AVANTI ENERGY INC.

Condensed Consolidated Interim Financial Statements

For the three and six months ended June 30, 2014 and 2013

(Expressed in Canadian Dollars)

**NOTICE OF NO AUDIT OR REVIEW OF INTERIM FINANCIAL STATEMENTS**

Under National Instrument 51-102, Part 4, subsection 4.3(3)(a), if an auditor has not performed a review of the interim financial statements, they must be accompanied by a notice indicating that the financial statements have not been reviewed by an auditor.

The accompanying unaudited interim financial statements of the Company have been prepared by and are the responsibility of the Company's management.

The Company's independent auditor has not performed a review of these financial statements in accordance with standards established by the Canadian Institute of Chartered Accountants for a review of interim financial statements by an entity's auditor.

**AVANTI ENERGY INC.**
CONDENSED CONSOLIDATED INTERIM STATEMENTS OF FINANCIAL POSITION
**(Expressed in Canadian Dollars)**

**AS AT**

| | Note | **June 30, 2014** | December 31. 2013 |
|---|---|---|---|
| | | **$** | $ |
| **ASSETS** | | | |
| **Current assets** | | | |
| Cash and equivalents | | 1,081,026 | 275,700 |
| Accounts receivable | | 13,035 | 10,530 |
| Prepaids and deposits | ***11*** | 58,323 | 120,712 |
| **Total current assets** | | 1,152,384 | 406,942 |
| **Non-current assets** | | | |
| Property, plant and equipment | ***7*** | 172,683 | - |
| Exploration and evaluation assets | ***6*** | 47,699 | 147,658 |
| Intangible assets | ***4*** | 1,903,043 | 1,903,043 |
| Long term deposits | ***5*** | 65,363 | 65,363 |
| **Total non-current assets** | | 2,188,788 | 2,116,064 |
| **Total assets** | | 3,341,172 | 2,523,006 |
| **LIABILITIES** | | | |
| **Current liabilities** | | | |
| Accounts payable and accrued liabilities | | 45,352 | 35,078 |
| Due to related parties | ***11*** | 52,504 | 88,335 |
| **Total current liabilities** | | 97,856 | 123,413 |
| Reclamation obligation | ***6*** | 15,000 | 15,000 |
| **Total liabilities** | | 112,856 | 138,413 |
| **SHAREHOLDERS' EQUITY** | | | |
| Share capital | ***8*** | 5,934,751 | 4,244,331 |
| Equity reserves | | 600,126 | 533,871 |
| Deficit | | (3,306,561) | (2,393,609) |
| **Total shareholders' equity** | | 3,228,316 | 2,384,593 |
| **Total liabilities and equity** | | 3,341,172 | 2,523,006 |
| **Nature and continuance of operations** | ***1*** | | |
| **Events after the reporting period** | ***14*** | | |

**APPROVED AND AUTHORIZED FOR ISSUE ON BEHALF OF THE BOARD ON AUGUST 29, 2014:**

Signed: ***"John McIntyre"***
Director

Signed: ***"Douglas Ford"***
Director

*The accompanying notes form an integral part of these consolidated financial statements*

**AVANTI ENERGY INC.**
CONDENSED CONSOLIDATED INTERIM STATEMENTS OF COMPREHENSIVE LOSS
**(Expressed in Canadian Dollars)**

| | | 3 months ended June 30, | | 6 months ended June 30, | |
|---|---|---|---|---|---|
| | | **2014** | 2013 | **2014** | 2013 |
| | | $ | $ | $ | $ |
| | ***Notes*** | | | | |
| **Oil and Gas Revenues** | | **79,160** | - | **79,160** | - |
| **General and Administrative Expenses** | | | | | |
| Administrative | ***11*** | **72,946** | 23,515 | **110,439** | 26,064 |
| Consulting fees | ***11*** | **208,745** | 144,564 | **398,530** | 181,064 |
| Depletion | | **7,200** | - | **7,200** | - |
| Gain on foreign exchange | | **8,446** | (6,888) | **4,828** | (6,888) |
| Lease operating expense | | **14,804** | 7,489 | **221,568** | 7,489 |
| Management fees | ***11*** | **75,000** | - | **150,000** | - |
| Professional fees | | **35,830** | 22,704 | **43,167** | 23,886 |
| Share-based payments | ***11*** | **-** | - | **38,183** | - |
| Transfer agent and filing fees | | **8,478** | 16,895 | **18,197** | 28,155 |
| Impairment of exploration and evaluation assets | ***6*** | **-** | 191,345 | **-** | 191,345 |
| **Total Expenses** | | **431,449** | 399,624 | **992,112** | 451,115 |
| **Loss and comprehensive loss for the period** | | **(352,289)** | (399,624) | **(912,952)** | (451,115) |
| **Loss per common share -** basic and diluted | | **(0.01)** | (0.02) | **(0.02)** | (0.03) |
| **Weighted average number of common shares outstanding**<br>- basic and diluted | | **47,021,606** | 18,296,264 | **42,921,622** | 16,020,778 |

*The accompanying notes form an integral part of these consolidated financial statements*

**AVANTI ENERY INC.**
CONDENSED CONSOLIDATED INTERIM STATEMENTS OF CASH FLOWS
**(Expressed in Canadian Dollars)**

| | Notes | 3 months ended June 30, **2014** $ | 3 months ended June 30, 2013 $ | 6 months ended June 30, **2014** $ | 6 months ended June 30, 2013 $ |
|---|---|---|---|---|---|
| **OPERATING ACTIVITIES** | | | | | |
| Net loss for the period | | **(352,289)** | (399,624) | **(912,952)** | (451,115) |
| Items not affecting cash | | | | | |
| Impairment of exploration and evaluation assets | ***6*** | **-** | 191,345 | **-** | 191,345 |
| Depletion | | **7,200** | - | **7,200** | - |
| Share-based payments | | **-** | - | **38,183** | - |
| Changes in non-cash working capital items: | | | | | |
| Accounts receivable and prepaids | | **18,387** | (4,702) | **59,884** | 7,634 |
| Accounts payable and accrued liabilities | | **(37,190)** | (20,588) | **(25,557)** | (31,034) |
| **Cash used in operating activities** | | **(363,892)** | (233,569) | **(833,242)** | (283,170) |
| **INVESTING ACTIVITIES** | | | | | |
| Cash acquired upon acquisition of Avanti SA and Avanti Oil | ***4*** | **-** | 5,151 | **-** | 5,151 |
| Cash advances paid to Avanti SA | ***4*** | **-** | (430,448) | **-** | (430,448) |
| Deferred charges | | **-** | 91,555 | **-** | - |
| Property, plant and equipment additions | | **(72,424)** | - | **(72,424)** | - |
| Exploration and evaluation assets expenditures | | **(7,500)** | 304,425 | **(7,500)** | (14,900) |
| **Cash used in investing activities** | | **(79,924)** | (29,317) | **(79,924)** | (440,197) |
| **FINANCING ACTIVITIES** | | | | | |
| Common shares issued for cash | ***8*** | **89,700** | 238,800 | **1,765,787** | 238,800 |
| Share issue costs | ***8*** | **(8,563)** | - | **(47,295)** | - |
| **Cash provided by financing activities** | | **81,137** | 238,800 | **1,718,492** | 238,800 |
| **Total increase (decrease) in cash during the period** | | **(362,679)** | (24,086) | **805,326** | (484,567) |
| **Cash, beginning of period** | | **1,443,705** | 106,664 | **275,700** | 567,145 |
| **Cash, end of period** | | **1,081,026** | 82,578 | **1,081,026** | 82,578 |
| **Cash paid for:** | | | | | |
| Interest | | **-** | - | **-** | - |
| Income taxes | | **-** | - | **-** | - |

Significant non-cash transactions ***12***

*The accompanying notes form an integral part of these consolidated financial statements*

**AVANTI ENERGY INC.**
CONDENSED CONSOLIDATED INTERIM STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY
**(Expressed in Canadian Dollars)**

| | Number of Shares | Share Capital | Equity Reserves | Deficit | Total Shareholders' Equity |
|---|---|---|---|---|---|
| Balance – December 31, 2012 | 13,050,000 | $ 921,246 | $ 119,600 | $ (324,343) | $ 716,503 |
| Common shares issued – acquisition of Avanti SA | 7,500,000 | 1,237,500 | - | - | 1,237,500 |
| Common shares issued – acquisition of Avanti Oil | 3,000,000 | 495,000 | - | - | 495,000 |
| Warrants exercised | 1,990,000 | 238,800 | - | - | 238,800 |
| Comprehensive loss for the period | - | - | - | (451,115) | (451,115) |
| Balance – June 30, 2013 | 25,540,000 | $ 2,892,246 | $ 119,600 | $ (775,458) | $ 2,236,688 |
| **Balance – December 31, 2013** | **34,901,665** | **$4,244,331** | **$533,871** | **$(2,393,609)** | **$2,384,593** |
| Warrants exercised | 4,792,000 | 575,040 | - | - | 575,040 |
| Private placement | 7,430,578 | 1,190,747 | - | - | 1,190,747 |
| Share issue costs (private placement) | - | (47,295) | - | - | (47,295) |
| Fair value of agent warrants | - | (28,072) | 28,072 | - | - |
| Share-based payments | - | - | 38,183 | - | 38,183 |
| Comprehensive loss for the period | - | - | - | (912,952) | (912,952) |
| **Balance – June 30, 2014** | **47,124,243** | **$5,934,751** | **$600,126** | **$(3,306,561)** | **$3,228,316** |

*The accompanying notes form an integral part of these consolidated financial statements*

## 1. NATURE AND CONTINUANCE OF OPERATIONS

Avanti Energy Inc. (the "Company" or "AVN", formerly Overlord Capital Ltd.) is an exploration stage company whose common shares trade on the TSX Venture Exchange ("TSX-V") and is in the business of acquiring, exploring and evaluating oil and gas properties. The Company was incorporated as a private company by Certificate of Incorporation issued pursuant to the provisions of the *British Columbia Business Corporations Act* on March 7, 2011.

On May 31, 2013, the Company announced the successful completion of the acquisitions of Avanti Exploration SA LLC ("Avanti SA") and Avanti Oil, LLC ("Avanti Oil"). The acquisition of Avanti SA and Avanti Oil were deemed to be acquisitions of a group of assets that do not constitute a business. As a result, the Company has acquired all of the issued and outstanding interests in Avanti SA and Avanti Oil.

The Company's head office is located at Suite 1450-701 West Georgia Street, Vancouver, British Columbia V6C 2T4 and its registered and records office address is Suite 1750, 1185 West Georgia Street, Vancouver, British Columbia, V6E 4B6**.**

These financial statements are presented in Canadian dollars, which is the functional currency of the Company and its subsidiaries.

These financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") with the assumption that the Company will be able to realize its assets and discharge its liabilities in the normal course of business rather than through a process of forced liquidation. The financial statements do not include adjustments to amounts and classifications of assets and liabilities that might be necessary should the Company be unable to continue operations.

The Company has only recently commenced generating revenue from operations and will require additional financing or outside participation to undertake further exploration and subsequent development of its exploration and evaluation assets. Future operations of the Company are dependent on its ability to raise additional equity financing and the attainment of profitable operations. These uncertainties may cast significant doubt about the Company's ability to continue as a going concern. The Company has sufficient cash reserves to meet its obligations for at least 12 months from the end of the reporting period.

The Company is in the process of exploring and evaluating its exploration and evaluation assets and has not yet determined whether the properties contain reserves that are economically recoverable. The recoverability of the amounts shown for exploration and evaluation assets are dependent upon the existence of economically recoverable reserves, the ability of the Company to obtain necessary financing to complete the development of those reserves and upon future production or proceeds from the disposition thereof.

## 2. BASIS OF PREPARATION

These unaudited condensed consolidated interim financial statements have been prepared in accordance with International Accounting Standards ("IAS") 34, Interim Financial Reporting as issued by the International Accounting Standards Board ("IASB"). The unaudited condensed consolidated interim financial statements follow the same accounting policies and methods of application as our most recent annual financial statements and do not include all of the information required for full annual financial statements. Accordingly, they should be read in conjunction with our IFRS financial statements for the fiscal year ended December 31, 2013. The accounting policies applied in these unaudited condensed consolidated interim financial statements are based on International Financial Reporting Standards ("IFRS") issued and outstanding as of August 29, 2014, the date the Board of Directors approved these unaudited condensed consolidated interim financial statements and they are consistent with those disclosed in the annual financial statements.

These condensed consolidated interim financial statements were approved and authorized for issue by the Board of Directors on August 29, 2014.

### Comparative figures

Certain comparative figures have been reclassified to conform with the current period financial statement presentation.

### Principles of consolidation

The condensed consolidated interim financial statements include the financial statements of the Company and its controlled subsidiaries of Avanti SA and Avanti Oil. All intercompany transactions, balances, revenues and expenses are eliminated on consolidation.

### Significant accounting judgments, estimates and assumptions

The preparation of these condensed consolidated interim financial statements requires management to make certain estimates, judgments and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported expenses during the period. Actual results could differ from these estimates.

<u>Critical judgments in applying accounting policies</u>

The preparation of these condensed consolidated interim financial statements requires management to make judgments regarding the going concern of the Company, as discussed in Note 1. In addition, management has made judgments regarding the functional currency of the Company, and has determined that the functional currency of the Company and its subsidiaries is the Canadian dollar.

<u>Key sources of estimation uncertainty</u>

Because a precise determination of many assets and liabilities is dependent upon future events, the preparation of financial statements in conformity with IFRS requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of assets and liabilities at the date of the financial statements and the reported amounts of expenses during the reporting periods. Actual results could differ from those estimates and such differences could be significant. Significant estimates made by management affecting our financial statements include, but are not limited to, the following:

## 2. BASIS OF PREPARATION (cont'd)

**Significant accounting judgments, estimates and assumptions** (cont'd)

*Carrying value and recoverability of exploration and evaluation assets*

The carrying amount of Company's exploration and evaluation assets does not necessarily represent present or future values, and the Company's exploration and evaluation assets have been accounted for under the assumption that the carrying amount will be recoverable. Recoverability is dependent on various factors, including the discovery of economically recoverable reserves, the ability of the Company to obtain the necessary financing to complete the development and upon future profitable production or proceeds from the disposition of the exploration and evaluation assets themselves. Additionally, there are numerous geological, economic, environmental and regulatory factors and uncertainties that could impact management's assessment as to the overall viability of its properties or to the ability to generate future cash flows necessary to cover or exceed the carrying value of the Company's exploration and evaluation assets.

*Share-based payments*

Estimating fair value for granted stock options requires determining the most appropriate valuation model which is dependent on the terms and conditions of the grant. This estimate also requires determining the most appropriate inputs to the valuation model including the expected life of the option, volatility, dividend yield, and rate of forfeitures and making assumptions about them. The value of the share-based compensation payment expense for the year along with the assumptions and model used for estimating fair value for share-based compensation transactions are disclosed in Note 7.

*Deferred tax Assets and Liabilities*

The estimation of income taxes includes evaluating the recoverability of deferred tax assets and liabilities based on an assessment of the Company's ability to utilize the underlying future tax deductions against future taxable income prior to expiry of those deductions. Management assesses whether it is probable that some or all of the deferred income tax assets and liabilities will not be realized. The ultimate realization of deferred tax assets and liabilities is dependent upon the generation of future taxable income, which in turn is dependent upon the successful discovery, extraction, development and commercialization of mineral reserves. To the extent that management's assessment of the Company's ability to utilize future tax deductions changes, the Company would be required to recognize more or fewer deferred tax assets or liabilities, and deferred income tax provisions or recoveries could be affected.

## 3. SIGNIFICANT ACCOUNTING POLICIES

**Cash and cash equivalents**

The Company considers cash and cash equivalents to include cash on deposit, cash held in trust, highly liquid short term interest bearing variable rate Guaranteed Investment Certificates, and Bankers' Acceptance Papers**.** As at June 30, 2014 and 2013, the Company had cash equivalents on hand.

## 3. SIGNIFICANT ACCOUNTING POLICIES (cont'd)

### Intangible assets

Intangible assets include the proprietary data of Avanti SA and Avanti Oil on the date of acquisition (Note 4).

Intangible assets acquired separately are measured on initial recognition at cost. The cost of intangible assets acquired in a business combination is their fair value as at the date of acquisition. Following initial recognition, intangible assets are carried at cost less any accumulated amortization and accumulated impairment losses, if any. The useful lives of intangible assets are assessed as either finite or indefinite.

Intangible assets with finite lives are amortized over the useful economic life and assessed for impairment whenever there is an indication that the intangible asset may be impaired. The amortization period and the amortization method for an intangible asset with a finite useful life is reviewed at least at the end of each reporting period. Changes in the expected useful life or the expected pattern of consumption of future economic benefits embodied in the asset are accounted for by changing the amortization period or method, as appropriate, and are treated as changes in accounting estimates. The amortization expense on intangible assets with finite lives is recognized in profit or loss in the expense category consistent with the function of the intangible assets.

Intangible assets with indefinite useful lives are not amortized, but are tested for impairment annually, either individually or at the cash-generating unit level. The assessment of indefinite life is reviewed annually to determine whether the indefinite life continues to be supportable. If not, the change in useful life from indefinite to finite is made on a prospective basis.

Gains or losses arising from derecognition of an intangible asset are measured as the difference between the net disposal proceeds and the carrying amount of the asset and are recognized in profit or loss when the asset is derecognized.

### Exploration and evaluation assets

*Pre-exploration costs*

Pre-exploration costs are expensed in the period in which they are incurred.

*Exploration and evaluation expenditures*

Once the legal right to explore a property has been acquired, all costs related to capital assets are capitalized by property. Consulting, management and lease operating costs are expensed to the consolidated statements of comprehensive loss. Costs not directly attributable to exploration and evaluation activities, including general and administrative overhead costs, are expensed in the period in which they occur.

The Company may occasionally enter into farm-out arrangements, whereby the Company will transfer part of a mineral interest, as consideration, for an agreement by the farmee to meet certain exploration and evaluation expenditures which would have otherwise been undertaken by the Company. The Company does not record any expenditures made by the farmee on its behalf. Any cash consideration received from the agreement is credited against the costs previously capitalized to the mineral interest given up by the Company, with any excess cash accounted for as a gain on disposal.

## 3. SIGNIFICANT ACCOUNTING POLICIES (cont'd)

### Exploration and evaluation assets (cont'd)

When a project is deemed to no longer have commercially viable prospects to the Company, exploration and evaluation expenditures in respect of that project are deemed to be impaired. As a result, those exploration and evaluation expenditure costs, in excess of estimated recoveries, are written- off to profit or loss.

The Company assesses exploration and evaluation assets for impairment when facts and circumstances suggest that the carrying amount of an asset may exceed its recoverable amount.

Once the technical feasibility and commercial viability of extracting the mineral resource has been determined, the property is considered to be under development. Exploration and evaluation assets are also tested for impairment before the assets are transferred to development properties.

As the Company currently has no operational income, any incidental revenues earned in connection with exploration activities are applied as a reduction to capitalized exploration costs.

### Property, plant and equipment

Property, plant and equipment, which include petroleum and natural gas properties where proven or probable reserves have been identified, are measured at cost less accumulated depletion and depreciation, and adjustments for impairment. Costs include expenditures that are directly attributable to the acquisition of the asset.

Gains and losses on disposal of an item of property, plant and equipment, including petroleum and natural gas properties, are determined by comparing the proceeds from disposal with the carrying amount of property, plant and equipment and are recognized in profit or loss. Farmouts of petroleum and natural gas properties included in property, plant and equipment are accounted for as a disposition of an interest in the asset in exchange for the fair value of goods and services received pertaining to the Company's retained interest in the asset.

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

### Depletion and depreciation

Petroleum and natural gas properties included in property, plant and equipment are depleted using the unit of production method by reference to the ratio of production in the period to the related proved and probable reserves, taking into account estimated future development costs necessary to bring those reserves into production. Future development costs are estimated taking into account the level of development required to produce the reserves. These estimates are reviewed by independent reserve engineers at least annually. Depletion is calculated separately for each cash-generating unit.

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

## 3. SIGNIFICANT ACCOUNTING POLICIES (cont'd)

**Revenue recognition**

Revenue from the sale of petroleum and natural gas is recognized when the significant risks and rewards of ownership have been transferred and it is probable that the measurable economic benefits will flow to the Company, which is normally when legal title passes to the customer. This generally occurs when product is physically transferred into a vessel, pipe or other delivery mechanism. Revenues associated with the sale of petroleum products are recognized when the title passes to the customer. Revenue is measured net of discounts, customs duties and royalties.

Revenue from the production of oil and natural gas in which the Company has an interest with other producers is recognized based on the Company's working interest and the terms of the relevant production sharing contracts. The costs associated with the delivery, including operating and maintenance costs, transportation and production based royalty expenses are recognized in the same period in which the related revenue is earned and recorded.

**Standards issued but not yet effective**

The standards and interpretations that are issued up to the date of issuance of the Company's financial statements, but were not effective during the period ended June 30, 2014, are disclosed below. The Company intends to adopt these standards, if applicable, when they become effective.

IFRS 9
Financial Instruments (iii)

IFRS 9, IFRS 7 and IAS 39 Amendments
Hedge Accounting and amendments to IFRS 9, IFRS 7 and IAS 39(iii)

IFRS 10, IFRS 12 and IAS 27 (2011) Amendments
Amendments to IFRS 10, IFRS 12 and IAS 27 (2011) – Investment Entities (i)

IAS 19 Amendment:
Amendments to IAS 19 Employee Benefits – Defined Benefit Plans: Employee Contributions (ii)

IAS 32 Amendments
Amendments to IAS 32 Financial Instruments: Presentation – Offsetting Financial Assets and Financial Liabilities (i)

IAS 39 Amendments
Amendments to IAS 39 Financial Instruments: Recognition and Measurement

(ii) Effective for annual periods beginning on or after July 1, 2014.
(iii) Mandatory effective date not yet determined.

The Company anticipates that the adoption of these standards and interpretations in future periods will have no material impact on the financial statements of the Company.

**(Expressed in Canadian Dollars)**

## 4. ASSET ACQUISITIONS

On May 15, 2013, the Company completed (i) a share purchase agreement with Avanti SA pursuant to which the Company acquired all of the issued and outstanding common shares in Avanti SA; and (ii) a share purchase agreement with Avanti Oil pursuant to which the Company acquired all of the issued and outstanding common shares in Avanti Oil.

The acquisition of Avanti SA was treated as an asset acquisition. The fair value of the assets acquired and liabilities assumed as at the date of acquisition were as follows:

| | | |
|---|---|---|
| Cash | $ | 5,151 |
| Prepaid assets | | 182,103 |
| Exploration and evaluation assets | | 113,288 |
| Intangible assets | | 1,473,406 |
| Accounts payable | | (106,000) |
| Net assets acquired | $ | 1,667,948 |

Consideration paid:

| | | |
|---|---|---|
| Value of 7,500,000 common shares of the Company | $ | 1,237,500 |
| Advances from Avanti Energy Inc. | | 430,448 |
| | | $1,667,948 |

The acquisition of Avanti Oil was treated as an asset acquisition. The fair value of the assets acquired and liabilities assumed as at the date of acquisition were as follows:

| | | |
|---|---|---|
| Deposit | $ | 65,363 |
| Intangible assets | | 429,637 |
| Net assets acquired | $ | 495,000 |

Consideration paid:

| | | |
|---|---|---|
| Value of 3,000,000 common shares of the Company | $ | 495,000 |

**(Expressed in Canadian Dollars)**

## 4. ASSET ACQUISITIONS (cont'd)

Summary of intangible assets:

| | |
|---|---|
| Acquisition of Avanti SA | $1,473,406 |
| Acquisition of Avanti Oil | 429,637 |
| | $ 1,903,043 |

Intangible assets include the proprietary data of Avanti SA and Avanti Oil on the date of acquisition and have indefinite useful lives that are tested for impairment annually.

The following contingent consideration from the Company is applicable to the Avanti Oil share purchase Agreement:

a. issuance of 2,000,000 common shares to the members of Avanti Oil, or their assignees, upon Avanti Oil entering into an agreement for the re-development of an onshore oil and gas field in Brazil;

b. issuance of 500,000 common shares to the members of Avanti Oil, or their assignees, upon Avanti Oil acquiring an oil and gas asset in South or Latin America;

c. issuance of 500,000 common shares to the members of Avanti Oil, or their assignees, upon Avanti Oil entering into a joint venture agreement for the participation in a bid to acquire oil and gas assets being auctioned by the Government of Brazil;

d. issuance of 1,000,000 common shares to the members of Avanti Oil, or their assignees, upon Avanti Oil commencing a submission of a work program to re-develop the Italy Project (as defined in the Avanti Oil share purchase agreement); and

e. issuance of 500,000 common shares to the members of Avanti Oil, or their assignees, upon Avanti Oil acquiring a minimum of an 87.5% interest in the Italy Project.

In addition to the share consideration set forth above, upon Avanti Oil acquiring a minimum of an 87.5% interest in the Italy Project, the Company will pay $300,000 to certain members of Avanti Oil, and will also pay to certain members of Avanti Oil, 30% of the net sale proceeds in connection with the sale of the Italy Project to a third party, or, in the event the Avanti Oil commences production of the Italy Project, 12.5% of the net proceeds of monies earned from production of the Italy Project.

## 5. LONG TERM DEPOSIT

On June 10, 2010, the Company's subsidiary, Avanti Oil, entered into an agreement with an Italian company, whereby Avanti Oil paid 50,000 Euros ($65,363) as consideration for the deposit to purchase 75% of the shares of the Italian company. At Avanti Oil's option, the Company may alternatively receive a like amount of the gas development activities of the Italian company in the Cugno le Macine concession, an oil and gas concession in the Region of Bascilicata, Italy.

**(Expressed in Canadian Dollars)**

## 6. EXPLORATION AND EVALUATION ASSETS

| | Orofino Project, Mexico | PWK Wells, USA | Forestar, USA | Total |
|---|---|---|---|---|
| Balance - December 31, 2012 | $170,294 | $ - | $ - | $ 170,294 |
| Additions | 21,051 | 7,035 | 12,335 | 40,421 |
| Reclamation provision | - | 7,500 | 7,500 | 15,000 |
| From Avanti SA asset acquisition | - | 85,424 | 27,864 | 113,288 |
| Transferred to Property, plant & equipment | - | - | - | - |
| Impairment | (191,345) | - | - | (191,345) |
| **Balance – December 31, 2013** | $ - | $ 99,959 | $ 47,699 | $ 147,658 |
| Additions | - | - | - | - |
| Transfer out to Property, plant & | - | (99,959) | - | (99,959) |
| **Balance – June 30, 2014** | $ - | $ - | $ 47,699 | $ 47,699 |

*Forestar 8 Well, Louisiana, USA*

The Company entered an agreement with Avanti Exploration and began work on the re-entry of the Forestar 8 well during 2013. Under this agreement, AVN paid 50% of the re-entry costs to earn a 25% interest in this well, as well as two other nearby wells known as the Dubose and Turnkey Temple Inland. The results of this well were negative and the Company plans to move on to the Dubose and Turnkey Temple Inland in 2014.

*Orofino Project, Mexico*

During the period ended December 31, 2011, the Company entered into an arm's length option agreement with Yale Resources Ltd. ("Yale") pursuant to which the Company has been granted an option to earn up to a 70% interest in the Orofino project (the "Project") located in Sonora State, Mexico (the "Transaction"). The Transaction is the Company's Qualifying Transaction. Under the terms of the Transaction, the Company can acquire up to a 70% interest in the Project by making option payments totalling $100,000, issuing 1,300,000 common shares of the Company to Yale and by meeting certain exploration and evaluation expenditure commitments. The Transaction closed on April 19, 2012.

During the year ended December 31, 2013, the Company relinquished the Orofino project and recorded an impairment of $191,345, effectively reducing the carrying value of the property to $nil.

**Reclamation Obligation**

| | |
|---|---|
| Balance, December 31, 2013 | $ 15,000 |
| Additions (reductions) | - |
| Accretion | - |
| Balance, June 30, 2014 | $ 15,000 |

**(Expressed in Canadian Dollars)**

## 6. EXPLORATION AND EVALUATION ASSETS (cont'd)

The Company's reclamation obligation consists of costs accrued based on the current best estimate of the plug and abandonment liability expense to be incurred upon the cessation of economic use of well locations. The Company's provision for future site closure and reclamation costs is based on the level of known disturbance at the reporting date, known legal requirements and estimates prepared by a third party specialist. It is not currently possible to estimate the impact on operating results, if any, of future legislative or regulatory developments.

Management used a risk-adjusted interest rate of 10% in preparing the Company's provision for closure and reclamation. Although the ultimate amount of reclamation costs to be incurred cannot be predicted with certainty, the net undiscounted amount of estimated cash flows required to settle the Company's estimated obligations is $35,000 over the next 9 years.

## 7. PROPERTY, PLANT AND EQUIPMENT

| | | **Total** |
|---|---|---|
| Balance - December 31, 2012 | $ | - |
| Additions | | - |
| **Balance – December 31, 2013** | $ | - |
| Additions | | 79,924 |
| Transfer in from Exploration Assets | | 99,959 |
| Depletion | | (7,200) |
| **Balance – June 30, 2014** | $ | 172,683 |

*VUA Miller #1 Well, Louisiana, USA*

The Company drilled, completed and tied-in the well during the period; and was placed on commercial production in June 2014. Under the agreement with Avanti Exploration, LLC ("Avanti Exploration") the operator, AVN paid 1/3 of the costs of the well to casing point, which totaled US$1.025 million to the 100% interest. After reaching casing point, the Company paid 25% of the costs of the well (prorated interest) for the balance of the completion work to earn a 25% working-interest in the well.

During the period, the well was directionally drilled and during an eight-hour period tested 108 bopd of 49 degrees gravity oil and 30 mcfgd with 1,200 flowing tubing pressure on a 16/64" choke, from the Cockfield reservoir.

Installation of production facilities was completed in April 2014 and the well was placed on production on May 8, 2014. After a week's production, the well averaged 196 barrels of oil per day (bopd) and 246 mcf of gas per day, on an 11/64" choke, with 1,245 flowing tubing pressure and a 50% water cut.

Through the period ending June 30, the well produced 8763 barrels of oil for an average of 162 bopd.

**(Expressed in Canadian Dollars)**

## 7. PROPERTY, PLANT AND EQUIPMENT (cont'd)

*PWK Wells, Louisiana, USA*

During the year ended December 31, 2013, the Company entered into a participation agreement (the "Participation Agreement") with Avanti Exploration dated January 24, 2013 under which the Company acquired a 25% interest in two oil and/or gas wells, known as the PWK 10-1 well and the Powell Lumber #1 well located in the Cowpen Creek Field area in Beauregard Parish, Louisiana.

Under the terms of the Participation Agreement, the Company received an undivided 25% working interest in the PWK 10-1 well and the Powell Lumber #1 well in consideration for the Company contributing 50%, of the cost of the work-over/re-entering of these wells. The Participation Agreement also provides that Avanti Exploration will be the operator of the wells.

During the period, the PWK 10-1 well continues to produce at marginal rates of 6-7 bopd.

## 8. CAPITAL STOCK

**Authorized**

Unlimited common shares with no par value.

During the period ended June 30, 2014, the Company:

(i) closed a non-brokered private placement for gross proceeds of $1,190,747 via the issuance of 7,430,578 common shares at $0.16 (US$0.145) per share. The Company paid Finder's Fees of $28,639 and US$870 in cash and issued 145,991 warrants with a value of $28,072, each exercisable into one common shares at $0.16 for a term of two years from the date of issuance. The warrants were valued using the Black-Scholes model with the following assumptions:

| | |
|---|---|
| Risk-free interest rate | 1.00% |
| Expected life | 2 years |
| Expected volatility | 147.99% |
| Expected dividend yield | Nil |
| Share price | $0.16 |

(ii) issued 4,792,000 common shares upon the exercise of warrants for gross proceeds of $575,040.

During the period ended June 30, 2013, the Company:

(iii) issued 10,500,000 common shares for the acquisition of Avanti Oil and Avanti SA, valued at $495,000 and $1,237,500, respectively (Note 4); and

(iv) issued 1,990,000 common shares upon the exercise of warrants for gross proceeds of $238,800.

**(Expressed in Canadian Dollars)**

## 8. CAPITAL STOCK (cont'd)

### Escrow shares

(i) *Pre-public shares*
As at June 30, 2014, 600,000 (2013: 1,200,000) common shares were held in escrow.

The escrow shares are released from escrow as follows:

- 10% released on April 27, 2012 (the date of TSX-V acceptance of the qualifying transaction)
- an additional 15% released on each of the six, twelve, eighteen, twenty-four, thirty and thirty-six months following the initial release on April 27, 2012.

(ii) *Avanti acquisition shares (Note 4)*
All shares issued for the acquisition of Avanti SA and Avanti Oil were the subject of an Escrow agreement dated May 15, 2013. As at June 30, 2014, 6,300,000 (2013: 9,450,000) common shares were held in escrow.

The escrow shares are released from escrow as follows:

- 10% released as of June 4, 2013 (the date of TSX-V acceptance of the Avanti transactions)
- an additional 15% released on each of the six, twelve, eighteen, twenty-four, thirty and thirty-six months following the initial release on June 4, 2013.

### Stock options

The Company has a stock option plan under which it is authorized to grant options to executive officers and directors, employees and consultants enabling them to acquire up to 10% of the issued and outstanding common stock of the Company. Under the plan, the exercise price of each option equals the market price of the Company's stock, less an applicable discount, as calculated on the date of grant. The options can be granted for a maximum term of 10 years and vest at the discretion of the board of directors.

As at June 30, 2014, the following options were outstanding and exercisable:

| Number of options | Exercise price | Remaining life (years) | Expiry date |
|---|---|---|---|
| 50,000 | $ 0.10 | 2.81 | April 19, 2017 |
| 2,900,000 | $ 0.20 | 4.41 | November 25, 2018 |
| 200,000 | $ 0.205 | 4.61 | February 5, 2019 |
| **3,150,000** | | | |

**(Expressed in Canadian Dollars)**

**8. CAPITAL STOCK** (cont'd)

**Stock Options** (cont'd)

A summary of changes of stock options outstanding is as follows:

| | **Options** | **Weighted average exercise price** |
|---|---|---|
| Balance outstanding and exercisable as at December 31, 2012 | 1,300,000 | $ 0.10 |
| Granted | 2,900,000 | 0.20 |
| Cancelled | (450,000) | (0.10) |
| Exercised | (800,000) | (0.10) |
| Balance outstanding and exercisable as at December 31, 2013 | 2,950,000 | $ 0.20 |
| Granted | 200,000 | 0.205 |
| **Balance outstanding and exercisable as at June 30, 2014** | **3,150,000** | **$ 0.20** |

These options entitle the holder thereof the right to acquire one common share for each option held. The weighted average remaining life of outstanding options is 4.40 years.

During the period ended June 30, 2014, the Company granted 200,000 (2013: nil) stock options with a fair value of $38,183 (2013: $nil) or $0.19 (2013: $nil) per option.

The options granted to directors and officers during the period vested on the grant date. The fair value of each option was estimated on the grant date using the Black-Scholes option valuation model with the following assumptions:

| | 2014 |
|---|---|
| Risk-free interest rate | 1.58% |
| Expected life | 5 years |
| Expected volatility | 149.01% |
| Expected dividend yield | Nil |
| Share price | $0.205 |

Expected volatility is determined using the historical share price volatility of the Company.

**Warrants**

As at June 30, 2014, the following warrants were issued and outstanding:

| Number of warrants | Exercise price | Remaining life (years) | Expiry date |
|---|---|---|---|
| 170,000 | $ 0.15 | 1.41 | November 25, 2015 |
| 145,991 | $ 0.16 | 1.68 | March 3, 2016 |
| 315,991 | | | |

**(Expressed in Canadian Dollars)**

## 8. CAPITAL STOCK (cont'd)

**Warrants** (cont'd)

A summary of changes of warrants outstanding is as follows:

| | Warrants | Weighted average exercise price |
|---|---|---|
| Balance, December 31, 2012 | 9,200,000 | $ 0.12 |
| Exercised | (200,000) | (0.10) |
| Exercised | (4,020,000) | (0.12) |
| Issued | 170,000 | 0.15 |
| Balance, December 31, 2013 | 5,150,000 | $ 0.12 |
| Exercised | (4,792,000) | (0.12) |
| Expired (unexercised) | (188,000) | (0.12) |
| Issued | 145,991 | 0.16 |
| Balance, June 30, 2014 | 315,991 | $ 0.15 |

## 9. FINANCIAL INSTRUMENTS

**Fair value**

The Company's consolidated financial instruments consist of cash and equivalents, accounts receivable, accounts payable and accrued liabilities and due to related parties. As at June 30, 2014, the carrying value of receivables, accounts payable and accrued liabilities and due to related parties approximate their fair value due to their short terms to maturity. Cash is measured at fair value using level 1 inputs.

The Company's risk exposures and the impact on the Company's financial statements are summarized below.

*Credit risk*

Credit risk is the risk of an unexpected loss if a customer or third party to a financial instrument fails to meet its contractual obligations.

The Company's cash and equivalents are held at large Canadian and US financial institution in interest bearing accounts and in lawyers trust accounts. The Company has no investment in asset-backed commercial paper. The Company's receivables consist mainly of government sales tax ("GST") receivable due from the government of Canada. As a result, the Company does not believe it is exposed to significant credit risk.

*Liquidity risk*

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they fall due.

All of the Company's financial liabilities are classified as current and are anticipated to mature within the next fiscal period. The Company intends to settle these with funds from its positive working capital position.

## 9. FINANCIAL INSTRUMENTS (cont'd)

*Market risk*

Market risk is the risk of loss that may arise from changes in market factors such as interest rates, foreign exchange rates, and commodity and equity prices.

a) Interest rate risk

Interest rate risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates.

The Company is exposed to interest rate risk to the extent that the cash maintained at the financial institutions is subject to a floating rate of interest. The interest rate risk on cash is not considered significant.

b) Foreign currency risk

The Company is exposed to foreign currency risk on fluctuations related to cash, receivables, and accounts payable and accrued liabilities that are denominated in a foreign currency. As at June 30, 2014, the Company considers foreign currency risk to be insignificant.

c) Price risk

The Company has limited exposure to price risk with respect to commodity and equity prices. Equity price risk is defined as the potential adverse impact on the Company's earnings due to movements in individual equity prices or general movements in the level of the stock market. Commodity price risk is defined as the potential adverse impact on earnings and economic value due to commodity price movements and volatilities.

## 10. CAPITAL MANAGEMENT

Capital is comprised of the Company's shareholders' equity. As at June 30, 2014, the Company's shareholders' equity was $3,228,316. The Company manages its capital structure to maximize its financial flexibility making adjustments to it in response to changes in economic conditions and the risk characteristics of the underlying assets and business opportunities. The Company does not presently utilize any quantitative measures to monitor its capital.

The Company is not currently subject to externally imposed capital requirements.

There has been no change to the Company's capital management approach during the period ended June 30, 2014.

**(Expressed in Canadian Dollars)**

## 11. RELATED PARTY TRANSACTIONS

Related parties and related party transactions impacting the accompanying financial statements are summarized below and include transactions with the following individuals or entities:

Key management personnel

Key management personnel include those persons having authority and responsibility for planning, directing and controlling the activities of the Company as a whole. The Company has determined that key management personnel consist of executive and non-executive members of the Company's Board of Directors and corporate officers.

| | Period ended June 30, | |
|---|---|---|
| **Key Management and Personnel** | 2014 | 2013 |
| Share-based payments | 38,183 | - |
| | $ 38,183 | $ - |

During the period ended June 30, 2014, the Company entered into the following transactions with key management personnel:

| Related party | Nature of transaction |
|---|---|
| BRL Consulting Inc. ("BRL") | Consulting fees for the services provided by Brent Lokash as Director and Secretary. |
| Mark Frascogna.LLC ("Frascogna") | Consulting fees for the services provided by Mark Frascogna as Vice President, Commercial Affairs |
| Tim Berge LLC ("Berge") | Consulting fees for the services provided of Tim Berge as Vice President, Exploration and Development |
| Contact Financial Corp. ("CFC") | Rent and shared office expenses. |
| Pacific Equity Management Corp. ("PEMC") | Management fees for services provided by CFO, VP Corporate Development, VP Finance, Independent Director, Accountant, and Administrator. |
| Avanti Exploration, LLC ("Avanti Exploration") | Participation agreements, and operating arrangements for exploration and evaluation assets in Louisiana |

(a) Paid $nil (2013 - $62,220) in consulting fees to BRL, a company controlled by a former director.

(b) Paid $3,000 (2013 - $3,000) in rent (included in administrative fees) and $nil (2013: $77,440) in consulting fees to CF, a company in which a director is a significant shareholder.

(c) Paid $150,000 (2013: $nil) to PEMC, a company controlled by two directors for management services.

(d) Paid US$93,000 (2013: $93,000) to Frascogna, a company controlled by an officer for consulting fees.

(e) Paid US$46,500 (2013: $38,750) to Berge, a company controlled by an officer for consulting fees.

(f) Included in prepaids and deposits is $26,647 (2013: $nil) paid to Avanti Exploration, a company with two common directors for advances on exploration work to be completed after June 30, 2014.

## 11. RELATED PARTY TRANSACTIONS (cont'd)

(g) Issued 200,000 (2013: nil) stock options to a director with a fair value of $38,183 (2013 - $nil).

(h) Due to related parties includes the following: $52,504 (2013: $77,933). Amounts due to related parties are unsecured with no fixed terms for payment.

These transactions were in the normal course of operations.

## 12. SUPPLEMENTAL DISCLOSURE WITH RESPECT TO CASH FLOWS

The Company's significant non-cash transactions during the period ended June 30, 2014 were as follows:

(a) issued 145,991 warrants with a fair value of $28,072 for Finders' fees in connection with a private placement (Note 7).

(b) granted 200,000 options with a value of $38,183 to a director of the company (Note 7).

During the period ended June 30, 2013, the Company recorded the following non-cash transactions:

(c) issued 7,500,000 common shares with a value of $1,237,500 in connection with the Avanti SA acquisition (Note 4).

(d) issued 3,000,000 common shares with a value of $495,000 in connection with the Avanti Oil acquisition (Note 4).

**(Expressed in Canadian Dollars)**

## 13. SEGMENT INFORMATION

The Company has one reportable operating segment, being the acquisition, exploration, and evaluation of exploration and evaluation assets. Geographic segmentation of the Company's non-current assets is as follows:

| | June 30, 2014 | | |
|---|---|---|---|
| | **USA** | **Italy** | **Total** |
| Property, plant and equipment | $ 172,683 | $ - | $ 172,683 |
| Exploration and evaluation assets | 47,699 | - | 47,699 |
| Long term deposits | - | 65,363 | 65,363 |
| Intangible assets | 1,903,043 | - | 1,903,043 |
| | $ 2,123,425 | $ 65,363 | $ 2,188,788 |

| | December 31, 2013 | | |
|---|---|---|---|
| | **USA** | **Italy** | **Total** |
| Exploration and evaluation assets | $ 147,658 | $ - | $ 147,658 |
| Long term deposits | - | 65,363 | 65,363 |
| Intangible assets | 1,903,043 | - | 1,903,043 |
| | $ 2,050,701 | $ 65,363 | $ 2,116,064 |

## 14. EVENTS AFTER THE REPORTING PERIOD

None to report.