



## **Condensed Interim Consolidated Financial Statements**

**For the three months ended  
March 31, 2023  
(unaudited)**

## Lycos Energy Inc.

### Condensed Interim Consolidated Statements of Financial Position

(unaudited)

(in thousands)

	Notes	March 31, 2023	December 31, 2022
<b>Assets</b>			
Current assets			
Cash		\$ 3,770	\$ 59,628
Accounts receivable	16	8,979	4,998
Due from related party		-	426
Prepaid expenses and deposits		1,541	968
Total current assets		14,290	66,020
Exploration and evaluation assets	6	1,666	755
Property, plant and equipment	4 & 7	166,678	64,797
Investment in associate	5	-	3,676
Total assets		\$ 182,634	\$ 135,248
<b>Liabilities and Shareholders' Equity</b>			
Current liabilities			
Accounts payable and accrued liabilities		\$ 19,147	\$ 9,141
Current portion of lease obligations	9	125	44
Current portion of decommissioning liabilities	8	1,000	1,000
Other obligations	4	300	-
Total current liabilities		20,572	10,185
Lease obligations	9	209	-
Decommissioning liabilities	8	28,238	16,662
Other long-term obligations	4	2,125	-
Deferred income tax	14	932	-
Total liabilities		52,076	26,847
Shareholders' equity			
Share capital	10	177,032	177,032
Contributed surplus		7,299	6,954
Deficit		(53,773)	(75,585)
Total shareholders' equity		130,558	108,401
Total liabilities and shareholders' equity		\$ 182,634	\$ 135,248

Commitments (note 17)

Subsequent events (note 16 and note 19)

See accompanying notes to the condensed interim consolidated financial statements

## Lycos Energy Inc.

### Condensed Interim Consolidated Statements of Income and Comprehensive Income

(unaudited)

*(in thousands, except per share data)*

	Notes	Three Months Ended March 31,	
		2023	2022
<b>Revenue</b>			
Petroleum and natural gas sales	12	\$ 14,843	\$ 9,497
Royalties		(1,597)	(1,193)
Petroleum and natural gas sales, net of royalties		13,246	8,304
Other income		458	51
Total revenue and other income		13,704	8,355
<b>Expenses</b>			
Operating		5,642	3,764
Blending and transportation		4,642	1,750
General and administrative		792	369
Stock-based compensation	11	213	-
Transaction costs	18	876	-
Finance expense	13	177	92
Depletion and depreciation	7	3,465	1,306
Gain on disposition		-	(185)
		15,807	7,096
Net income (loss) before investment in associate		\$ (2,103)	\$ 1,259
Gain on CDLP Acquisition	4 & 5	11,382	-
Share of profit of investment in associate	4 & 5	35	88
Income from investment in associate		\$ 11,417	\$ 88
Income before income taxes		9,314	1,347
Deferred income tax recovery	14	(12,498)	-
<b>Net income and comprehensive income</b>		<b>\$ 21,812</b>	<b>\$ 1,347</b>
<b>Net income per share</b>			
Basic	10	\$ 0.07	\$ 0.02
Diluted	10	\$ 0.06	\$ 0.02

See accompanying notes to the condensed interim consolidated financial statements

## Lycos Energy Inc.

### Condensed Interim Consolidated Statements of Changes in Shareholders' Equity

(unaudited)

*(in thousands, except share amounts)*

	Notes	Number of Common Shares	Share Capital	Contributed Surplus	Deficit	Total Equity
Balance, December 31, 2021	10	78,498,598	\$ 113,332	\$ 6,954	\$ (79,256)	\$ 41,030
Net income		-	-	-	1,347	1,347
Balance, March 31, 2022		78,498,598	\$ 113,332	\$ 6,954	\$ (77,909)	\$ 42,377
Balance, December 31, 2022	10	318,147,806	\$ 177,032	\$ 6,954	\$ (75,585)	\$ 108,401
Stock-based compensation	11	-	-	345	-	345
Net income		-	-	-	21,812	21,812
<b>Balance, March 31, 2023</b>		<b>318,147,806</b>	<b>\$ 177,032</b>	<b>\$ 7,299</b>	<b>\$ (53,773)</b>	<b>\$ 130,558</b>

*See accompanying notes to the condensed interim consolidated financial statements*

## Lycos Energy Inc.

### Condensed Interim Consolidated Statements of Cash Flows

(unaudited)

(in thousands)

		Three Months Ended	
		March 31,	
	Notes	2023	2022
<b>Operating Activities</b>			
Net income		\$ 21,812	\$ 1,347
Items not affecting cash:			
Finance expense	13	171	89
Depletion and depreciation	7	3,465	1,306
Share-based compensation	11	213	-
Gain on disposition		-	(185)
Other income		-	(43)
Gain on CDLP Acquisition	4 & 5	(11,382)	-
Share of profit of investment in associate	4 & 5	(35)	(88)
Deferred income tax recovery	14	(12,498)	-
Decommissioning expenditures	8	(107)	-
Change in non-cash operating working capital	15	(5,063)	(339)
Cash flow from (used in) operating activities		(3,424)	2,087
<b>Financing Activities</b>			
Payments on lease obligations	9	(22)	(53)
Cash flow used in financing activities		(22)	(53)
<b>Investing Activities</b>			
Capital expenditures - exploration and evaluation	6	(911)	(10)
Capital expenditures - property, plant and equipment	7	(10,776)	(481)
Acquisition through business combination	4	(50,000)	-
Proceeds on disposition		-	185
Change in non-cash investing working capital	15	9,275	265
Cash flow used in investing activities		(52,412)	(41)
Change in cash		(55,858)	1,993
Cash, beginning of period		59,628	243
Cash, end of period		\$ 3,770	\$ 2,236

See accompanying notes to the condensed interim consolidated financial statements.

## **Lycos Energy Inc.**

Notes to Unaudited Condensed Interim Consolidated Financial Statements

For the three months ended March 31, 2023, and 2022

*(Tabular amounts in thousands)*

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### **1. Corporate information**

Lycos Energy Inc. (“Lycos” or the “Company”) is a Canadian resource company engaged in the exploration for and development of petroleum and natural gas production in western Canada. The consolidated financial statements (the “financial statements”) of the Company are comprised of the accounts of Lycos, Chronos Duvernay LP, Chronos Duvernay GP Ltd., Chronos Duvernay Ltd., Chronos Duvernay MIS Ltd. and Chronos Duvernay Sub Co. Ltd., which are incorporated in Canada. Lycos is a public company existing under the Alberta Business Corporations Act with common shares listed on the TSX Venture Exchange (“TSXV”) under the symbol “LCX”.

On February 28, 2023, Lycos purchased its partner’s equity interest in the Company’s limited partnership (“the CDLP Acquisition”). The purchase price consisted of \$50.0 million cash and the grant of a 2.345% gross overriding royalty (“GORR”) to the former partner on any newly drilled wells on the acquired lands. The strategic CDLP Acquisition provides the Company with 100% working interest in certain lands and heavy oil producing wells in Lloydminster, Alberta (see note 4).

On December 12, 2022, Lycos (formerly Samoth Oilfield Inc. or “Samoth”) and Chronos Resources Ltd. (formerly “Chronos”) completed an amalgamation (the “Transaction”) pursuant to a Definitive Agreement dated November 7, 2022, between Samoth and Chronos. The amalgamation was treated as a reverse takeover transaction (“RTO”) for accounting purposes. In accordance with IFRS 3, Samoth did not meet the definition of a business for accounting purposes. Therefore, the RTO does not constitute a business combination, but instead a share-based payment to acquire Samoth’s listing status, with Chronos being the continuing entity from an accounting perspective.

On May 1, 2023, Lycos amalgamated with CDLP by way of a vertical amalgamation with Chronos Duvernay GP Ltd., Chronos Duvernay Ltd., Chronos Duvernay MIS Ltd. and Chronos Duvernay Sub Co. Ltd.

Lycos principal place of business is located at 1900, 215 – 2nd Street S.W., Calgary, Alberta and its registered office is located at 4300 Bankers Hall West, 888-3rd Street S.W. Calgary, Alberta.

### **2. Basis of preparation**

#### ***Statement of compliance***

These unaudited condensed interim financial statements have been prepared in accordance with IAS 34 – Interim Financial Reporting as issued by the International Accounting Standards Board (“IASB”). The unaudited condensed interim financial statements do not include all information required for annual financial statements and should be read in conjunction with the Company’s audited financial statements for the year ended December 31, 2022.

These unaudited condensed interim financial statements have been prepared following the same accounting policies as the Company’s audited financial statements for the year ended December 31, 2022.

The timely preparation of these financial statements requires management to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amount of assets, liabilities, income and expenses. Actual results may differ materially from these estimates. Significant judgments, estimates and assumptions made by management in these financial statements are outlined in the audited financial statements for the year ended December 31, 2022.

These unaudited condensed interim financial statements were approved and authorized for issue by the Board of Directors on May 25, 2023.

## Lycos Energy Inc.

Notes to Unaudited Condensed Interim Consolidated Financial Statements

For the three months ended March 31, 2023, and 2022

*(Tabular amounts in thousands)*

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### 3. Significant accounting policies

Except as described below, these Condensed Interim Consolidated Financial Statements as at March 31, 2023 have been prepared following the same accounting policies as the consolidated financial statements as at December 31, 2022.

#### Business combinations

The acquisition method of accounting is used to account for acquisitions of entities or assets that meet the definition of a business under IFRS. The cost of an acquisition is measured at the fair value of the assets given, equity instruments issued, and liabilities incurred or assumed at the date of acquisition.

The consideration transferred in the acquisition is generally measured at fair value, as are the identifiable net assets acquired. Any goodwill that arises is tested annually for impairment. Any gain on a bargain purchase is recognized in the Condensed Interim Consolidated Statement of Income and Comprehensive Income immediately. Transaction costs are expensed as incurred, except if related to the issue of debt or equity securities.

The consideration transferred does not include amounts related to the settlement of pre-existing relationships. Such amounts are generally recognized in the Condensed Interim Consolidated Statement of Income and Comprehensive Income.

Acquisition-related costs are recognized in earnings as incurred. Identifiable assets acquired, liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date. The excess cost of acquisition over the fair value of the identifiable assets and liabilities acquired and contingent liabilities for which a provision is provided is recorded as goodwill. If the cost of the acquisition is less than the fair value of the net assets of the entities acquired, the difference is recognized as a bargain purchase gain in the Condensed Interim Consolidated Statement of Income and Comprehensive Income. Operational results of the business acquired are included in earnings from the closing date of acquisition.

Any contingent consideration is measured at fair value at the date of acquisition. If an obligation to pay contingent consideration that meets the definition of a financial instrument is classified as equity, then it is not remeasured and settlement is accounted for within equity. Otherwise, other contingent consideration is remeasured at fair value at each reporting date and subsequent changes in the fair value of the contingent consideration are recognized in Condensed Interim Consolidated Statements of Income and Comprehensive Income.

### 4. Business combination

On February 28, 2023, Lycos purchased its partner's equity interest in the Company's limited partnership, Chronos Duvernay LP ("the CDLP Acquisition"). The purchase price consisted of \$50.0 million cash and the grant of a 2.345% gross overriding royalty ("GORR") to the former partner on any newly drilled wells on the acquired lands. The cash consideration was funded by existing cash on hand.

This transaction was accounted for as a business combination through a step acquisition in accordance with IFRS 3. Accordingly, the Company remeasured its investment in CDLP immediately before the acquisition date. The fair value of net assets acquired was estimated at \$67.5 million (or \$14.8 million for the Company's 21.85% share in CDLP), resulting in a gain of \$11.4 million when compared to the carrying value of the investment of \$3.7 million (including the \$0.3 million unrecognized portion of transaction costs). Lycos and CDLP were subsequently amalgamated on May 1, 2023.

The acquisition complements Lycos' existing heavy oil asset base in the Lloydminster area. The operations from the acquisition have been included in the results of Lycos commencing February 28, 2023.

Lycos incurred transaction costs of \$0.8 million on the acquisition which were expensed through the Condensed Interim Consolidated Statements of Income and Comprehensive Income.

The Company assessed the acquisition and determined it constitutes a business combination in

## Lycos Energy Inc.

Notes to Unaudited Condensed Interim Consolidated Financial Statements

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(Tabular amounts in thousands)

accordance with IFRS 3. The table below summarizes the identifiable assets acquired and liabilities assumed.

The purchase price, based on management's estimates of fair values and subject to change, is as follows:

Consideration	Note		
Cash		\$	50,000
Investment in associate	5		15,093
GORR <sup>(1)</sup>			2,425
<b>Total consideration paid</b>		<b>\$</b>	<b>67,518</b>

  

Fair value of net assets acquired	Notes		
Property, plant and equipment	7	\$	90,344
Deferred income tax liability	14		(13,430)
Decommissioning liabilities <sup>(2)</sup>	8		(7,730)
Working capital	15		(1,666)
<b>Fair value of net assets acquired</b>		<b>\$</b>	<b>67,518</b>

<sup>(1)</sup> The private equity firm retained a 2.345% GORR on any newly drilled wells on the acquired lands. The Company has included \$2.4 million as contingent consideration related to the GORR, which represents fair value as at the date of acquisition. The GORR is recorded in other obligations and other long-term obligations on the Condensed Interim Consolidated Statement of Financial Position.

<sup>(2)</sup> The decommissioning liabilities acquired in the business combination were initially recognized using a credit adjusted risk free discount rate in calculating fair value. They were subsequently revalued using the risk-free rate resulting in a change in estimate with the offset recorded to property, plant and equipment (note 8).

The fair value of acquired property, plant and equipment and GORR was determined based on internally prepared estimates of proved and probable petroleum and natural gas reserves discounted at rates that range from 12%-40% and 9%-20%, respectively. Petroleum and natural gas revenue of \$5.2 million and net income of \$0.5 million are included in the Consolidated Statement of Income and Comprehensive Income for the CDLP acquisition since the closing date of February 28, 2023.

If the CDLP acquisition had occurred on January 1, 2023, the Company's pro forma results of petroleum and natural gas revenue and net income and comprehensive income for the period ended March 31, 2023 are estimated to have been as follows:

For the period ended March 31, 2023	As stated	CDLP prior to February 28, 2023 <sup>(1)</sup>	Pro forma
Petroleum and natural gas revenue	\$ 14,843	\$ 4,858	\$ 19,701
Net income and comprehensive income	\$ 21,812	\$ 126	\$ 21,938

<sup>(1)</sup> The net income and comprehensive income was offset by two months of share of profit in CDLP.

### 5. Investment in associate

On June 14, 2018, the Company entered into a partnership and financing arrangement with a private equity firm for the development of the Company's land base in the East Duvernay Shale Basin in Alberta, and subsequently the Lloydminster area of Alberta. At closing, Chronos contributed undeveloped Duvernay properties into Chronos Duvernay LP ("the Partnership") and the private equity firm contributed cash, each in return for an equity investment in the Partnership.

The financing arrangement is comprised of an equity line of credit pursuant to which the private equity firm may invest, on a capital call basis, from time to time, up to \$100 million in consideration of additional equity of the Partnership.

The cash contributed by the private equity firm on closing represented the first capital contribution under the initial tranche of capital to be invested under the equity line of credit. Exploration and development activities on the East Duvernay Shale Basin assets are to be funded with the cash contributed by the



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(Tabular amounts in thousands)

private equity firm under the equity line of credit.

In 2018, the Company shared joint control with the private equity firm and the resulting joint arrangement was classified as a Joint Venture under IFRS 11 and was required to be accounted for using the equity method of accounting. The investment was initially recorded at the cost of the undeveloped land disposed and related expenses and the subsequent carrying amount is increased or decreased by the Company's share of Consolidated Statement of Income and Comprehensive Income.

In 2019, the private equity firm contributed additional cash in exchange for additional equity, reducing Chronos working interest in the Partnership to lower than 50 percent. As such, the Company was reduced from joint control to significant influence over the investment and continued using the equity method of accounting.

In 2023 and 2022, the private equity firm did not contribute any additional cash in exchange for additional equity interest in the Partnership.

On February 28, 2023, Lycos acquired the remaining 78.15% interest in the Partnership (see note 4).

Summarized below is the financial information of Chronos Duvernay LP.

	Note	February 28, 2023	December 31, 2022
Current assets		\$ 3,659	\$ 3,801
Non-current assets		90,344	29,092
Current liabilities		(5,325)	(5,882)
Non-current liabilities		(21,160)	(11,750)
Net assets		\$ 67,518	\$ 15,261
Share of associate (percentage)		21.85%	21.85%
Share of net assets		\$ 14,752	\$ 3,335
Unrecognized portion of transaction costs <sup>(1)</sup>		341	341
Investment in associate before acquisition		15,093	3,676
Derecognition of investment in associate	4	(15,093)	-
Investment in associate		\$ -	\$ 3,676

<sup>(1)</sup> The amount represented transaction costs incurred in 2018 and 2019 on the financing of the Partnership that are not included in the net assets of the associate.

<b>Results of Operations</b>		February 28, 2023	December 31, 2022
Revenues		\$ 4,858	\$ 24,125
Expenses		(3,624)	(30,325)
Depletion		(1,073)	(4,451)
Net income (loss)		\$ 161	\$ (10,651)
Share of investment in associate (weighted average percentage)		21.85%	21.8%
Share of profit (loss) of investment in associate		\$ 35	\$ (2,327)

## Lycos Energy Inc.

Notes to Unaudited Condensed Interim Consolidated Financial Statements

For the three months ended March 31, 2023, and 2022

(Tabular amounts in thousands)

The Company's carrying amount of the investment in associate is as follows:

Investment in associate, December 31, 2021	Note	\$	6,931
Share of net loss from investment in associate			(2,327)
Adjustment related to Class D unit distribution <sup>(1)</sup>			(928)
Investment in associate, December 31, 2022		\$	3,676
Share of net income from investment in associate			35
Gain on previously held investment in associate recognized in Consolidated Statement of Income and Comprehensive Income			11,382
Derecognition of investment in associate	4		(15,093)
<b>Investment in associate, February 28, 2023</b>		<b>\$</b>	<b>-</b>

<sup>(2)</sup> During 2022, the Partnership paid a distribution of \$4.2 million to the class D unitholders which are held with the private equity firm.

### 6. Exploration and evaluation assets

The following table reconciles the movements of the Company's Exploration and evaluation ("E&E") assets for the periods:

		March 31, 2023	December 31, 2022
Balance, beginning of period	\$	755	\$ 755
Additions		911	\$ -
Balance, end of period	\$	1,666	\$ 755

E&E assets consist of the Company's undeveloped land and exploration projects which are pending the determination of proved and probable petroleum and natural gas reserves. Additions represent the Company's share of the cost of E&E assets.

At March 31, 2023, \$1.7 million (December 31, 2022 - \$0.8 million) remained in E&E assets. The Company does not amortize its E&E assets.

#### Impairment

The Company concluded there are no indicators of impairment for its E&E assets as at March 31, 2023.

### 7. Property, plant and equipment

A reconciliation of the carrying value of property, plant and equipment as at March 31, 2023, and December 31, 2022 is set out below:

## Lycos Energy Inc.

Notes to Unaudited Condensed Interim Consolidated Financial Statements

For the three months ended March 31, 2023, and 2022

(Tabular amounts in thousands)

<b>Cost</b>	<b>Notes</b>	<b>Total Property, plant and equipment</b>
Balance, December 31, 2021		\$ 113,993
Additions		10,091
Disposal of right-of-use asset		(499)
Changes in decommissioning liabilities	8	(3,000)
Balance, December 31, 2022		\$ 120,585
Additions		10,776
Acquisition through business combination	4	90,344
Right of use assets	9	318
Disposal of right-of-use asset		(47)
Changes in decommissioning liabilities	8	3,791
Capitalized stock-based compensation	11	132
<b>Balance, March 31, 2023</b>		<b>\$ 225,899</b>
<b>Accumulated depletion, depreciation and impairment</b>		
Balance, December 31, 2021		\$ 58,675
Depletion and depreciation		6,386
Impairment reversal		(8,922)
Disposal of right-of-use asset		(351)
Balance, December 31, 2022		\$ 55,788
Depletion and depreciation		3,465
Disposal of right-of-use asset		(32)
<b>Balance, March 31, 2023</b>		<b>\$ 59,221</b>
Net carrying value:		
December 31, 2022		\$ 64,797
<b>March 31, 2023</b>		<b>\$ 166,678</b>

The Company capitalized \$0.4 million (December 31, 2022 - \$0.7 million) of general and administrative costs and \$0.1 million (December 31, 2022 - \$nil million) of stock-based compensation for the period ended March 31, 2023.

### Impairment

The Company concluded there are no indicators of impairment or impairment reversal for its CGUs as at March 31, 2023.

At December 31, 2022, the Company conducted an assessment of indicators of impairment or impairment reversal for the Company's CGUs. In performing the assessment, management determined an impairment or impairment reversal trigger existed for the southwest Saskatchewan CGU and therefore conducted an impairment test. At December 31, 2022, there were no indicators of impairment for the Lloydminster Saskatchewan CGU.

The recoverable amount of the southwest Saskatchewan CGU were estimated using value in use based on the net present value of before tax cash flows from proved and probable petroleum and natural gas reserves estimated by the Company's independent third-party reserve evaluators discounted at rates ranging from 12 to 25 percent. In determining the appropriate discount rates, the Company referenced recent market transactions completed on assets similar to those in the CGU.

At December 31, 2022, the Company determined the recoverable amount of the southwest Saskatchewan CGU was \$41.5 million. Accordingly, an aggregate impairment reversal of \$8.9 million

## Lycos Energy Inc.

Notes to Unaudited Condensed Interim Consolidated Financial Statements

For the three months ended March 31, 2023, and 2022

(Tabular amounts in thousands)

was recorded for the year ended December 31, 2022.

The following table outlines forecasted commodity prices and exchange rates used in the Company's impairment reversal test as at December 31, 2022. The forecasted commodity prices are consistent with those used by the Company's independent third-party reserve evaluators and are a key assumption in assessing recoverable amount. The independent third-party reserve evaluators also include financial assumptions regarding royalty rates, operating costs, and future development capital that can significantly impact the recoverable amount which is assigned based on historical rates and future anticipated activities by management.

	WTI Price - Oil (US\$/bbl) <sup>(1)</sup>	WCS Price - Oil (\$/bbl)	AECO Price - Gas (\$/MMBtu) <sup>(1)</sup>	Exchange Rate (\$Cdn/\$US)
2023	86.00	88.00	4.33	0.75
2024	84.00	89.38	4.34	0.80
2025	80.00	84.06	4.00	0.80
2026	81.60	85.74	4.08	0.80
2027	83.23	87.46	4.16	0.80
2028	84.90	89.21	4.24	0.80
2029	86.59	90.99	4.33	0.80
2030	88.33	92.81	4.42	0.80
2031	90.09	94.67	4.50	0.80
2032	91.89	96.56	4.59	0.80

Escalation rate of 2% per year thereafter

<sup>(1)</sup> The forecast benchmark commodity prices listed are adjusted for quality differentials, heat content, transportation and marketing costs and other factors specific to the Company's operations in performing the Company's impairment test.

## 8. Decommissioning liabilities

The Company's decommissioning obligations result from net ownership interests in petroleum and natural gas assets including well sites, gathering systems and processing facilities. A risk-free rate of 3.02% (2022 – 3.28%) and an inflation rate of 1.68% (2022 – 2.09%) was used to calculate the decommissioning liabilities.

	Note	March 31, 2023	December 31, 2022
Balance, beginning of period		\$ 17,662	\$ 20,716
Change in estimates <sup>(1)</sup>		(378)	(3,272)
Additions		187	101
Decommissioning expenditures	16	(107)	(28)
Liabilitied acquired on CDLP acquisition and RTO <sup>(2)</sup>	4	7,730	92
Revaluation of liabilities incurred <sup>(3)</sup>		3,982	79
Liabilities settled by government grants		-	(503)
Accretion	13	162	477
Balance, end of period		\$ 29,238	\$ 17,662
Expected to be incurred within one year		\$ 1,000	\$ 1,000
Expected to be incurred beyond one year		\$ 28,238	\$ 16,662

<sup>(1)</sup> The change in estimates in 2023 is due to a change in estimated abandonment and remediation cost of \$nil (December 31, 2022 - \$0.2 million) and change in discount and inflation rates totaling \$(0.3) million (December 31, 2022 - \$(3.2) million).

<sup>(2)</sup> The amount represents the decommissioning liability incurred in the CDLP acquisition (note 4) and RTO in 2022.

<sup>(3)</sup> The decommissioning liabilities acquired in the CDLP acquisition (note 4) and assumed in the RTO were initially recognized using a credit adjusted risk free discount rate in calculating fair value. They were subsequently revalued using the risk-free rate resulting in a change in estimate with the offset recorded to property, plant and equipment.

## Lycos Energy Inc.

Notes to Unaudited Condensed Interim Consolidated Financial Statements

For the three months ended March 31, 2023, and 2022

(Tabular amounts in thousands)

### 9. Lease obligations

	Note	March 31, 2023	December 31, 2022
Balance, beginning of period		44	\$ 182
Additions	7	318	-
Disposal		(15)	(87)
Interest expense	13	9	2
Payments		(22)	(53)
Balance, end of period		\$ 334	\$ 44
Current		125	44
Non-current		209	-
		\$ 334	\$ 44

On November 24, 2022, Lycos entered into a head office sublease agreement for a period of two years and eight months resulting in the recognition of a \$0.2 million right-of-use asset and lease obligation. The Company took possession on January 1, 2023. The Company is obligated to pay basic rent of approximately \$94 thousand per year. In addition, during the period ended March 31, 2023, the Company has recognized \$0.1 million in the right-of-use asset and lease obligation related to field trucks.

### 10. Share capital

#### (a) Authorized

The Company's authorized share capital consists of an unlimited number of common voting shares and an unlimited number of preferred shares, issuable in series.

#### (b) Issued and outstanding common shares

The following table summarizes the Company's issued and outstanding common shares for the periods:

	March 31, 2023		March 31, 2022	
	Number of Shares	Amount	Number of Shares	Amount
Balance, beginning of period	318,147,806	\$ 177,032	78,498,598	\$ 113,332
<b>Balance, end of period</b>	<b>318,147,806</b>	<b>\$ 177,032</b>	<b>78,498,598</b>	<b>\$ 113,332</b>

### Warrants

	Number of Warrants	
	March 31, 2023	December 31, 2022
Balance, beginning of period	45,650,000	-
Issued	-	45,650,000
<b>Balance, end of period</b>	<b>45,650,000</b>	<b>45,650,000</b>

On December 12, 2022, the Company issued 45,650,000 warrants in connection with the RTO transaction in 2022 which were recorded in share capital.

	Warrants outstanding			Warrants exercisable		
	Number outstanding	Weighted average exercise price	Weighted average life remaining (years)	Number outstanding	Weighted average exercise price	Weighted average life remaining (years)
<b>Balance, end of period</b>	<b>45,650,000</b>	<b>\$ 0.28</b>	<b>4.8</b>	<b>45,650,000</b>	<b>\$ 0.28</b>	<b>4.8</b>

## Lycos Energy Inc.

Notes to Unaudited Condensed Interim Consolidated Financial Statements  
For the three months ended March 31, 2023, and 2022  
(Tabular amounts in thousands)

### (c) Per share amounts

The following table summarizes the shares used in calculating net income per share:

	March 31, 2023	March 31, 2022
Weighted average number of shares - basic	318,147,806	78,498,598
Effect of dilutive securities	20,255,298	-
Weighted average number of shares - diluted	338,403,104	78,498,598

In computing diluted per share amounts at March 31, 2023, 45,650,000 (2022 – nil) warrants were included in the calculation and 15,935,000 (2022 – nil) stock options (note 11) were excluded from the calculation as their effect was anti-dilutive.

At March 31, 2022, there were no warrants or stock options.

## 11. Share-based compensation

The Company established a share option plan for its directors, officers, employees, and certain consultants under which the Company may grant options to acquire a maximum number of common shares equal to 10% of the total issued and outstanding common shares of the Company.

On January 25, 2023, Lycos granted 15,935,000 stock options to certain employees, directors, and officers. The stock options expire five years from the date of grant and are exercisable at a price of \$0.55 per common share. The options vest as to one-third on each of the first, second and third anniversary of the grant date.

There were no options granted in 2022. The total fair value of each option granted during the period ended March 31, 2023 was estimated on the date of grant using the Black-Scholes pricing model with weighted average assumptions as follows:

	March 31, 2023
Weighted average fair value of options granted	\$ 0.39
Risk-free interest rate	2.88%
Expected life years	5
Expected volatility <sup>(1)</sup>	89.94%

<sup>(1)</sup> During the period ended March 31, 2023, the expected volatility was estimated based on a peer group historical volatility.

The range of exercise price of stock options outstanding and exercisable as at March 31, 2023, is as follows:

Outstanding options			
Exercise price	Number of Options Outstanding	Weighted average remaining term (years)	Weighted average exercise price
\$ 0.55	15,935,000	4.8	\$ 0.55

At March 31, 2023, there are no exercisable options.

During the three months ended March 31, 2023, the Company recorded gross stock-based compensation expense of \$0.2 million (March 31, 2022 - \$nil million) and capitalized stock-based compensation expense of \$0.1 million (March 31, 2022 - \$nil million) for stock options granted.

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(Tabular amounts in thousands)

### 12. Revenue

The Company sells its production pursuant to fixed or variable-price contracts. The transaction price for variable priced contracts is based on the commodity price, adjusted for quality, location or other factors, whereby each component of the pricing formula can be either fixed or variable, depending on the contract terms. Under the contracts, the Company is required to deliver a fixed or variable volume of crude oil, condensate, natural gas or natural gas liquids to the customer. Revenue is recognized when a unit of production is delivered to the customer.

The amount of revenue recognized is based on the agreed transaction price, whereby any variability in revenue relates specifically to the Company's efforts to transfer production, and therefore the resulting revenue is allocated to the production delivered in the period during which the variability occurs. As a result, none of the variable revenue is considered constrained.

Crude oil and natural gas are sold under contracts of varying terms of up to one year. Revenues are typically collected on the 25th day of the month following production.

The following table summarizes the Company's petroleum and natural gas sales, all of which are from revenue with contracts with customers:

	<b>March 31, 2023</b>	March 31, 2022
Crude oil	\$ 14,330	\$ 9,058
Natural gas	31	18
Petroleum and natural gas revenues	<b>14,361</b>	9,076
Processing income	<b>482</b>	421
Total petroleum and natural gas sales	<b>\$ 14,843</b>	\$ 9,497

Included in accounts receivable as at March 31, 2023, is \$8.2 million (December 31, 2022 - \$3.7 million) of accrued crude oil and natural gas sales related to March 2023 production.

### 13. Finance expense

	Note	<b>March 31, 2023</b>	March 31, 2022
Accretion on decommissioning liabilities	8	\$ 162	\$ 87
Interest expense		6	3
Interest on lease obligations	9	9	2
		<b>\$ 177</b>	\$ 92

### 14. Income tax

#### (i) Deferred income tax recovery

The provision for future tax in the financial statements differs from the result, which would have been obtained by applying the combined federal and provincial tax rate to the Company's net income. This difference results from the following items:

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	<b>March 31, 2023</b>	March 31, 2022
Net income before taxes	\$ 9,314	\$ 1,347
Combined federal and provincial rate	<b>25.01%</b>	25.37%
Computed "expected" income tax expense	<b>2,329</b>	342
Increase (decrease) in income tax resulting from:		
Non-deductible expense	<b>236</b>	-
Rate change and other	<b>(3,564)</b>	-
Change in unrecognized DTA	<b>(11,499)</b>	(342)
Income tax recovery	<b>\$ (12,498)</b>	\$ -

### (ii) Deferred income tax liability

The components of the Company's recognized deferred income tax liability are as follows:

	<b>March 31, 2023</b>	December 31, 2022
Deferred income tax liabilities:		
Property, plant and equipment	\$ (28,828)	\$ (8,309)
Investment in associate	-	(933)
Deferred income tax assets:		
Decommissioning liabilities	<b>7,435</b>	4,481
Non-capital losses	<b>19,868</b>	4,058
Share Issue costs	<b>510</b>	690
Lease obligation	<b>83</b>	11
Others	-	2
Deferred income tax liability:	<b>\$ (932)</b>	\$ -

At March 31, 2023, the company has \$79.4 million (December 31, 2022 - \$61.3 million) in non-capital losses that will begin to expire in 2032.

The following table provides a continuity of the deferred income tax liability:

	December 31, 2022	Recognized in Consolidated Statement of Income and Comprehensive Income	Acquired in a business combination (note 4)	<b>March 31, 2023</b>
Property, plant and equipment	\$ -	\$ (10,938)	\$ (17,890)	<b>\$ (28,828)</b>
Decommissioning liabilities	-	5,501	1,934	<b>7,435</b>
Non-capital losses	-	17,342	2,526	<b>19,868</b>
Share Issue costs	-	510	-	<b>510</b>
Lease obligation	-	83	-	<b>83</b>
Deferred income tax liability	<b>\$ -</b>	<b>\$ 12,498</b>	<b>\$ (13,430)</b>	<b>\$ (932)</b>



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The components of the Company's unrecognized deductible temporary differences are as follows:

	March 31, 2023	December 31, 2022
Non-capital losses	\$ -	\$ 45,327
Deferred income tax asset	\$ -	\$ 45,327

### 15. Supplementary cash flow information

The following table details the changes in non-cash working capital.

	Note	March 31, 2023	March 31, 2022
Accounts receivable		\$ (3,981)	(640)
Due from related party		426	511
Prepaid expenses and deposits		(573)	(161)
Accounts payable and accrued liabilities		10,006	216
Working capital assumed on CDLP acquisition <sup>(1)</sup>	4	(1,666)	-
		\$ 4,212	\$ (74)
Relating to:			
Operating activities		\$ (5,063)	\$ (339)
Investing activities		9,275	265
		\$ 4,212	\$ (74)

<sup>(1)</sup> The amount represents the working capital acquired on the CDLP acquisition (note 4)

### 16. Financial instruments

The Company has exposure to credit and liquidity risks from its financial assets and liabilities and exposure to market risks relating to commodity prices, interest rates and foreign exchange rates. This note presents information about the Company's exposure to these risks, the Company's objectives, policies and processes for measuring and managing risk, and the Company's management of capital.

Further quantitative disclosures are included throughout these Condensed Interim Consolidated Financial Statements.

The Board of Directors has overall responsibility for the establishment and oversight of the Company's risk management framework. The Board of Directors has implemented and monitors compliance with risk management policies.

The Company's risk management policies are established to identify and analyze the risks faced by the Company, to set appropriate risk limits and controls, and to monitor risks and adherence to market conditions and the Company's activities.

#### Market risk

Market risk is the risk that changes in market prices, such as commodity prices for crude oil and natural gas, foreign exchange rates and interest rates will affect the Company's valuation of financial instruments, the debt levels of the Company, as well as its income and cash flow from operations.

The objective of market risk management is to manage and control market risk exposures within acceptable parameters, while maximizing the Company's returns. All such transactions are conducted in accordance with the Company's risk management policy that has been approved by the Board of Directors.

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### Commodity price risk

Commodity price risk is the risk that the fair value of future cash flows will fluctuate as a result of changes in commodity prices. Commodity prices for petroleum and natural gas are impacted by the relationship between the Canadian and United States dollar and also world economic events that dictate the levels of supply and demand. The Company may utilize both financial derivatives and physical delivery contracts to manage commodity price risks in accordance with the Company's expected sale requirements.

Fixed price physical delivery contracts that were entered into by the Company continue to be held for the purpose of the receipt or delivery of a non-financial item in accordance with the Company's expected purchase, sale or usage requirements which meets 'own use exemption'. These contracts are accounted for as executory contracts and are not considered financial instruments; therefore, no asset or liability has been recognized in the financial statements. As at March 31, 2023, no financial derivative contracts have been entered into however the Company had the following fixed price physical sales contracts:

Option Traded	Term	Volume	Price/Unit
WCS	May 1, 2023 to May 31, 2023	500 bbl/d	CAD \$77.00
WCS	June 1, 2023 to June 30, 2023	250 bbl/d	CAD \$77.15
WCS	June 1, 2023 to June 30, 2023	250 bbl/d	CAD \$80.25
WCS	January 1, 2023 to December 31, 2023	9,000 bbl/month	US \$45.25
LLK (Lloyd Kerrobert) <sup>(1)</sup>	January 1, 2023 to December 31, 2023	200 bbl/d	CAD \$90.50

<sup>(1)</sup> Subsequent to the quarter end, the Company cancelled the LLK fixed price contract from August 2023 to December 2023 for \$0.5 million.

### Interest rate risk

The Company is exposed to interest rate risk on cash balances to the extent of changes in market interest rates. As at March 31, 2023 the Company had no interest rate swap or derivative contracts in place.

### Foreign exchange risk

Foreign exchange risk arises from changes in foreign exchange rates that may affect the fair value or future cash flows of the Company's financial assets or liabilities. The Company is exposed to foreign exchange risk in relation to its crude oil sales. As at March 31, 2023, the Company had no foreign exchange swap or derivative contracts in place.

### Credit risk

Credit risk is the risk of financial loss to the Company if a customer or counterparty to a financial instrument fails to meet its contractual obligations and arises principally from the Company's receivables from purchasers of the Company's petroleum and natural gas and counterparties to cash joint venture partners and the counterparties to risk management contracts.

As at March 31, 2023, the Company's receivables consisted of \$8.2 million from petroleum and natural gas purchasers and \$0.7 million other receivables. The Company's cash is deposited in high yield saving accounts with financial institutions and are subject to counterparty credit risk. The Company mitigates this risk by only transacting with investment grade financial institutions with high credit ratings.

During the three months ended March 31, 2023, the Company sold its crude oil and natural gas production to various counterparties with one counterparty accounting for 93% of sales (March 31, 2022 one counterparty accounted for 72% of sales). Receivables from purchasers of the Company's petroleum and natural gas are normally collected on the 25th day of the month following shipment. The Company's policy to mitigate credit risk associated with these balances is to establish marketing relationships with large, credit worthy petroleum marketers.

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Financial derivative contracts are only entered into with credit worthy institutions. Joint venture receivables are typically collected within one to four months of the joint venture bill being issued to the partner.

The Company attempts to mitigate the risk from joint venture receivables by obtaining partner approval of significant capital expenditures prior to commencement of the joint venture project and smaller partners are cash called to pay for their share of costs in advance of a project commencing. However, the receivables are from participants in the petroleum and natural gas sector, and collection of the outstanding balances is dependent on industry factors such as commodity price fluctuations, escalating costs and the risk of unsuccessful drilling. In addition, further risk exists with joint venture partners as disagreements occasionally arise that increase the potential for non-collection.

To offset this risk, the Company often has the ability to withhold production from joint venture partners in the event of non-payment.

The carrying amount of accounts receivable and due from related party represents the maximum credit exposure. The Company has calculated the expected credit losses using the simplified approach which permits the use of the lifetime expected loss provision. To assess the expected credit loss, the Company uses historical information and forward-looking information. No loss provision was recorded for the three months ended March 31, 2023. Historically, there was no indication that amounts were non-collectable thus, an allowance for doubtful accounts was not set up.

As at March 31, 2023, and December 2022 the Company's accounts receivables are aged as follows:

Period ended	Total Receivables	< 90 Days	Past Due
<b>March 31, 2023</b>	<b>\$ 8,979</b>	<b>\$ 8,230</b>	<b>\$ 749</b>
	<b>100%</b>	<b>92%</b>	<b>8%</b>
December 31, 2022	\$ 4,998	\$ 4,327	\$ 671
	100%	87%	13%

Fair value of financial instruments:

The Company classifies the fair value of these transactions according to the following hierarchy based on the amount of observable inputs used to value the instrument.

- Level 1 – Quoted prices are available in active markets for identical assets or liabilities as of the reporting date. Active markets are those in which transactions occur in sufficient frequency and volume to provide pricing information on an ongoing basis.
- Level 2 – Pricing inputs are other than quoted prices in active markets included in Level 1. Prices are either directly or indirectly observable as of the reporting date. Level 2 valuations are based on inputs, including quoted forward 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 Company's exposure under its financial instruments is limited to financial assets and liabilities, all of which are included in these financial statements. The carrying value of cash, accounts receivable, and accounts payable and accrued liabilities included in the Consolidated Statement of Financial Position approximate fair value due to the short-term nature of those instruments or the indexed rate of interest.

### (i) Level 3 fair value

On February 28, 2023, the Company recorded contingent GORR consideration of \$2.4 million assumed in the CDLP Acquisition (note 4). There was no significant change in fair value or in the significant unobservable inputs from February 28, 2023 to March 31, 2023.

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### Liquidity risk

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they are due. The Company manages liquidity risk through cash and debt management strategies to mitigate the likelihood of encountering difficulties in meeting its financial obligations. Such strategies include an actively managed operating and capital expenditure budgeting process, authorizations for expenditures on both operated and non-operated projects to further manage capital expenditures, and the Company also attempts to match its payment cycle with collection of petroleum and natural gas revenues on the 25th of each month. The Company entered into a credit facility in the first quarter of 2023 to further strengthen its liquidity (discussed below).

The Company's objectives when managing capital are to i) deploy capital to provide an appropriate return on investment to its shareholders; ii) maintain financial flexibility in order to preserve the Company's ability to meet financial obligations; and iii) maintain a capital structure that provides financial flexibility to execute strategic acquisitions. To aid in managing the capital structure, the Company monitors adjusted working capital (net debt) and adjusted funds flow from operations.

The Company's strategy is designed to maintain a flexible capital structure consistent with the objectives as stated above and to respond to changes in economic conditions and the risk characteristics of the underlying crude oil assets. Key indicators of changing economic conditions include adjusted working capital (net debt) and adjusted funds flow from operations. Lycos considers its capital structure to include shareholders' equity and working capital (net debt). In order to maintain or adjust its capital structure, the Company may from time to time issue new common shares, seek debt financing and adjust its capital spending to manage working capital.

The following are the contractual maturities of financial obligations and associated interest payments as at March 31, 2023:

	Less than 1 year	1 to 2 years	Thereafter	Total
Accounts payable and accrued liabilities	\$ 19,147	\$ -	\$ -	\$ 19,147
Other obligations	\$ 300	\$ 569	\$ 1,556	\$ 2,425
Lease obligations	\$ 125	\$ 207	\$ 2	\$ 334

### Credit facility

During the first quarter of 2023, the Company entered into an agreement with the National Bank of Canada ("the Lender") providing for an uncommitted demand revolving credit facilities for up to \$20 million, of which \$10.0 million is immediately available for general corporate purposes and additional \$10.0 million is available at the discretion of the Lender.

As at March 31, 2023, Lycos had not drawn on the credit facilities.

The credit facilities are secured by a demand debenture in the amount of \$100.0 million. The Company is subject to a financial covenant whereby the Company's ratio of adjusted working capital, including any undrawn availability under the revolving facility as a current asset, shall not be less than 1.00:1.00. Repayments of principal are not required until the Lender demands, provided that the borrowings do not exceed the authorized credit facility and the Company is in compliance with all covenants, representations and warranties.

On May 24, 2023, Lycos entered into its first amending agreement with the Lender, increasing the revolving credit facility from \$20.0 million to \$35.0 million. The next borrowing base review is expected to be completed on or about November 30, 2023.

### Capital management

The Company manages its capital structure and makes adjustments by continually monitoring its business conditions, including changes in economic conditions and resulting changes in capital markets, the current and forecasted net debt levels, the forecasted commodity prices and resulting cash flow from operations and adjusted funds flow from operations, adjusted working capital, and capital expenditures.

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The Company prepares annual capital expenditure budgets and longer term plans, which are continually monitored and updated as necessary depending on varying factors including current and forecast commodity prices, earning and expiry commitments, weather and access restrictions, and project investment risk return profile. The annual and updated budgets are approved by the Board of Directors. The Company will adjust its capital structure through issuance of shares and make adjustments to capital spending to balance the capital structure. The Board of Directors does not establish quantitative return on capital targets for management, but rather relies on the expertise of the Company's management to sustain future development of the business.

### i) Adjusted funds flow from operations:

Management considers adjusted funds flow from operations to be a key measure to assess the performance of the Company's oil and gas properties and the Company's ability to fund future capital investment. Adjusted funds flow from operations is an indicator of operating performance as it varies in response to production levels and management of costs.

Changes in non-cash working capital, decommissioning costs incurred and transaction costs vary from period to period and Management believes that excluding the impact of these provides a useful measure of Lycos' ability to generate the funds necessary to manage the capital needs of the Company.

	Notes	March 31, 2023	March 31, 2022
Cash flow from operating activities		\$ (3,424)	\$ 2,087
Changes in non-cash working capital		5,063	339
Funds flow from operations		1,639	2,426
Decommissioning costs incurred	8	107	-
Transaction costs	18	876	-
Adjusted funds flow from operations		\$ 2,622	\$ 2,426

### ii) Adjusted working capital (net debt):

Management considers adjusted working capital to be a key measure to assess the Company's liquidity and capital management. The Company believes its presentation of adjusted working capital (net debt) is a useful supplemental measure because Management maintains the flexibility to adjust its decommissioning expenditures to manage working capital requirements and the current portion of other obligations relates to contractual obligations for future production periods and are included in Lycos' reported adjusted funds flow from operations in the production month to which the obligation relates.

	March 31, 2023	December 31, 2022
Working capital	\$ (6,282)	\$ 55,835
Current portion of decommissioning liabilities	1,000	1,000
Other obligations	300	-
Adjusted working capital (net debt)	\$ (4,982)	\$ 56,835

The following table reconciles the movements of the Company's capital structure for the periods:

	March 31, 2023	December 31, 2022
Adjusted working capital	\$ (4,982)	56,835
Shareholders' equity	\$ 130,558	\$ 108,401

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### iii) Total capital expenditures:

Management considers total capital expenditures to be a key measure to assess the Company's capital investment in exploration and production activity, as well as property acquisitions and dispositions:

	March 31, 2023	March 31, 2022
Net cash used in investing activities	\$ 52,412	\$ 41
Change in non-cash working capital	9,275	265
<b>Total capital expenditures</b>	<b>\$ 61,687</b>	<b>\$ 306</b>

### 17. Commitments

Future minimum payments relating to variable office rent payments, which are a non-lease component of the Company's head office sublease, as at March 31, 2023 are as follows:

	March 31, 2023
Less than 1 year	\$ 528
1-2 years	1,008
<b>Total commitments</b>	<b>\$ 1,536</b>

The variable office rent payments will be recorded to general and administrative expense in the period in which incurred.

### 18. Transaction costs

The following table presents the Company's transaction costs:

	Note	March 31, 2023	March 31, 2022
Transaction costs related to acquisitions	4	\$ 777	\$ -
Transaction costs related to credit facilities		99	-
		<b>\$ 876</b>	<b>\$ -</b>

### 19. Subsequent events

- 1) On May 15, 2023, Lycos granted 1,140,000 stock options to certain employees. The stock options expire five years from the date of grant and are exercisable at a price of \$0.45 per common share. The options vest as to one-third on each of the first, second and third anniversary of the grant date.
- 2) Subsequent to March 31, 2023, the Company entered into the following financial derivative contracts.

Option Traded	Term	Volume	Price/Unit
WCS	June 1, 2023 to June 30, 2023	250 bbl/d	CAD \$87.30
WCS	July 1, 2023 to September 30, 2023	250 bbl/d	CAD \$85.35
WCS Differential	July 1, 2023 to September 30, 2023	500 bbl/d	CAD \$(19.00)