net income (loss) attributable to common shareholders of the Corporation by the weighted-average number of common shares outstanding during the period. Diluted net loss per share is determined by adjusting the weighted-average number of common shares outstanding during the period for the effects of dilutive instruments such as stock options.

**Reclassification of Prior Year Figures**

The Corporation has reclassified certain prior year figures in the consolidated statements of financial position, consolidated statements of operations and comprehensive income (loss) and the consolidated statements of cash flows for comparative purposes.

**Recent Accounting Pronouncements**

A number of accounting standards became effective on January 1, 2019, however they do not have a material impact on the financial statements, with the exception of IFRS 16 Leases ("IFRS 16") as described below.

On January 1, 2019, the Corporation adopted IFRS 16 to replace the existing guidance of IAS 17 Leases ("IAS 17"). IFRS 16 establishes principles and disclosures related to the amount, timing and uncertainty of cash flows arising from a lease arrangement and establishes a single definition of a lease arrangement rather than distinguish between an operating and finance lease. Under IFRS 16, lease arrangements, previously classified as operating leases under IAS 17, are potentially recognized on the consolidated statement of financial position as a right-of-use asset and corresponding lease obligation upon meeting the updated IFRS 16 criteria. IAS 17 criteria recognized a lease arrangement as a finance lease when substantially all of the risks and rewards of ownership of the underlying asset are transferred to the lessor; whereas IFRS 16 recognizes a finance lease based on the right to control the use of an identified asset.

The Corporation reviewed its lease arrangements to determine which of them meet the definition of a lease under IFRS 16 and the corresponding impact on the financial statements. For all lease arrangements determined to be a lease under IFRS 16, the Corporation has recognized a right-of-use asset of $5.9 million (note 5) and a lease obligation of $7.3 million (note 12) on the consolidated statements of financial position as at January 1, 2019.

Under IFRS 16, an intermediate lessor of an office lease accounts for the head lease and the sub-lease as two separate contracts. The intermediate lessor is required to classify the sub-lease as a finance or operating lease by reference of the right-of-use asset arising from the head lease. Upon transition to IFRS 16, the Corporation recognized $1.4 million of the total $7.3 million lease obligation (note 12) related to an office head lease and an office sub-lease was recognized as an investment of $1 million (note 7). The difference between the PV of the head lease payments and sub-lease receipts was adjusted to the opening retained earnings (deficit) balance as at January 1, 2019.

The Corporation has applied IFRS 16 using the modified retrospective approach, under which the cumulative effect of the initial adoption is recognized as at January 1, 2019 and does not impact comparative figures or retained earnings (deficit), with the exception of the difference between the PV of the head lease payments and sub-lease receipts. The Corporation has elected not to recognize right-of-use assets and lease obligations for low-value assets or short-term lease arrangements. The Corporation has recognized leases previously recorded as finance leases under IAS 17 at the carrying value of the finance lease asset and the finance lease obligation as at December 31, 2018.

*(in United States dollars (tabular amounts in thousands) except as otherwise noted)*

The contractual commitments disclosed as at December 31, 2018 recognized as lease obligations as at January 1, 2019 are as follows:

| **Office lease commitments** | | **December 31, 2018** |
|---|---|---|
| Office lease commitments - disclosed as at December 31, 2018 | $ | 3,104 |
| Adjustment for a head lease and a sub-lease reported as separate contracts[1] | | 1,180 |
| Adjustment for reasonably certain renewal terms and consumer price index | | 1,381 |
| **Adjusted office lease commitments - undiscounted basis** | **$** | **5,665** |

[1] As at December 31, 2018, the Corporation's office head lease commitments were disclosed net of a sub-lease contract

| **IFRS 16 adoption** | | **January 1, 2019** |
|---|---|---|
| Adjusted office lease commitments - undiscounted basis | $ | 5,665 |
| Adjustment for discounting the office lease commitments at 6.875% | | (576) |
| Adjusted office lease commitments - discounted basis | | 5,089 |
| Other lease obligations[1] - discounted basis | | 2,224 |
| **Total lease obligations - discounted basis (note 12)** | **$** | **7,313** |

[1] Other lease obligations recognized as at January 1, 2019 relate to operational and information technology equipment

## NOTE 4 – EXPLORATION AND EVALUATION ASSETS

| | | |
|---|---|---|
| Balance at December 31, 2017 | $ | 43,867 |
| Additions | | 42,534 |
| Exploration impairment | | (9,865) |
| Transferred to D&P assets (note 5) | | (36,981) |
| Balance at December 31, 2018 | | 39,555 |
| Additions | | 36,778 |
| Transferred to D&P assets (note 5) | | (22,466) |
| **Balance at December 31, 2019** | **$** | **53,867** |

During the year ended December 31, 2018, the Corporation made natural gas discoveries, Breva-1 on its VIM-21 block, Pandereta-3 and Chirimia-1 on its VIM-5 block and Cañahuate-2 and Cañahuate-3 on its Esperanza block and, accordingly, $37 million of exploration costs associated with such discoveries have been transferred to D&P assets.

During the year ended December 31, 2018, the Corporation assessed its exploration blocks for impairment and, as a result of relinquishment of a block, all costs associated with such block have been written off to exploration impairment. In addition to the $9.9 million of relinquishment related costs, $3.8 million of pre-license costs were also included in pre-license costs and exploration impairment for the year ended December 31, 2018. During the year ended December 31, 2019, there were no indicators of impairment.

During the year ended December 31, 2019 the Corporation made natural gas discoveries, Acordeon-1 and Ocarina-1 on its VIM-5 block and Arandala-1 on its VIM-21 block and, accordingly, $22.5 million of exploration costs associated with such discoveries have been transferred to D&P assets.

*(in United States dollars (tabular amounts in thousands) except as otherwise noted)*

## NOTE 5 – PROPERTY, PLANT AND EQUIPMENT

| | | Property, Plant and Equipment | | Right-of-Use Leased Assets [1] | | Total |
|---|---|---|---|---|---|---|
| **Cost** | | | | | | |
| Balance at December 31, 2017 | $ | 865,716 | $ | 8,940 | $ | 874,656 |
| Additions | | 74,296 | | 13,761 | | 88,057 |
| Dispositions | | (3,000) | | — | | (3,000) |
| Transferred from E&E (note 4) | | 36,981 | | — | | 36,981 |
| Balance at December 31, 2018 | | 973,993 | | 22,701 | | 996,694 |
| Adoption of IFRS 16 (note 3) | | — | | 5,877 | | 5,877 |
| Additions | | 70,088 | | 4,285 | | 74,373 |
| Transferred to assets held for sale (note 6) | | (16,281) | | — | | (16,281) |
| Transferred from E&E assets (note 4) | | 22,466 | | — | | 22,466 |
| Dispositions and de-recognition | | (15,176) | | (1,365) | | (16,541) |
| **Balance at December 31, 2019** | **$** | **1,035,090** | **$** | **31,498** | **$** | **1,066,588** |
| **Accumulated depletion and depreciation** | | | | | | |
| Balance at December 31, 2017 | $ | (491,226) | $ | (74) | $ | (491,300) |
| Depletion and depreciation | | (43,553) | | (693) | | (44,246) |
| Impairment recovery | | 19,126 | | — | | 19,126 |
| Derecognition and inventory adjustments | | 154 | | — | | 154 |
| Balance at December 31, 2018 | | (515,499) | | (767) | | (516,266) |
| Dispositions | | 1,225 | | — | | 1,225 |
| Depletion and depreciation | | (49,997) | | (4,286) | | (54,283) |
| Transferred to assets held for sale (note 6) | | 8,321 | | — | | 8,321 |
| Derecognition and inventory adjustments | | 20 | | 492 | | 512 |
| **Balance at December 31, 2019** | **$** | **(555,930)** | **$** | **(4,561)** | **$** | **(560,491)** |
| **Carrying value** | | | | | | |
| As at December 31, 2017 | $ | 374,490 | $ | 8,866 | $ | 383,356 |
| As at December 31, 2018 | $ | 458,494 | $ | 21,934 | $ | 480,428 |
| **As at December 31, 2019** | **$** | **479,160** | **$** | **26,937** | **$** | **506,097** |

[1] Prior to January 1, 2019, the Right-of-Use Asset related to a capital lease under IAS 17 (note 3).

During the year ended December 31, 2018, the Corporation purchased the Jobo 2 gas processing facility ("Jobo 2"), which had a finance lease obligation carrying value of $21.3 million, for a purchase price of $24.2 million, resulting in $3 million being capitalized to the Jobo 2 asset carrying value (note 12).

During the year ended December 31, 2018, an impairment recovery of $19.1 million was recorded based on the estimated recoverable amount of the Rancho Hermoso block (CGU) with an estimated decommissioning obligation of $10.2 million, resulting in a net recoverable amount of $8.9 million. The recoverable amount estimate at the time of revaluation, was based on the fair value less cost of disposal using discounted cash flows, as estimated by the management, an after-tax discount rate of 15% and the following forward West Texas Intermediate crude oil price per barrel of oil ("bbl") estimates: 2018 - $67.04/bbl, 2019 - $65.83/bbl, 2020 - $67.65/bbl, 2021 - $69.38/bbl, 2022 - $71.77/bbl and an increase of 2% per year thereafter. The recoverable amount of the Rancho Hermoso block was estimated using the fair value less cost of disposal and is considered Level 3, as defined in note 23. Such recovery was primarily a result of increased market participant interest in acquiring the block and the recovery in benchmark crude oil prices during the year ended December 31, 2018. The Corporation's other CGUs were unaffected.

During the year ended December 31, 2018, the Corporation sold its gas plant on its Rancho Hermoso block for proceeds of $3 million which was equal to the carrying value of the asset.

The Corporation began depleting its Jobo 3 natural gas processing facility ("Jobo 3") during the year ended December 31, 2019. The liquefied natural gas plant has not yet commenced full capacity operation; consequently, the carrying amount of $20.9 million is not yet being depleted as at December 31, 2019.

As a result of the Corporation's recent expansion of its natural gas processing and transportation systems, including the completion of Jobo 3, the Corporation has reassessed its CGU structure during the year ended December 31, 2019. Since the Corporation's cash flows are generated through common processing and transportation systems rather than at the individual block or field level, it was determined that an aggregate natural gas CGU is more appropriate than individual block level CGUs. The Corporation has assessed its individual block level CGUs for impairment prior to consolidating such CGUs and determined there was no impairment.

Due to the adoption of IFRS 16, the Corporation recognized right-of-use leased assets of $5.9 million as at January 1, 2019, which have been adjusted for certain changes, additions and expiry of contracts and depreciated over the terms of the lease contracts.

During the year ended December 31, 2019, the Corporation sold its working interest in the Sabanas flowline for net proceeds of $12 million, with a carrying value of $13.3 million and corresponding decommissioning obligation of $0.5 million, resulting in a loss on sale of assets of $0.8 million.

During the year ended December 31, 2019, certain costs related to the Corporation's Rancho Hermoso block were transferred to assets held for sale at their carrying values due to the Corporation's intention to sell such assets subsequent to December 31, 2019 (note 6).

## NOTE 6 – ASSETS AND LIABILITIES HELD FOR SALE

During the year ended December 31, 2018, the Corporation completed the sale of its Ecuador IPC investment held for sale and received $22.1 million of the total $28.1 million cash proceeds and the $8.3 million outstanding term deposit, previously recorded as restricted cash. The remaining $6 million of the cash proceeds were collected during the year ended December 31, 2019. The proceeds received were equal to the carrying amount of the assets held for sale at the disposition date.

During the year ended December 31, 2018, the Corporation completed the sale of certain petroleum held for sale assets and corresponding liabilities, for an aggregate consideration of $40 million, adjusted for customary closing adjustments of $0.8 million, resulting in total adjusted consideration of $39.2 million. The adjusted consideration consisted of $14.2 million in cash payments, $20 million through the receipt of 22,598,870 of common shares of Arrow ("Arrow's Shares") and a $5 million promissory note, bearing annual interest rate of 15%, with a maturity date of April 2021. Additional other assets with carrying values of $1 million were also transferred to Arrow, resulting in an overall loss on assets and liabilities held for sale of $1.8 million recognized during the year ended December 31, 2018. Subsequently, the 22,598,870 Arrow's Shares were distributed to the Corporation's shareholders (the "Shareholders") as a return of share capital. The Shareholders received 0.127 of Arrow's Shares per each common share of Canacol owned by the shareholder.

During the year ended December 31, 2019, the Corporation classified costs and corresponding liabilities related to its Rancho Hermoso block as assets and liabilities held for sale due to its intention to sell its working interest within one year of December 31, 2019. As at December 31, 2019, the held for sale assets and liabilities were recognized at their carrying amounts of $8 million and $10.6 million, respectively, which are the lower of their carrying amounts and estimated fair value less cost to sell.

*(in United States dollars (tabular amounts in thousands) except as otherwise noted)*

## NOTE 7 – OTHER ASSETS

| | December 31, 2019 | December 31, 2018 |
|---|---|---|
| **Current** | | |
| Restricted cash | $ 1,189 | $ 1,208 |
| Prepaid expenses and deposits | 1,634 | 1,909 |
| Investments | 1,186 | 1,466 |
| Crude oil inventory | 277 | 314 |
| Hedging contract | 644 | — |
| | $ 4,930 | $ 4,897 |
| **Non-Current** | | |
| Restricted cash | $ 3,335 | $ 2,988 |
| Prepaid expenses and deposits | 2,033 | 1,608 |
| Investments | 655 | 350 |
| | $ 6,023 | $ 4,946 |

### Restricted cash

| | December 31, 2019 | December 31, 2018 |
|---|---|---|
| Restricted cash - current | $ 1,189 | $ 1,208 |
| Restricted cash - non-current | 3,335 | 2,988 |
| | $ 4,524 | $ 4,196 |

At December 31, 2019, restricted cash consisted of $4.5 million (2018 - $4.2 million) for work commitments and other capital commitments, of which $1.2 million (2018 - $1.2 million) is classified as current and $3.3 million (2018 - $3 million) is classified as non-current.

### Investments

| | Office Sub-Lease | Share Investments | Total Investments |
|---|---|---|---|
| Balance at December 31, 2017 | $ — | $ 18,629 | $ 18,629 |
| Additions | — | 5,125 | 5,125 |
| Disposals | — | (12,725) | (12,725) |
| Realized loss | — | (2,489) | (2,489) |
| Unrealized loss | — | (7,076) | (7,076) |
| Foreign exchange gain | — | 352 | 352 |
| Balance at December 31, 2018 | $ — | $ 1,816 | $ 1,816 |
| Adoption of IFRS 16 | 1,007 | — | 1,007 |
| Sub-lease receipts and finance income | (363) | — | (363) |
| Unrealized loss | — | (721) | (721) |
| Foreign exchange gain | 39 | 63 | 102 |
| **Balance at December 31, 2019** | **$ 683** | **$ 1,158** | **$ 1,841** |
| Investments - current | $ 378 | $ 808 | $ 1,186 |
| Investments - non-current | 305 | 350 | 655 |
| **Balance at December 31, 2019** | **$ 683** | **$ 1,158** | **$ 1,841** |

During the year ended December 31, 2018, the Corporation disposed of certain share investments as follows: i) Interoil Exploration and Production ASA shares for proceeds and a realized gain on investment of $1.9 million, ii) 0.5% interest in Oleoducto Bicentenario de Colombia ("OBC") was transferred to Arrow for no additional proceeds, resulting in a realized loss on investment of $1.8 million and iii) Interamerican Energy Corp. for proceeds of $12.4 million, consisting of $10.8 million for its investment and settlement of an outstanding loan receivable of $1.6 million, resulting in a loss on investment of $2.5 million.

(in United States dollars (tabular amounts in thousands) except as otherwise noted)

The Corporation holds five million shares of Arrow valued at $0.8 million as at December 31, 2019. Two members of key management of Canacol are also members of the board of directors of Arrow.

The Corporation holds a head lease for an office lease recognized as a finance lease obligation, which is subleased to a third party in return for monthly lease income. The sub-lease contract is reported separately from the head lease and is recognized as a net investment upon transition of IFRS 16 (note 3). A portion of the investment equal to $0.4 million has been classified as current as it will be received within the next twelve months.

## NOTE 8 – OTHER LIABILITIES

| | December 31, 2019 | December 31, 2018 |
|---|---|---|
| **Current** | | |
| Deferred income | $ 11,134 | $ 5,413 |
| Restricted share units | 2,235 | 2,112 |
| Settlement liability | 2,306 | 3,600 |
| | $ 15,675 | $ 11,125 |
| **Non-Current** | | |
| Restricted share units | $ 15 | $ 31 |
| Settlement liability | 13,542 | 13,149 |
| Other long term obligations | 3,219 | 2,533 |
| | $ 16,776 | $ 15,713 |

### Deferred Income

During the year ended December 31, 2019, the Corporation received proceeds for natural gas and crude oil to be delivered at a later date (“Undelivered Nominations”). As at December 31, 2019, Undelivered Nominations resulted in a deferred income balance of $11.1 million (2018 - $5.4 million), all of which related to natural gas (2018 - gas $5.2 million; crude oil - $0.2 million) which has been classified as a current liability as it is expected to be settled within the next twelve months.

### Restricted Share Units

| | |
|---|---|
| Balance at December 31, 2017 | $ 2,003 |
| Grant | 3,542 |
| Settled | (3,341) |
| Realized loss | 100 |
| Unrealized gain | (169) |
| Foreign exchange loss | 8 |
| Balance at December 31, 2018 | 2,143 |
| Amortized | 4,523 |
| Settled | (4,532) |
| Foreign exchange loss | 116 |
| **Balance at December 31, 2019** | **$ 2,250** |

RSUs are recognized as an obligation and expensed on a graded vesting basis over the vesting term of each grant. The vested RSU obligation as at December 31, 2019 was $2.3 million (2018 - $2.1 million). Amortized RSUs of 625,790 of the total 879,586 RSUs outstanding have been recognized as an obligation as at December 31, 2019. The remaining 253,796 RSUs will be recognized over the remaining vesting period.

(in United States dollars (tabular amounts in thousands) except as otherwise noted)

The number of outstanding RSUs as at December 31, 2019 were as follows:

| | Outstanding Units (000's) |
|---|---|
| Balance at December 31, 2017 | 617 |
| Granted | 1,039 |
| Settled | (932) |
| Balance at December 31, 2018 | 724 |
| Granted | 1,461 |
| Settled | (1,305) |
| **Balance at December 31, 2019** | **880** |

On January 26, 2018, August 16, 2018, and October 3, 2018 the Corporation granted 631,500, 393,000 and 14,433 RSUs with reference prices of C$4.42, C$4.12 and a range from C$4.12 to C$4.26 per share, respectively. The RSUs vested one-half in six months and one-half in one year from the grant date, and were settled in cash. During the year ended December 31, 2018, 931,886 RSUs were settled in cash at a price ranging from C$4.01 to C$4.71 per share, resulting in cash settlements of $3.3 million.

On January 28, 2019 and August 28, 2019, the Corporation granted 970,500 and 490,000 RSUs, respectively. The RSUs vest one-half in six months and one-half in one year from the grant date, and are anticipated to be settled in cash. During the year ended December 31, 2019, 1,304,711 RSUs were settled in cash at a price ranging from C$4.24 to C$4.62 per share, resulting in cash settlements of $4.5 million.

**Settlement liability**

| | | |
|---|---|---|
| Balance at December 31, 2017 | $ | — |
| Settlement expense | | 20,258 |
| Settlement payments | | (1,396) |
| Foreign exchange gain | | (2,113) |
| Balance at December 31, 2018 | | 16,749 |
| Settlement payments, net of accrued interest | | (1,042) |
| Foreign exchange loss | | 141 |
| **Balance at December 31, 2019** | **$** | **15,848** |

Pursuant to a settlement agreement between the Corporation and another Colombian entity over the payment of certain operating costs relating to crude oil production, a settlement liability and expense of $20.3 million (the "Settlement") was recorded during the year ended December 31, 2018. The settlement amount is subject to a 8.74% annual interest rate on the outstanding balance. In accordance with the terms of the settlement agreement, cash payments of approximately $0.3 million per month, including accrued interest will be paid by the Corporation and, as such, $2.3 million has been classified as current.

*(in United States dollars (tabular amounts in thousands) except as otherwise noted)*

## NOTE 9 – SHARE CAPITAL

**Authorized**

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

**Issued and Outstanding**

| | Number (000's) | | Amount |
|---|---|---|---|
| Balance at December 31, 2017 | 176,109 | $ | 707,125 |
| Issued on exercise of stock options | 1,705 | | 4,215 |
| Transfer from other reserves for stock options | — | | 2,660 |
| Common share repurchases | (352) | | (1,037) |
| Transfer of deficit to share capital | — | | (533,847) |
| Return of share capital | — | | (20,000) |
| Balance at December 31, 2018 | 177,462 | | 159,116 |
| Issued on exercise of stock options | 3,048 | | 8,634 |
| Transfer from other reserves for stock options | — | | 3,152 |
| Common share repurchases | (435) | | (1,443) |
| **Balance at December 31, 2019** | **180,075** | **$** | **169,459** |

On July 3, 2018, the shareholders of the Corporation (the "Shareholders") approved a reduction in stated share capital by the amount of the Corporation's deficit of $533.8 million as at January 1, 2018. A distribution to the Shareholders, as a return of share capital, either in cash, or property, in the amount of $20 million was also approved by the Shareholders. During the year ended December 31, 2018, the board of directors declared a $20 million special distribution, in this regard, to be settled by the transfer of the 22,598,870 Arrow's Shares received as a portion of sale proceeds (note 6). The Shareholders received 0.127 of Arrow's Shares per each common share of Canacol owned by the shareholder.

During the year ended December 31, 2018, the Corporation obtained necessary approval to conduct a normal course issuer bid ("NCIB") to purchase outstanding common shares of the Corporation ("Common Shares") on the open market, in accordance with the rules of the TSX. As approved by the TSX, the Corporation was authorized to purchase up to 14,086,746 Common Shares, representing approximately 10% of the public float of Canacol at the time. The maximum number of Common Shares that Canacol could purchase on any given day is 31,126 Common Shares, which was 25% of the Corporation's average daily trading volume on the TSX for the six months ended October 31, 2018. Canacol was also authorized to make one weekly block repurchase which exceeded the daily limit subject to prescribed rules. The Corporation was authorized to make purchases during the period from November 20, 2018 to November 19, 2019, or until such earlier time as the NCIB was completed or terminated at the option of the Corporation. During the year ended December 31, 2018, the Corporation purchased 351,282 Common Shares at a cost of $1 million, including transaction fees. All Common Shares acquired under the NCIB were cancelled.

During the year ended December 31, 2019, the Corporation renewed its NCIB authorization to purchase up to 14,276,439 Common Shares, representing approximately 10% of the public float of Canacol at the time. The maximum number of Common Shares that Canacol may purchase on any given day is 46,189 Common Shares, which is 25% of the Corporation's average daily trading volume on the TSX for the six months ended November 30, 2019. Canacol may also make one weekly block repurchase which exceeds the daily limit subject to prescribed rules. The Corporation is authorized to make purchases during the period from December 11, 2019 to December 10, 2020, or until such earlier time as the NCIB is completed or terminated at the option of the Corporation. During the year ended December 31, 2019, the Corporation repurchased 434,608 Common Shares at a cost of $1.4 million, including transaction fees. Subsequent to December 31, 2019, the Corporation repurchased 269,345 shares at a cost of $0.9 million, including transaction fees.

*(in United States dollars (tabular amounts in thousands) except as otherwise noted)*

### Stock Options

The number and weighted-average exercise prices of stock options were as follows:

| | Number | Weighted-Average Exercise Price |
|---|---|---|
| | (000's) | (C$) |
| Balance at December 31, 2017 | 14,853 | 3.89 |
| Granted | 3,781 | 4.34 |
| Exercised | (1,705) | 3.17 |
| Forfeited and cancelled | (1,247) | 4.50 |
| Balance at December 31, 2018 | 15,682 | 4.02 |
| Granted | 3,108 | 4.51 |
| Exercised | (3,048) | 3.69 |
| Forfeited and cancelled | (1,508) | 5.87 |
| **Balance at December 31, 2019** | **14,234** | **3.92** |

Information with respect to stock options outstanding at December 31, 2019 is presented below.

| Stock Options Outstanding | | | | Stock Options Exercisable | |
|---|---|---|---|---|---|
| Range of Exercise Prices | Number of Stock Options | Weighted-Average Remaining Contractual Life | Weighted-Average Exercise Price | Number of Stock Options | Weighted-Average Exercise Price |
| (C$) | (000's) | (years) | (C$) | (000's) | (C$) |
| \$2.13 - \$4.20 | 7,724 | 1.5 | 3.53 | 7,540 | 3.52 |
| \$4.21 - \$4.62 | 6,510 | 3.3 | 4.38 | 4,541 | 4.34 |
| | **14,234** | **2.3** | **3.92** | **12,081** | **3.83** |

The fair value of the stock options granted was estimated using the Black-Scholes option pricing model with the following weighted-average inputs:

| Year ended December 31, | 2019 | 2018 |
|---|---|---|
| Weighted-average fair value at grant date (C$) | **1.19** | 1.51 |
| Share price (C$) | **4.45 - 4.62** | 4.34 - 4.42 |
| Exercise price (C$) | **4.45 - 4.62** | 4.34 - 4.42 |
| Volatility | **27% - 34%** | 42% - 47% |
| Option life | **5 years** | 5 years |
| Dividends | **Nil** | Nil |
| Risk-free interest rate | **1.67% - 1.87%** | 1.85% - 1.96% |

A forfeiture rate of 8% (2018 - 6%) was used when recording stock-based compensation for the year ended December 31, 2019. Stock-based compensation of \$3.4 million (2018 - \$4.9 million) was expensed during the year ended December 31, 2019.

*(in United States dollars (tabular amounts in thousands) except as otherwise noted)*

## NOTE 10 – LONG-TERM DEBT

| | Senior Notes | Bank Debt | Total |
|---|---|---|---|
| Balance at December 31, 2017 | $ — | $ 294,590 | $ 294,590 |
| Draw, net of transaction costs | 310,135 | 28,601 | 338,736 |
| Repayment | — | (305,000) | (305,000) |
| Loss on settlement of long-term debt | — | 9,426 | 9,426 |
| Amortization of transaction costs | 920 | 1,012 | 1,932 |
| Balance at December 31, 2018 | 311,055 | 28,629 | 339,684 |
| Amortization of transaction costs | 1,393 | 508 | 1,901 |
| **Balance at December 31, 2019** | **$ 312,448** | **$ 29,137** | **$ 341,585** |

On May 3, 2018, the Corporation completed a private offering of senior unsecured notes ("Senior Notes") in the aggregate principal amount of $320 million. The net proceeds were used to fully repay the outstanding amounts borrowed under its existing credit facility in the amount of $305 million plus accrued interest and transaction costs. As a result of the repayment of the existing credit facility, a loss on settlement of long-term obligations totaling $14.4 million was recognized, consisting of $9.4 million of unamortized financing fees at the time of settlement and a prepayment penalty of $5 million. The Senior Notes pay interest semi-annually at a fixed rate of 7.25% per annum, and will mature in May 2025, unless earlier redeemed or repurchased in accordance with their terms.

On December 6, 2018, the Corporation entered into a credit agreement for an amount of $30 million with Credit Suisse ("Bank Debt"). The Bank Debt will mature on December 11, 2022, with interest payable quarterly and principal repayable in 11 equal quarterly installments starting June 11, 2020, following more than one year of initial grace period. The Bank Debt carries interest at a fixed rate of 6.875% per annum and is secured by Jobo 2. A portion of the proceeds from the Bank Debt totaling $24.2 million were used to purchase Jobo 2, previously held under a finance lease agreement (note 12).

Long-term debt includes various financial and non-financial covenants relating to indebtedness, operations, investments, assets sales, capital expenditures and other standard operating business covenants. The Bank Debt is also subject to various financial covenants, including a maximum consolidated leverage ratio of 3.50:1.00 and a minimum consolidated EBITDAX to interest expense, excluding non-cash interest expenses, ratio of 2.50:1.00. As at December 31, 2019, the Corporation was in compliance with the covenants.

A portion of Bank Debt, net of unamortized transaction costs equal to $8.2 million has been classified as current due to the first of eleven quarterly installments commencing on June 11, 2020. As at December 31, 2019, unamortized transaction costs of $7.6 million (2018 - $8.9 million) and $0.9 million (2018 - $1.4 million) are netted against the Senior Notes and Bank Debt principal amounts, resulting in carrying values of $312.4 million (2018 - $311.1 million) and $29.1 million (2018 - $28.6 million), respectively.

*(in United States dollars (tabular amounts in thousands) except as otherwise noted)*

## NOTE 11 – DECOMMISSIONING OBLIGATION

| | | |
|---|---|---|
| Balance at December 31, 2017 | $ | 19,223 |
| Accretion | | 1,625 |
| Additions | | 5,219 |
| Settlements | | (2,250) |
| Change in estimates | | (127) |
| Balance at December 31, 2018 | | 23,690 |
| Accretion | | 1,496 |
| Additions | | 2,594 |
| Disposition (note 5) | | (499) |
| Settlements | | (847) |
| Transferred to assets held for sale (note 6) | | (10,591) |
| Change in estimates | | 555 |
| **Balance at December 31, 2019** | **$** | **16,398** |

The Corporation's decommissioning obligations result from its ownership interests in natural gas and petroleum assets, including well sites, facilities, and gathering systems. The total decommissioning obligations are estimated based on the Corporation's net ownership interest in all wells and facilities, estimated costs to reclaim and abandon these wells and facilities and the estimated timing of the costs to be incurred in future years. The Corporation has estimated the present value of the decommissioning obligations to be $16.4 million at December 31, 2019 (2018 - $23.7 million) based on an undiscounted total future liability of $34.7 million (2018 - $35 million). These payments are expected to be made over the next 14 years. The average discount factor, being the risk-free rate related to the liability, is 6.4% (2018 - 6.1%) and the average inflation rate is 3.3% (2018 - 3.3%).

During the year ended December 31, 2019, the Corporation sold its working interest in the Sabanas flowline for net proceeds of $12 million, with a carrying value of $13.3 million and corresponding decommissioning obligation of $0.5 million, resulting in a loss on sale of assets of $0.8 million (note 5).

During the year ended December 31, 2019, the Corporation classified $10.6 million of decommissioning obligations related to the Corporation's Rancho Hermoso block as liabilities held for sale (note 6).

*(in United States dollars (tabular amounts in thousands) except as otherwise noted)*

## NOTE 12 – LEASE OBLIGATIONS

| As at December 31, 2019 | | Minimum Lease Payments | | PV of Minimum Lease Payments |
|---|---|---|---|---|
| **IFRS 16 adoption** | | | | |
| Not later than one year | $ | 3,243 | $ | 2,882 |
| Later than one year and not later than five years | | 4,612 | | 4,444 |
| Later than five years | | — | | — |
| | | 7,855 | | 7,326 |
| Less: future finance charges | | (529) | | — |
| **PV of minimum lease payments** | **$** | **7,326** | **$** | **7,326** |
| **Compression stations** | | | | |
| Not later than one year | $ | 2,839 | $ | 1,849 |
| Later than one year and not later than five years | | 11,936 | | 9,067 |
| Later than five years | | 9,596 | | 8,856 |
| | | 24,371 | | 19,772 |
| Less: future finance charges | | (4,599) | | — |
| **PV of minimum lease payments** | **$** | **19,772** | **$** | **19,772** |
| Lease obligations - current | | | $ | 4,731 |
| Lease obligations - non-current | | | | 22,367 |
| **PV of minimum lease payments** | | | **$** | **27,098** |

| As at December 31, 2018 | | Minimum Lease Payments | | PV of Minimum Lease Payments |
|---|---|---|---|---|
| **Compression stations** | | | | |
| Not later than one year | $ | 2,783 | $ | 1,701 |
| Later than one year and not later than five years | | 11,702 | | 8,378 |
| Later than five years | | 12,669 | | 11,394 |
| | | 27,154 | | 21,473 |
| Less: future finance charges | | (5,681) | | — |
| **PV of minimum lease payments** | **$** | **21,473** | **$** | **21,473** |
| Lease obligations - current | | | $ | 1,701 |
| Lease obligations - non-current | | | | 19,772 |
| **PV of minimum lease payments** | | | **$** | **21,473** |

During the year ended December 31, 2018, the Corporation purchased Jobo 2, which had a finance lease obligation carrying value of $21.3 million, for a purchase price of $24.2 million, resulting in $3 million being capitalized to the Jobo 2 asset carrying value (note 5).

As at January 1, 2019, the Corporation adopted IFRS 16, resulting in the recognition of $7.3 million of lease obligations, previously recognized as operating leases under IAS 17 (note 3). The lease obligations were discounted at the incremental borrowing rate of 6.875% at inception and was initially recognized at the present value of minimum lease payments. The lease terms range from one to four years. The amortized lease carrying value as at December 31, 2019 was $7.3 million.

The Corporation utilized certain IFRS 16 exemptions to exclude low-value right-of-use assets and short-term lease arrangements as leases. Lease arrangements with variable payments were also excluded from being recognized as a lease obligation and right-of-use asset. Low-value right-of-use assets were recognized as operating expenses on the consolidated statements of operations during the year ended December 31, 2019. A portion of the short-term lease arrangements were capitalized to E&E and D&P assets (note 4 and note 5) and a portion was recognized as operating expenses on the consolidated statements of operations during the year ended December 31, 2019. The variable lease payments were recognized as transportation expenses on the consolidated statements of operations during the year ended December 31, 2019.

(in United States dollars (tabular amounts in thousands) except as otherwise noted)

These lease payments were recognized on a straight-line basis summarized as follows:

| Year ended December 31, | | 2019 | | 2018 |
|---|---|---|---|---|
| Low-value right-of-use assets | $ | 103 | $ | — |
| Short-term lease arrangements | | 797 | | — |
| Variable lease payments | | 25,637 | | — |
| **Total lease payments** | $ | 26,537 | $ | — |

Future lease payments related to these lease arrangements as at December 31, 2019 are as follows:

| | | Less than 1 | | 1-3 years | | Thereafter | | Total |
|---|---|---|---|---|---|---|---|---|
| Future lease payments | $ | 26,771 | $ | 46,799 | $ | 32,780 | $ | 106,350 |

## NOTE 13 – OTHER EXPENSES (INCOME)

| | Note | | December 31, 2019 | | December 31, 2018 |
|---|---|---|---|---|---|
| Donations | | $ | 1,371 | $ | 2,668 |
| Foreign exchange loss | | | 59 | | 3,559 |
| Other expenses | | | 5,493 | | 2,979 |
| Other tax expense | | | 3,666 | | 2,222 |
| Loss on financial instruments | | | 9 | | 8,580 |
| Dividend income | | | — | | (356) |
| Loss on assets and liabilities held for sale | 6 | | — | | 1,822 |
| | | $ | 10,598 | $ | 21,474 |

### Loss (Gain) on Financial Instruments

| Year ended December 31, | | 2019 | | 2018 |
|---|---|---|---|---|
| Hedging contract - unrealized | $ | (643) | $ | 35 |
| Hedging contract - realized | | (69) | | (251) |
| Investments - unrealized | | 721 | | 7,076 |
| Investments - realized | | — | | 2,489 |
| Crude oil payable in kind - realized | | — | | (844) |
| Crude oil payable in kind - unrealized | | — | | 144 |
| Restricted share units - unrealized | | — | | (169) |
| Restricted share units - realized | | — | | 100 |
| | $ | 9 | $ | 8,580 |

### Dividend Income

The Corporation was eligible to receive dividends on its OBC investment, which totaled $0.4 million during the year ended December 31, 2018. The Corporation sold its OBC investment during the year ended December 31, 2018 (note 7).

*(in United States dollars (tabular amounts in thousands) except as otherwise noted)*

## NOTE 14 – FINANCE INCOME AND EXPENSE

| Year ended December 31, | | 2019 | | 2018 |
|---|---|---|---|---|
| **Finance income** | | | | |
| Interest and other income | $ | 1,283 | $ | 865 |
| **Finance expense** | | | | |
| Accretion on decommissioning obligations | | 1,496 | | 1,625 |
| Amortization of upfront fees | | 1,901 | | 1,932 |
| Interest expense on lease obligations | | 1,531 | | 3,462 |
| Interest and other financing costs | | 29,257 | | 28,385 |
| | $ | 34,185 | $ | 35,404 |
| **Net finance expense** | $ | 32,902 | $ | 34,539 |

## NOTE 15 – NET INCOME (LOSS) PER SHARE

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

| Year ended December 31, | | 2019 | | 2018 |
|---|---|---|---|---|
| Net income (loss) | $ | 34,247 | $ | (21,835) |
| **Weighted-average common shares outstanding:** | | | | |
| Weighted-average common shares outstanding, basic | | 178,266 | | 177,184 |
| Effect of stock options | | 2,129 | | — |
| **Weighted-average common shares outstanding, diluted** | | 180,395 | | 177,184 |

Due to the net loss realized during the year ended December 31, 2018, stock options were anti-dilutive.

## NOTE 16 – DIVIDEND DECLARED

During the year ended December 31, 2019, the Corporation declared a dividend of C$0.052 per share, totaling $7.1 million paid on December 30, 2019, to the Corporation's shareholders of record at the close of business on December 16, 2019. The ex-dividend date for all shareholders was December 13, 2019. The declaration, timing, amount and payment of future dividends remain at the discretion of the Board of Directors.

*(in United States dollars (tabular amounts in thousands) except as otherwise noted)*

## NOTE 17 – INCOME TAXES

The following table reconciles income taxes calculated at the Canadian Statutory rate with actual income taxes:

| Year ended December 31, | | 2019 | | 2018 |
|---|---|---|---|---|
| Net income (loss) before taxes | $ | 64,734 | $ | 7,348 |
| Statutory rates | | 27% | | 27% |
| Expected income taxes | | 17,478 | | 1,984 |
| Effect on taxes resulting from: | | | | |
| Non-deductible share-based payments and other permanent differences | | 776 | | 5,794 |
| Tax differential on foreign jurisdictions | | 6,324 | | 6,515 |
| Change in unrecognized tax benefit | | 6,340 | | 1,803 |
| Provision to filing true-up | | 926 | | (404) |
| Change in enacted tax rate | | 1,028 | | (5,058) |
| Foreign exchange and other | | (2,385) | | 20,303 |
| **Provision for income taxes** | $ | 30,487 | $ | 30,937 |
| Current | | 32,058 | $ | 23,587 |
| Deferred tax (recovery) expense | | (1,571) | | 7,350 |
| | $ | 30,487 | $ | 30,937 |

The net deferred tax asset is comprised of:

| Year ended December 31, | | 2019 | | 2018 |
|---|---|---|---|---|
| Net book value of property, plant and equipment in excess of asset tax base | $ | (45,559) | $ | (48,091) |
| Losses carried forward | | 59,001 | | 62,415 |
| Decommissioning liabilities and other provision | | 9,274 | | 7,867 |
| Timing differences on revenue and expense recognition and other | | 1,901 | | 855 |
| **Deferred tax asset** | $ | 24,617 | $ | 23,046 |

At December 31, 2019, the Corporation had non-capital losses carried forward of approximately $184.5 million (2018 - $195.7 million) available to reduce future years taxable income. At December 31, 2019, the Corporation had deferred income tax assets of $73.5 million (2018 - $67.2 million) related to Canada and Colombia that were not recognized in the financial statements due to uncertainties associated with its ability to utilize these balances in the future.

In the fourth quarter of 2019, the Colombian government enacted a new tax reform to replace the 2018 tax reform, which was overturned by the Colombian Constitutional Court. This new tax reform maintains the same corporate tax rates that were approved by congress in 2018. The enacted tax rates are 32% for 2020, 31% for 2021 and 30% for 2022 and onwards. The tax rates applied to the calculation of deferred income taxes, before valuation allowances, have been adjusted to reflect these changes.

*(in United States dollars (tabular amounts in thousands) except as otherwise noted)*

## NOTE 18 – OTHER CASH FLOW ACTIVITIES

### Other Operating Activities

| Year ended December 31, | Note | 2019 | 2018 |
|---|---|---|---|
| Settlement liability principal payments | 8 | $ (1,042) | $ (1,396) |
| Settlement of decommissioning obligations | 11 | (847) | (2,250) |
| Settlement of restricted share units liability | 8 | (4,532) | (3,241) |
| | | $ (6,421) | $ (6,887) |

### Other Investing Activities

| Year ended December 31, | Note | 2019 | 2018 |
|---|---|---|---|
| Investment | 7 | $ 363 | $ (5,125) |
| Change in restricted cash | | (328) | 23,723 |
| Change in prepaid expenses and deposits | | (425) | 1,072 |
| Proceeds from investment in subsidiary | 7 | — | 500 |
| Proceeds from disposal of investments | 7 | — | 12,725 |
| | | $ (390) | $ 32,895 |

### Non-Cash Working Capital

| Year ended December 31, | 2019 | 2018 |
|---|---|---|
| **Change in:** | | |
| Trade and other receivables | $ (12,993) | $ (12,985) |
| Prepaid expenses and deposits | 275 | (347) |
| Tax installments and receivables | (3,567) | (2,396) |
| Crude oil inventory | 17 | (48) |
| Trade and other payables | 3,800 | (13,917) |
| Crude oil payable in kind | — | (48) |
| Deferred income | 5,721 | 608 |
| Taxes payable | (270) | (5,920) |
| | $ (7,017) | $ (35,053) |
| **Attributable to:** | | |
| Operating activities | $ (13,824) | $ (8,653) |
| Investing activities | 6,807 | (26,400) |
| | $ (7,017) | $ (35,053) |

*(in United States dollars (tabular amounts in thousands) except as otherwise noted)*

## NOTE 19 – SUPPLEMENTAL INFORMATION

### Natural Gas and Crude Oil Revenues, Net of Royalties

The Corporation records natural gas and crude oil revenues, net of royalties on a consolidated basis which were allocated as follows:

| Year ended December 31, | | 2019 | | 2018 |
|---|---|---|---|---|
| Natural gas revenues, net of royalties | $ | 234,629 | $ | 188,725 |
| Petroleum revenues, net of royalties | $ | 6,212 | $ | 30,694 |

Natural gas and crude oil royalties incurred were allocated as follows:

| Year ended December 31, | | 2019 | | 2018 |
|---|---|---|---|---|
| Natural gas royalties | $ | 34,219 | $ | 24,581 |
| Petroleum royalties | $ | 521 | $ | 3,200 |

### Take-or-Pay Natural Gas Income

During the year ended December 31, 2019, the Corporation realized take-or-pay natural gas income of $1.2 million (2018 - $3 million) relating to the portion of natural gas sales nominations by the Corporation's off-takers that did not get delivered, due to the off-takers' inability to accept such gas and for which the off-takers have no recourse or legal right to delivery at a later date.

### Cash Income taxes and Interest Expenses

Cash payments of income taxes and interest were as follows:

| Year ended December 31, | | 2019 | | 2018 |
|---|---|---|---|---|
| Income taxes paid | $ | 30,336 | $ | 32,569 |
| Interest paid | $ | 27,148 | $ | 23,943 |

## NOTE 20 – KEY MANAGEMENT PERSONNEL

The Corporation has determined that the key management personnel of the Corporation consists of its executive management and its Board of Directors. In addition to the salaries and fees paid to key management, the Corporation also provides compensation to both groups under its stock-based compensation and restricted share unit plans. Compensation expenses paid to key management personnel were as follows:

| Year ended December 31, | | 2019 | | 2018 |
|---|---|---|---|---|
| Salaries and director fees | $ | 4,980 | $ | 4,412 |
| Severance | | 2,858 | | — |
| Benefits | | 691 | | 812 |
| Stock-based compensation | | — | | 1,202 |
| Restricted share units | | 2,098 | | 1,997 |
| **Key management personnel compensation** | $ | **10,627** | $ | 8,423 |

*(in United States dollars (tabular amounts in thousands) except as otherwise noted)*

## NOTE 21 – SIGNIFICANT SUBSIDIARIES

The Corporation has the following significant subsidiaries:

| | Country of | | Ownership Interest | |
|---|---|---|---|---|
| | **Incorporation** | **Fiscal year end** | **December 31, 2019** | **December 31, 2018** |
| Canacol Energy Inc. | Canada | December 31 | 100% | 100% |
| Shona Energy L.P. | Canada | December 31 | 100% | 100% |
| CNE Oil & Gas S.A.S (Colombia) | Colombia | December 31 | 100% | 100% |

## NOTE 22– SEGMENTED INFORMATION

The Corporation's only reportable segment is "Colombia". The main purpose of "Other Segments" is to reconcile the reportable segment to the Corporation's combined results. "Other Segments" is not a reportable segment. The Corporation's chief operating decision makers are its executive officers.

| | Colombia (reportable) | Other Segments (non-reportable) | Total |
|---|---|---|---|
| **Year ended December 31, 2019** | | | |
| Revenue and other income | $ 242,079 | $ — | $ 242,079 |
| Expenses, excluding income tax | (129,070) | (48,275) | (177,345) |
| Net income (loss) before taxes | 113,009 | (48,275) | 64,734 |
| Income tax expense | 29,617 | 870 | 30,487 |
| Net income (loss) | $ 83,392 | $ (49,145) | $ 34,247 |
| Capital expenditures, net of dispositions | $ 98,654 | $ 1,833 | $ 100,487 |
| **Year ended December 31, 2018** | | | |
| Revenue and other income | $ 222,769 | $ — | $ 222,769 |
| Expenses, excluding income tax and impairments | (158,266) | (66,416) | (224,682) |
| Impairment on E&E assets | (9,865) | — | (9,865) |
| Impairment recovery | 19,126 | — | 19,126 |
| Net income (loss) before taxes | 73,764 | (66,416) | 7,348 |
| Income tax expense | 29,183 | — | 29,183 |
| Net income (loss) | $ 44,581 | $ (66,416) | $ (21,835) |
| Capital expenditures, net of dispositions | $ 127,396 | $ 195 | $ 127,591 |
| **Balance at December 31, 2019** | | | |
| Total assets | $ 697,471 | $ 56,591 | $ 754,062 |
| Total liabilities | $ 151,253 | $ 360,063 | $ 511,316 |
| **Balance at December 31, 2018** | | | |
| Total assets | $ 471,653 | $ 233,350 | $ 705,003 |
| Total liabilities | $ 153,789 | $ 345,777 | $ 499,566 |

Major customers are customers which represent more than 10% of total revenue for a given period. For the year ended December 31, 2019, three major customers represented 32%, 13% and 13% of total revenues in the year, respectively. For the year ended December 31, 2018, three major customers represented 28%, 19% and 10% of total revenues in the year, respectively.

*(in United States dollars (tabular amounts in thousands) except as otherwise noted)*

## NOTE 23 – FINANCIAL INSTRUMENTS AND RISK MANAGEMENT

**Fair Value of Financial Instruments**

The carrying values of cash and cash equivalents, restricted cash, trade and other receivables, tax installments and receivables, trade and other payables, taxes payable, lease obligations, settlement liability approximate their fair values at December 31, 2019. Restricted Share Units ("RSUs"), investments and hedging contract are recorded at fair value. The fair value of the Senior Notes and Bank Debt is $336.4 million and $30 million, respectively.

The Corporation classifies the fair value of financial instruments measured at fair value 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 in Level 2 are either directly or indirectly observable as of the reporting date. Level 2 valuations are based on inputs, including quoted forward prices for commodities, 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's financial instruments have been assessed on the fair value hierarchy described above. Investments, Senior Notes and RSUs were classified as Level 1 and the hedging contract, settlement liability and Bank Debt were classified as level 2 as at December 31, 2019. There has been no reclassification of financial instruments into or out of each fair value hierarchy during the year ended December 31, 2019. Assessment of the significance of a particular input to the fair value measurement requires judgement and may affect the placement within the fair value hierarchy level.

**Market Risk**

Market risk is the risk that changes in market factors, such as commodity prices, foreign exchange rates, and interest rates will affect the Corporation's cash flows, profit or loss, liquidity or the value of financial instruments. The objective of market risk management is to mitigate market risk exposures where considered appropriate and maximize returns.

(i) Commodity Price Risk

Commodity price risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate as a result of changes in commodity prices. Lower commodity prices can also impact the Corporation's ability to raise capital. The majority of Canacol's production volume is subject to long-term fixed price contracts, which limits the Corporation's exposure to commodity price risk. The Corporation had no commodity contracts in place as at or during the year ended December 31, 2019.

(ii) Foreign Currency Risk

Foreign currency risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate as a result of changes in foreign currency exchange rates. The Corporation is exposed to foreign currency fluctuations as certain expenditures, as well as the Corporation's unused tax losses, are denominated in Colombian pesos ("COP") and Canadian dollars ("CAD"). As at December 31, 2019, the COP to the United States dollar ("USD") exchange rate was 3,277:1 (December 31, 2018 – 3,250:1) and the CAD to USD exchange rate was 1.30:1 (December 31, 2018 – 1.36:1).

During the year ended December 31, 2019, the Corporation entered into a foreign exchange contract under the following terms:

| Term | Principal | Type | Exchange Rate Range |
|---|---|---|---|
| August 2019 - July 2020 | $2.5 million | COP to USD foreign exchange collar | 3,383:1 - 3,535:1 |

*(in United States dollars (tabular amounts in thousands) except as otherwise noted)*

(iii) Interest Rate Risk

Interest rate risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate as a result of changes in market interest rates to the extent that variable interest rate debt instruments are drawn. The Corporation is not currently exposed to interest rate risk as its interest-bearing loans are all subject to fixed interest rates. The remainder of the Corporation's financial assets and liabilities are not exposed to interest rate risk. The Corporation had no interest rate contracts in place as at or during the year ended December 31, 2019.

**Liquidity Risk**

Liquidity risk is the risk that the Corporation will not be able to meet its financial obligations as they become due. The Corporation's approach to managing liquidity is to ensure, within reasonable means, sufficient liquidity to meet its liabilities when due, under both normal and unusual conditions, without incurring unacceptable losses or jeopardizing the Corporation's business objectives. The Corporation prepares an annual budget which is monitored regularly and updated as considered necessary. Natural gas and crude oil production is monitored daily to provide current cash flow estimates and the Corporation utilizes authorizations for expenditures on projects to manage capital expenditures.

The following table outlines the contractual maturities of the Corporation's financial liabilities at December 31, 2019:

| | Less than 1 year | 1-2 years | Thereafter | Total |
|---|---|---|---|---|
| Long-term debt – principal | $ 8,182 | $ 10,909 | $ 330,909 | $ 350,000 |
| Lease obligations – undiscounted | 6,082 | 5,254 | 20,890 | 32,226 |
| Trade and other payables | 52,591 | — | — | 52,591 |
| Taxes payable | 6,043 | — | — | 6,043 |
| Deferred income | 11,134 | — | — | 11,134 |
| Settlement liability | 2,306 | 2,306 | 11,236 | 15,848 |
| Other long term obligation | — | 3,219 | — | 3,219 |
| Restricted share units | 2,235 | 15 | — | 2,250 |
| | **$ 88,573** | **$ 21,703** | **$ 363,035** | **$ 473,311** |

**Credit Risk**

Credit risk reflects the risk of loss if counterparties do not fulfill their contractual obligations. The majority of the Corporation's trade receivable balances relate to natural gas and crude oil sales. The Corporation's policy is to enter into agreements with customers that are well established and well financed entities in the oil and gas industry such that the level of risk is mitigated. To date, the Corporation has not experienced any material credit losses in the collection of its trade receivables. In Colombia, a significant portion of natural gas and crude oil sales are with customers that are directly or indirectly controlled by the government. The Corporation has also entered into sales agreements with certain Colombian private sector companies, mostly with investment grade credit ratings.

The Corporation's trade receivables primarily relate to sales of natural gas and crude oil, which are normally collected within 45 days of the month of production. The Corporation has historically not experienced any collection issues with its customers. The trade receivable balance, relating to contracts with customers, as at December 31, 2019 was $56.5 million (2018 - $41.4 million), $10.8 million related to the recovery of transportation costs passed-through to customers (2018 - $4.9 million), $5.7 million from Arrow related to the sale of certain petroleum assets (2018 - $8.2 million) and $2.2 million of other receivables (2018 - $1.1 million). The $5.7 million receivable from Arrow is scheduled to be collected through six equal monthly payments commencing in April 2021, and as such, has been classified as non-current as at December 31, 2019. The remaining receivable balances are anticipated be collected in 2020 and there are no expected credit losses as assessed by the Corporation.

(in United States dollars (tabular amounts in thousands) except as otherwise noted)

### Capital Management

The Corporation's policy is to maintain a strong capital base in order to provide flexibility in the future development of the business and maintain investor, creditor and market confidence. The Corporation manages its capital structure and makes adjustments in response to changes in economic conditions and the risk characteristics of the underlying assets. The Corporation considers its capital structure to include share capital, long-term debt, settlement liability, lease obligations and working capital, defined as current assets less current liabilities excluding the current portion of long-term obligations. In order to maintain or adjust the capital structure, from time to time the Corporation may issue or repurchase common shares or other securities, sell assets or adjust its capital spending to manage current and projected debt levels.

The Corporation monitors leverage and adjusts its capital structure based on its net debt level. Net debt is defined as the principal amount of its outstanding long-term obligations less working capital, as defined above. In order to facilitate the management of its net debt, the Corporation prepares annual budgets, which are updated as necessary depending on varying factors including current and forecast commodity prices, changes in capital structure, execution of the Corporation's business plan and general industry conditions. The annual budget is approved by the Board of Directors and updates are prepared and reviewed as required.

| | | December 31, 2019 | | December 31, 2018 |
|---|---|---|---|---|
| Senior Notes - Principal (7.25%) | $ | 320,000 | $ | 320,000 |
| Bank debt - Principal (6.875%) | | 30,000 | | 30,000 |
| Settlement liability (8.74%) | | 15,848 | | 16,749 |
| Lease obligation (2019 - 6.875%; 2018 - 5.2%) | | 27,098 | | 21,473 |
| Total debt | | 392,946 | | 388,222 |
| Working capital surplus | | (50,676) | | (60,782) |
| **Net debt** | **$** | **342,270** | **$** | **327,440** |

## NOTE 24 – COMMITMENTS AND CONTINGENCIES

Presented below are the Corporation's contractual commitments at December 31, 2019:

| | | Less than 1 year | | 1-3 years | | Thereafter | | Total |
|---|---|---|---|---|---|---|---|---|
| Exploration and production contracts | $ | 17,008 | $ | 29,176 | $ | 4,781 | $ | 50,965 |
| Compression station operating contracts | | 2,558 | | 5,270 | | 14,125 | | 21,953 |

### Letters of Credit

At December 31, 2019, the Corporation had letters of credit outstanding totaling $76.2 million to guarantee work commitments on exploration blocks and to guarantee other contractual commitments, of which, $11.3 million relates to certain assets previously sold, which will be transferred to Arrow no later than the end of 2021.

### Exploration and Production Contracts

The Corporation has entered into a number of exploration contracts in Colombia which require the Corporation to fulfill work program commitments and issue financial guarantees related thereto. In aggregate, the Corporation has outstanding exploration commitments at December 31, 2019 of $51 million and has issued $38.6 million in financial guarantees related thereto.

### Contingencies

In the normal course of operations, the Corporation has disputes with industry participants and assessments from tax authorities for which it currently cannot determine the ultimate results. The Corporation has a policy to record contingent liabilities as they become determinable and the probability of loss is more likely than not.