

TORCHLIGHT ENERGY RESOURCES INC

Form 10-K

March 16, 2018

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

(Mark One)

Annual report under Section 13 or 15(d) of the Securities Exchange Act of 1934  
For the fiscal year ended December 31, 2017.

Transition report under Section 13 or 15(d) of the Securities Exchange Act of 1934 (No fee required)  
For the transition period from \_\_\_\_\_ to \_\_\_\_\_.

Commission file number 000-53473

Torchlight Energy Resources, Inc.

(Exact name of registrant in its charter)

Nevada

74-3237581

(State or other jurisdiction of incorporation or (I.R.S. Employer Identification No.)  
Organization)

5700 W. Plano Parkway, Suite 3600

Plano, Texas 75093

(Address of principal executive offices)

(214) 432-8002

(Registrant's telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Exchange Act:

Common Stock (\$0.001 Par Value)

(Title of Each Class)

The NASDAQ Stock Market LLC

(Name of each exchange on which registered)

Securities registered pursuant to Section 12(g) of the Exchange Act:

None

Indicate by check mark if the registrant is a well-known seasoned issuer as defined in Rule 405 of the Securities Act.  
Yes   No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes   No



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Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of the registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer

Accelerated filer

Non-accelerated filer (Do not check if a smaller reporting company) Smaller reporting company

Emerging growth company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes No

The aggregate market value of the common stock held by non-affiliates of the registrant on June 30, 2017, the last business day of the registrant's most recently completed second fiscal quarter, based on the closing price on that date of \$1.66 on the Nasdaq Stock Market, was approximately \$76,874,895.

At March 15, 2018, there were 63,640,034 shares of the registrant's common stock outstanding (the only class of common stock).

#### EXPLANATORY NOTE

The Company meets the "accelerated filer" requirements as of the end of its 2017 fiscal year pursuant to Rule 12b-2 of the Securities Exchange Act of 1934. However, pursuant to Rule 12b-2 and SEC Release No. 33-8876, the Company (as a smaller reporting company transitioning to the larger reporting company system based on its public float as of June 30, 2017) is not required to satisfy the larger reporting company requirements until its first quarterly report on Form 10-Q for the 2018 fiscal year and thus remains eligible to use the scaled disclosure requirements applicable to smaller reporting companies under Item 10 of Regulation S-K under the Securities Act of 1933 in this Annual Report on Form 10-K.

DOCUMENTS INCORPORATED BY REFERENCE

None.



## NOTE ABOUT FORWARD-LOOKING STATEMENTS

This Annual Report on Form 10-K contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. These statements include, among other things, statements regarding plans, objectives, goals, strategies, future events or performance and underlying assumptions and other statements, which are other than statements of historical facts. Forward-looking statements may appear throughout this report, including without limitation, the following sections: Item 1 “Business,” Item 1A “Risk Factors,” and Item 7 “Management’s Discussion and Analysis of Financial Condition and Results of Operations.” Forward-looking statements generally can be identified by words such as “anticipates,” “believes,” “estimates,” “expects,” “intends,” “plans,” “predicts,” “projects,” “will be,” “will continue,” “likely result,” and similar expressions. These forward-looking statements are based on current expectations and assumptions that are subject to risks and uncertainties, which could cause our actual results to differ materially from those reflected in the forward-looking statements. Factors that could cause or contribute to such differences include, but are not limited to, those discussed in this Annual Report on Form 10-K, and in particular, the risks discussed under the caption “Risk Factors” in Item 1A and those discussed in other documents we file with the Securities and Exchange Commission (“SEC”). Important factors that in our view could cause material adverse effects on our financial condition and results of operations include, but are not limited to, risks associated with the company's ability to obtain additional capital in the future to fund planned expansion, the demand for oil and natural gas, general economic factors, competition in the industry and other factors that may cause actual results to be materially different from those described herein as anticipated, believed, estimated or expected. We undertake no obligation to revise or publicly release the results of any revision to any forward-looking statements, except as required by law. Given these risks and uncertainties, readers are cautioned not to place undue reliance on such forward-looking statements.

As used herein, the “Company,” “Torchlight,” “we,” “our,” and similar terms include Torchlight Energy Resources, Inc. and its subsidiaries, unless the context indicates otherwise.





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## PART I

### ITEM 1. BUSINESS

#### Corporate History and Background

Torchlight Energy Resources, Inc. was incorporated in October, 2007 under the laws of the State of Nevada as Pole Perfect Studios, Inc. (“PPS”).

On November 23, 2010, we entered into and closed a Share Exchange Agreement (the “Exchange Agreement”) between the major shareholders of PPS and the shareholders of Torchlight Energy, Inc. (“TEI”). As a result of the transactions effected by the Exchange Agreement, at closing TEI became our wholly-owned subsidiary, and the business of TEI became our sole business. TEI is an energy company, incorporated under the laws of the State of Nevada in June, 2010. We are engaged in the acquisition, exploration, exploitation, and/or development of oil and natural gas properties in the United States. We operate our business through TEI and four other wholly-owned subsidiaries, Torchlight Energy Operating, LLC, a Texas limited liability company, Hudspeth Oil Corporation, a Texas corporation, Torchlight Hazel LLC, a Texas limited liability company, and Warwink Properties LLC, a Texas limited liability company.

#### Business Overview

Our business model is to focus on drilling and working interest programs within the United States, primarily in basins or areas with known geology such as the Permian Basin in West Texas. We have interests in four oil and gas projects, which projects are described in more detail below in the section titled “Current Projects.” We anticipate being involved in other oil and gas projects moving forward, pending adequate funding. We anticipate acquiring exploration and development projects both as a non-operating working interest partner, participating in drilling activities primarily on a basis proportionate to the working interest, and acquiring properties we can operate. We intend to spread the risk associated with drilling programs by entering into a variety of programs in different fields with differing economics.

The core strategy of the Company is pursuing the ongoing development of its assets in the Permian basin consisting of the Orogrande and the Hazel Projects. These West Texas properties demonstrate significant value potential and future production capabilities based upon the analysis of scientific data already gathered in the day by day development activity. Therefore, the Board has determined to focus its efforts and capital on these two projects to maximize shareholder value for the long run.

#### Key Business Attributes

**Experienced People.** We build on the expertise and experiences of our management team, including John Brda and Roger Wurtele. We will also receive guidance from outside advisors as well as our Board of Directors and will align with high quality exploration and technical partners.

**Project Focus.** We are focusing primarily on exploitation projects by pursuing resources in areas where commercial production has already been established but where opportunity for additional and nearby development is indicated. We may pursue high risk exploration prospects which may appear less favored than low risk exploration. We will, however, consider these high risk-high reward exploration prospects in connection with exploitation opportunities in a project that would reduce the overall project economic risk. We will consider such high risk-high reward prospects on their individual merits.

**Lower Cost Structure.** We will attempt to maintain the lowest possible cost structure, enabling the greatest margins and providing opportunities for investment that would not be feasible for higher cost competitors.

**Limit Capital Risks.** Limited capital exposure is planned initially to add value to a project and determine its economic viability. Projects are staged and have options before additional capital is invested. We will limit our exposure in any one project by participating at reduced working interest levels, thereby being able to diversify with limited capital. Management has experience in successfully managing risks of projects, finance, and value.

#### Project Focus

Generally, we will focus on exploitation projects (primarily for oil, although gas projects will be considered if the economics are favorable). Projects are first identified, evaluated, and followed by the engagement of third party operating or financial partners. Subject to overall availability of capital, our interest in large capital projects will be limited. Each opportunity will be investigated on a standalone basis for both technical and financial merit.

We will be actively seeking quality new investment opportunities to sustain our growth, and we believe we will have access to many new projects. The sources of these opportunities will vary but all will be evaluated with the same criteria of technical and economic factors. It is expected that projects will come from the many small producers who find themselves under-funded or over-extended and therefore vulnerable to price volatility. The financial ability to respond quickly to opportunities will ensure a continuous stream of projects and will enable us to negotiate from a stronger position to enhance value.



## ITEM 1. BUSINESS - continued

With emphasis on acquisitions and development strategies, the types of projects in which we will be involved vary from increased production due to simple re-engineering of existing wellbores to step-out drilling, drilling horizontally, and extensions of known fields. Recompletion of existing wellbores in new zones, development of deeper zones and detailing of structure, and stratigraphic traps with three-dimensional seismic and utilization of new technologies will all be part of our anticipated program. Our preferred type of projects are in-fills to existing production with nearly immediate cash flow and/or adjacent or on trend to existing production. We will prefer projects with moderate to low risk, unrecognized upside potential, and geographic diversity.

### Business Processes

We believe there are three principal business processes that we must follow to enable our operations to be profitable. Each major business process offers the opportunity for a distinct partner or alliance as we grow. These processes are:

- Investment Evaluation and Review;
- Operations and Field Activities; and
- Administrative and Finance Management.

**Investment Evaluation and Review.** This process is the key ingredient to our success. Recognition of quality investment opportunities is the fuel that drives our engine. Broadly, this process includes the following activities: prospect acquisition, regional and local geological and geophysical evaluations, data processing, economic analysis, lease acquisition and negotiations, permitting, and field supervision. We expect these evaluation processes to be managed by our management team. Expert or specific technical support will be outsourced as needed. Only if a project is taken to development, and only then, will additional staff be hired. New personnel will have very specific responsibilities. We anticipate attractive investment opportunities to be presented from outside companies and from the large informal community of geoscientists and engineers. Building a network of advisors is key to the pipeline of high quality opportunities.

**Operations and Field Activities.** This process begins following management approval of an investment. Well site supervision, construction, drilling, logging, product marketing, and transportation are examples of some activities. We will prefer to be the operator, but when operations are not possible, we will farm-out sufficient interests to third parties that will be responsible for these operating activities. We provide personnel to monitor these activities and associated costs.

**Administrative and Finance Management.** This process coordinates our initial structuring and capitalization, general operations and accounting, reporting, audit, banking and cash management, regulatory agencies reporting and interaction, timely and accurate payment of royalties, taxes, leases rentals, vendor accounts and performance management that includes budgeting and maintenance of financial controls, and interface with legal counsel and tax and other financial and business advisors.

### Current Projects

As of December 31, 2017 the Company had interests in four oil and gas projects:, the Orogrande Project in Hudspeth County, Texas, and the Hazel Project in Sterling, Tom Green, and Irion Counties, Texas, the Winkler Project in Winkler County, Texas, and the Hunton wells in partnership with Husky Ventures in Central Oklahoma ..

Orogrande Project, West Texas

On August 7, 2014, we entered into a Purchase Agreement with Hudspeth Oil Corporation (“Hudspeth”), McCabe Petroleum Corporation (“MPC”), and Greg McCabe. Mr. McCabe was the sole owner of both Hudspeth and MPC. Under the terms and conditions of the Purchase Agreement, at closing, we purchased 100% of the capital stock of Hudspeth which holds certain oil and gas assets, including a 100% working interest in 172,000 mostly contiguous acres in the Orogrande Basin in West Texas. As of December 31, 2017, leases covering 133,000 acres remain in effect. This acreage is in the primary term under five-year leases that carry additional five-year extension provisions. As consideration, at closing we issued 868,750 shares of our common stock to Mr. McCabe and paid a total of \$100,000 in geologic origination fees to third parties. Additionally, Mr. McCabe has, at his option, a 10% working interest back-in after payout and a reversionary interest if drilling obligations are not met, all under the terms and conditions of a participation and development agreement. All drilling obligations through December 31, 2017 have been met.

On September 23, 2015, our subsidiary, Hudspeth Oil Corporation (“HOC”), entered into a Farmout Agreement by and between HOC, Pandora Energy, LP (“Pandora”), Founders Oil & Gas, LLC (“Founders”), McCabe Petroleum Corporation and Greg McCabe (McCabe Petroleum Corporation and Greg McCabe are parties to the Farmout Agreement for limited purposes) for the entire Orogrande Project in Hudspeth County, Texas. The Farmout Agreement provided for Founders to earn from HOC and Pandora (collectively, the “Farmor”) an undivided 50% of the leasehold interest in the Orogrande Project by Founder’s spending a minimum of \$45 million on actual drilling operations on the Orogrande Project in the following two years.

Under a joint operating agreement (on A.A.P.L. Form 610 – 1989 Model Form Operating Agreement with COPAS 2005 Accounting Procedures) (“JOA”) also entered into on September 23, 2015, Founders is designated as operator of the leases.



ITEM 1. BUSINESS - continued

On March 22, 2017, the Company, along with Founders, their operating partner, signed a Drilling and Development Unit (DDU) Agreement with University Lands on its Orogrande Basin Project. The agreement has an effective date of January 1, 2017 and required a payment from both Torchlight and Founders of \$335,323 as part of the extension fee. Torchlight's portion of the fee was paid by Founders in April 2017 and will be deducted from the required spud fee payable to Torchlight at commencement of the next well drilled.

The DDU agreement allows for all 192 existing leases covering the 133,000 net acres leased from University Lands to be combined into one lease for development purposes. The time to drill on the unit is extended through April of 2023 on the first extension. The agreement also grants exclusive right to continue through April of 2028 if compliance with the agreement is met and extension fee associated with the additional time paid. The Company's drilling obligations begin with one well in the first year, and increase to five wells per year by year 2023. The drilling obligation set is a minimum requirement and may be exceeded if acceleration is desired. The DDU agreement replaces all prior agreements and will govern future drilling obligations on the lease.

The Orogrande Rich A-11 test well that was drilled by Torchlight in second quarter, 2015 was evaluated and numerous scientific tests were performed to provide key data for the field development thesis. Future utility of this well may be conversion to a salt water disposal well in the course of further development of the Orogrande acreage.

The second test well, the University Founders B-19 #1, was spudded on April 24, 2016 and drilled in second quarter, 2016. The well successfully pumped down completion fluid in the third quarter of 2016 and indications of hydrocarbons were seen at the surface on this second Orogrande Project test well. Future utility of this well may be conversion to a salt water disposal well in the course of further development of the Orogrande acreage.

During the fourth quarter, 2017, the Company took back operational control from Founders Oil and Gas on the Orogrande Basin Project. Torchlight was joined by Wolfbone Investments, LLC, ("Wolfbone"), a company owned by Greg McCabe, Torchlight's Chairman. The two entities have entered into an Assignment of Farmout Agreement with Founders and will share the remaining commitments under the prior agreement with Founders. All original provisions of Torchlight's carried interest will remain in place including reimbursement to the Company on each wellbore. Founders will remain a 9.5% Working Interest owner in the project under the agreement for the \$9.5 million it has spent to date and be carried until the remaining \$40.5 million is spent by Wolfbone and Torchlight, with each contributing 50% of that capital spend, under the existing agreement. Torchlight's interest in the Project thereby increased by 20.25% Working Interest to a total of 67.75% and Wolfbone now owns 20.25%.

Founders will operate a newly drilled well called the University Founders #A25 with supervision from Torchlight and its Partners. The University Founders #A25 was spudded on the 27th of November and satisfies the obligation under the University Lands D&D Agreement. Once the #A25 is completed Torchlight will assume full operational control including managing drilling plans and timing for all future wells drilled in the Project.

Hazel Project in the Midland Basin in West Texas

Effective April 1, 2016, Torchlight Energy Inc. acquired from McCabe Petroleum Corporation, a 66.66% working interest in approximately 12,000 acres in the Midland Basin in exchange for 1,500,000 warrants to purchase our common stock with an exercise price of \$1.00 for five years and a back-in after payout of a 25% working interest to the seller.

Initial development of the first well on the property, the Flying B Ranch #1, began July 10, 2016 and development continued through September 30, 2016. This well is classified as a test well in the development pursuit of the Hazel

Project. It is anticipated that this wellbore will be utilized as a salt water disposal well in support of future development.

In October, 2016, the holders of the Company's Series C Preferred shares (which were issued in July, 2016) elected to convert into a 33.33% Working Interest in the Company's Hazel Project, reducing Torchlight's ownership from 66.66% to a 33.33% Working Interest.

On December 27, 2016, drilling activities commenced on the second Hazel Project well, the Flying B Ranch #2. The well is a vertical test similar to the Company's first Hazel Project well, the Flying B Ranch #1. Recompletion in an alternative geological formation for this well was performed during the three months ended September 30, 2017 however the results were uneconomic for continuing production. It is anticipated that this wellbore will be utilized as a salt water disposal well in support of future development.

The Company commenced planning to drill a horizontal well in the Project in June, 2017 in compliance with the continuous drilling obligation. The well, the Flying B Ranch #3, was spudded on June 10, 2017. The well was completed and began production in late September, 2017.



ITEM 1. BUSINESS - continued

Acquisition of Additional Interests in Hazel Project

On January 30, 2017, we and our wholly-owned subsidiary, Torchlight Acquisition Corporation, a Texas corporation (“TAC”), entered into and closed an Agreement and Plan of Reorganization and Plan of Merger with Line Drive Energy, LLC, a Texas limited liability company (“Line Drive”), under which agreements TAC merged with and into Line Drive and the separate existence of TAC ceased, with Line Drive being the surviving organization and becoming our wholly-owned subsidiary. Line Drive, which was wholly-owned by Gregory McCabe, our Chairman, owned certain assets and securities, including approximately 40.66% of 12,000 gross acres in the Hazel Project and 521,739 warrants to purchase our common stock (which warrants had been assigned by Mr. McCabe to Line Drive). Under the merger transaction, our shares of common stock of TAC converted into a membership interest of Line Drive, the membership interest in Line Drive held by Mr. McCabe immediately prior to the transaction ceased to exist, and we issued Mr. McCabe 3,301,739 restricted shares of common stock as consideration therefor. Immediately after closing, the 521,739 warrants held by Line Drive were cancelled, which warrants had an exercise price of \$1.40 per share and an expiration date of June 9, 2020. A Certificate of Merger for the merger transaction was filed with the Secretary of State of Texas on January 31, 2017. Subsequent to the closing the name of Line Drive Energy, LLC was changed to Torchlight Hazel, LLC.

Also on January 30, 2017, our wholly-owned subsidiary, Torchlight Energy, Inc., a Nevada corporation (“TEI”), entered into and closed a Purchase and Sale Agreement with Wolfbone Investments, LLC, a Texas limited liability company (“Wolfbone”) which is wholly-owned by Gregory McCabe, our Chairman. Under the agreement, TEI acquired certain of Wolfbone’s Hazel Project assets, including its interest in the Flying B Ranch #1 well and the 40 acre unit surrounding the well, for consideration of \$415,000, and additionally, Wolfbone caused to be cancelled a total of 2,780,000 warrants to purchase our common stock, including 1,500,000 warrants held by McCabe Petroleum Corporation, an entity owned by Mr. McCabe, and 1,280,000 warrants held by Green Hill Minerals, an entity owned by Mr. McCabe’s son, which warrant cancellations were effected through certain Warrant Cancellation Agreements. The 1,500,000 warrants held by McCabe Petroleum Corporation had an exercise price of \$1.00 per share and an expiration date of April 4, 2021. The warrants held by Green Hill Minerals included 100,000 warrants with an exercise price of \$1.73 and an expiration date of September 30, 2018 and 1,180,000 warrants with an exercise price of \$0.70 and an expiration date of February 15, 2020.

Since Mr. McCabe held the controlling interest in both Line Drive and Wolfbone Investments, LLC, the transactions were combined for accounting purposes. The working interest in the Hazel Project was the only asset held by Line Drive. The warrant cancellation was treated in the aggregate as an exercise of the warrants with the transfer of the working interests as the consideration. The Company recorded the transactions as an increase in its investment in the Hazel project working interests of \$3,644,431 which is equal to the exercise price of the warrants plus the cash paid to Wolfbone.

Upon the closing of the transactions, the Company’s working interest in the Hazel project increased by 40.66% to a total ownership of 74%.

Effective June 1, 2017, the Company acquired an additional 6% working interest from unrelated working interest owners in exchange for 268,656 shares of common stock valued at \$373,430, increasing its working interest in the Hazel project to 80%.

Winkler Project, Winkler County, Texas

On December 1, 2017, the Agreement and Plan of Reorganization that we and our newly formed wholly-owned subsidiary, Torchlight Wolfbone Properties, Inc., a Texas corporation (“TWP”), entered into with McCabe Petroleum Corporation, a Texas corporation (“MPC”), and Warwink Properties, LLC, a Texas limited liability company (“Warwink Properties”) closed. Under the agreement, which was entered into on November 14, 2017, TWP merged with and into Warwink Properties and the separate existence of TWP ceased, with Warwink Properties becoming the surviving organization and our wholly-owned subsidiary. Warwink Properties was wholly owned by MPC which is wholly owned by Gregory McCabe, our Chairman. Warwink Properties owns certain assets, including a 10.71875% working interest in 640 acres in Winkler County, Texas. At closing of the merger transaction, our shares of common stock of TWP converted into a membership interest of Warwink Properties, the membership interest in Warwink Properties held by MPC ceased to exist, and we issued MPC 2,500,000 restricted shares of common stock as consideration. Also on December 1, 2017, MPC closed its transaction with MECO IV, LLC (“MECO”) for the purchase and sale of certain assets as contemplated by the Purchase and Sale Agreement dated November 9, 2017 (the “MECO PSA”), to which we are not a party. Under the MECO PSA, Warwink Properties received a carry from MECO (through the tanks) of up to \$1,475,000 in the next well drilled on the Winkler County leases. A Certificate of Merger for the merger transaction was filed with the Secretary of State of Texas on December 5, 2017.

Also on December 1, 2017, the transactions contemplated by the Purchase Agreement that our wholly-owned subsidiary, Torchlight Energy, Inc., a Nevada corporation (“TEI”), entered into with MPC closed. Under the Purchase Agreement, which was entered into on November 14, 2017, TEI acquired beneficial ownership of certain of MPC’s assets, including acreage and wellbores located in Ward County, Texas (the “Ward County Assets”). As consideration under the Purchase Agreement, at closing TEI issued to MPC an unsecured promissory note in the principal amount of \$3,250,000, payable in monthly installments of interest only beginning on January 1, 2018, at the rate of 5% per annum, with the entire principal amount together with all accrued interest due and payable on December 31, 2020. In connection with TEI’s acquisition of beneficial ownership in the Ward County Assets, MPC sold those same assets, on behalf of TEI, to MECO at closing of the MECO PSA, and accordingly, TEI received \$3,250,000 in cash for its beneficial interest in the Ward County Assets. Additionally, at closing of the MECO PSA, MPC paid TEI a performance fee of \$2,781,500 in cash as compensation for TEI’s marketing and selling the Winkler County assets of MPC and the Ward County Assets as a package to MECO.



ITEM 1. BUSINESS - continued

Hunton Play, Central Oklahoma

As of December 31, 2017, we were producing from one well in the Viking AMI, and one well in Prairie Grove.

Legal Proceeding

In May, 2016, Torchlight Energy Resources, Inc. and its subsidiary Torchlight Energy, Inc. filed a lawsuit in the 429th judicial district court in Collin County, Texas against Husky Ventures, Inc., Charles V. Long, April Glidewell, Silverstar of Nevada, Inc., Maximus Exploration, LLC, Atwood Acquisitions, LLC, Gastar Exploration Inc., J. Russell Porter, Michael A. Gerlich, Jerry R. Schuyler, and John M. Selser, Sr. Reference is made to Item 3, "Legal Proceedings," for more information regarding this lawsuit.

Viking AMI

In the fourth quarter of 2013 we entered into an Area of Mutual Interest (AMI) with Husky Ventures, the Viking Prospect. We acquired a 25% interest in 3,945 acres and subsequently acquired an additional 5% in May, 2014. We had an interest in 8,800 total acres as of December 31, 2016. (Net undeveloped acres = 2,600) Our net cumulative investment through December 31, 2016 in undeveloped acres in the Viking AMI was \$1,387,928. In addition the company incurred \$133,468 as its share of costs related to the early stages of the construction of a gas pipeline which was to serve the Viking AMI. As of December 31, 2017, to the best knowledge of the Company, substantially all of the leases have expired (although some may have been renewed without notice to Torchlight) and the leases remain subject to settlement negotiations in the legal action referenced above.

Rosedale AMI

In January of 2014 we contracted for a 25% Working Interest in approximately 5,000 acres in the Rosedale AMI consisting of eight townships in South Central Oklahoma. We subsequently acquired an additional 5% in May, 2014. The Company had an interest in 11,600 total acres as of December 31, 2016 (Net undeveloped acres = 3,500) Our cumulative investment through December 31, 2016 in the Rosedale AMI was \$2,833,744. As of December 31, 2017, to the best knowledge of the Company, substantially all of the leases have expired (although some may have been renewed without notice to Torchlight) and the leases remain subject to settlement negotiations in the legal action referenced above.

Prairie Grove – Judy Well

In February of 2014, we acquired a 10% Working Interest in a well in the Prairie Grove AMI from a non-consenting third party who elected not to participate in the well. The well is producing at December 31, 2017.

Thunderbird AMI

In July of 2014, we contracted for a 25% Working Interest in the Thunderbird AMI. The total acres in which the Company has an interest at December 31, 2016 was 4,300 acres (Net undeveloped acres = 1,100). Our cumulative investment through December 31, 2016 in the Thunderbird AMI was \$949,530. As of December 31, 2017, to the best knowledge of the Company, substantially all of the leases have expired (although some may have been renewed without notice to Torchlight) and the leases remain subject to settlement negotiations in the legal action referenced above.

## Industry and Business Environment

We are experiencing a time of fluctuating oil prices caused by lower demand, higher US Supply, and OPEC's policies on production. Unfortunately, this is the cyclical nature of the oil and gas industry. We experience highs and lows that seem to come in cycles. Fortunately, advances in technology drive the US market and we feel this will drive the development costs down on our exploration and drilling programs.

## Competition

The oil and natural gas industry is intensely competitive, and we will compete with numerous other companies engaged in the exploration and production of oil and gas. Some of these companies have substantially greater resources than we have. Not only do they explore for and produce oil and natural gas, but also many carry on midstream and refining operations and market petroleum and other products on a regional, national, or worldwide basis. The operations of other companies may be able to pay more for exploratory prospects and productive oil and natural gas properties. They may also have more resources to define, evaluate, bid for, and purchase a greater number of properties and prospects than our financial or human resources permit.



## ITEM 1. BUSINESS - continued

Our larger or integrated competitors may have the resources to be better able to absorb the burden of current and future federal, state, and local laws and regulations more easily than we can, which would adversely affect our competitive position. Our ability to locate reserves and acquire interests in properties in the future will be dependent upon our ability and resources to evaluate and select suitable properties and consummate transactions in this highly competitive environment. In addition, we may be at a disadvantage in producing oil and natural gas properties and bidding for exploratory prospects because we have fewer financial and human resources than other companies in our industry. Should a larger and better financed company decide to directly compete with us, and be successful in its efforts, our business could be adversely affected.

### Marketing and Customers

The market for oil and natural gas that we will produce depends on factors beyond our control, including the extent of domestic production and imports of oil and natural gas, the proximity and capacity of natural gas pipelines and other transportation facilities, demand for oil and natural gas, the marketing of competitive fuels, and the effects of state and federal regulation. The oil and gas industry also competes with other industries in supplying the energy and fuel requirements of industrial, commercial, and individual consumers.

Our oil production is expected to be sold at prices tied to the spot oil markets. Our natural gas production is expected to be sold under short-term contracts and priced based on first of the month index prices or on daily spot market prices. We will rely on our operating partners to market and sell our production.

### Governmental Regulation and Environmental Matters

Our operations are subject to various rules, regulations, and limitations impacting the oil and natural gas exploration and production industry as a whole.

#### Regulation of Oil and Natural Gas Production

Our oil and natural gas exploration, production, and related operations, when developed, will be subject to extensive rules and regulations promulgated by federal, state, tribal, and local authorities and agencies. Certain states may also have statutes or regulations addressing conservation matters, including provisions for the unitization or pooling of oil and natural gas properties, the establishment of maximum rates of production from wells, and the regulation of spacing, plugging, and abandonment of such wells. Failure to comply with any such rules and regulations can result in substantial penalties. The regulatory burden on the oil and gas industry will most likely increase our cost of doing business and may affect our profitability. Although we believe we are currently in substantial compliance with all applicable laws and regulations, because such rules and regulations are frequently amended or reinterpreted, we are unable to predict the future cost or impact of complying with such laws. Significant expenditures may be required to comply with governmental laws and regulations and may have a material adverse effect on our financial condition and results of operations.

#### Environmental Matters

Our operations and properties are and will be subject to extensive and changing federal, state, and local laws and regulations relating to environmental protection, including the generation, storage, handling, emission, transportation, and discharge of materials into the environment, and relating to safety and health. In the future, environmental legislation and regulation may trend toward stricter standards. These laws and regulations may:

- require the acquisition of a permit or other authorization before construction or drilling commences and for certain other activities;
- limit or prohibit construction, drilling, and other activities on certain lands lying within wilderness and other protected areas;
- impose substantial liabilities for pollution resulting from operations; or
- restrict certain areas from fracking and other stimulation techniques.

The permits required for our operations may be subject to revocation, modification, and renewal by issuing authorities. Governmental authorities have the power to enforce their regulations, and violations are subject to fines or injunctions, or both. In the opinion of management, we are and will be in substantial compliance with current applicable environmental laws and regulations, and have no material commitments for capital expenditures to comply with existing environmental requirements. Nevertheless, changes in existing environmental laws and regulations or in interpretations thereof could have a significant impact on our company, as well as the oil and natural gas industry in general.

The Comprehensive Environmental, Response, Compensation, and Liability Act ("CERCLA") and comparable state statutes impose strict, joint, and several liability on owners and operators of sites and on persons who disposed of or arranged for the disposal of "hazardous substances" found at such sites. It is not uncommon for the neighboring landowners and other third parties to file claims for personal injury and property damage allegedly caused by the hazardous substances released into the environment. The Federal Resource Conservation and Recovery Act ("RCRA") and comparable state statutes govern the disposal of "solid waste" and "hazardous waste" and authorize the imposition of substantial fines and penalties for noncompliance. Although CERCLA currently excludes petroleum from its definition of "hazardous substance," state laws affecting our operations may impose clean-up liability relating to petroleum and petroleum related products. In addition, although RCRA classifies certain oil field wastes as "non-hazardous," such exploration and production wastes could be reclassified as hazardous wastes thereby making such wastes subject to more stringent handling and disposal requirements.



## ITEM 1. BUSINESS - continued

The Endangered Species Act (“ESA”) seeks to ensure that activities do not jeopardize endangered or threatened animal, fish, and plant species, nor destroy or modify the critical habitat of such species. Under ESA, exploration and production operations, as well as actions by federal agencies, may not significantly impair or jeopardize the species or its habitat. ESA provides for criminal penalties for willful violations of the Act. Other statutes that provide protection to animal and plant species and that may apply to our operations include, but are not necessarily limited to, the Fish and Wildlife Coordination Act, the Fishery Conservation and Management Act, the Migratory Bird Treaty Act and the National Historic Preservation Act. Although we believe that our operations will be in substantial compliance with such statutes, any change in these statutes or any reclassification of a species as endangered could subject our company to significant expenses to modify our operations or could force our company to discontinue certain operations altogether.

Hydraulic fracturing is regulated by state and federal oil and gas regulatory authorities, including specifically the requirement to disclose certain information related to hydraulic fracturing operations. Operators must follow applicable legal requirements for groundwater protection in our operations that are subject to supervision by state and federal regulators (including the Bureau of Land Management on federal acreage). Furthermore, well construction practices require the installation of multiple layers of protective steel casing surrounded by cement that are specifically designed and installed to protect freshwater aquifers by preventing the migration of fracturing fluids into aquifers. Regulatory proposals in some states and local communities have been initiated to require or make more stringent the permitting and compliance requirements for hydraulic fracturing operations. Federal and state agencies have continued to assess the impacts of hydraulic fracturing, which could spur further action toward federal and/or state legislation and regulation of hydraulic fracturing activities. In addition, in light of concerns about seismic activity being triggered by the injection of produced waters into underground wells and hydraulic fracturing, certain regulators are also considering additional requirements related to seismic safety for hydraulic fracturing activities. Further restrictions on hydraulic fracturing could make it prohibitive to conduct our operations, and also reduce the amount of oil and natural gas that we or our operators are ultimately able to produce in commercial quantities from our properties.

### Climate Change

Significant studies and research have been devoted to climate change and global warming, and climate change has developed into a major political issue in the United States and globally. Certain research suggests that greenhouse gas emissions contribute to climate change and pose a threat to the environment. Recent scientific research and political debate has focused in part on carbon dioxide and methane incidental to oil and natural gas exploration and production. Many states and the federal government have enacted legislation directed at controlling greenhouse gas emissions, and future legislation and regulation could impose additional restrictions or requirements in connection with our drilling and production activities and favor use of alternative energy sources, which could affect operating costs and demand for oil products. As such, our business could be materially adversely affected by domestic and international legislation targeted at controlling climate change.

### Employees

We currently have four full time employees and no part time employees. We anticipate adding additional employees, when adequate funds are available, and using independent contractors, consultants, attorneys, and accountants as necessary to complement services rendered by our employees. We presently have independent technical professionals under consulting agreements who are available to us on an as needed basis.

### Research and Development

We did not spend any funds on research and development activities during years ended December 31, 2017 or 2016.

#### ITEM 1A. RISK FACTORS

An investment in us involves a high degree of risk and is suitable only for prospective investors with substantial financial means who have no need for liquidity and can afford the entire loss of their investment in us. Prospective investors should carefully consider the following risk factors, in addition to the other information contained in this report.

##### Risks Related to the Company and the Industry

We have a limited operating history relative to larger companies in our industry, and may not be successful in developing profitable business operations.

We have a limited operating history relative to larger companies in our industry. Our business operations must be considered in light of the risks, expenses and difficulties frequently encountered in establishing a business in the oil and natural gas industries. As of the date of this report, we have generated limited revenues and have limited assets. We have an insufficient history at this time on which to base an assumption that our business operations will prove to be successful in the long-term. Our future operating results will depend on many factors, including:



ITEM 1A. RISK FACTORS - continued

our ability to raise adequate working capital;  
the success of our development and exploration;  
the demand for natural gas and oil;  
the level of our competition;  
our ability to attract and maintain key management and employees;  
and  
our ability to efficiently explore, develop, produce or acquire sufficient quantities of marketable natural gas or oil in a highly competitive and speculative environment while maintaining quality and controlling costs.

To achieve profitable operations in the future, we must, alone or with others, successfully manage the factors stated above, as well as continue to develop ways to enhance our production efforts. Despite our best efforts, we may not be successful in our exploration or development efforts, or obtain required regulatory approvals. There is a possibility that some, or all, of the wells in which we obtain interests may never produce oil or natural gas.

We have limited capital and will need to raise additional capital in the future.

We do not currently have sufficient capital to fund both our continuing operations and our planned growth. We will require additional capital to continue to grow our business via acquisitions and to further expand our exploration and development programs. We may be unable to obtain additional capital when required. Future acquisitions and future exploration, development, production and marketing activities, as well as our administrative requirements (such as salaries, insurance expenses and general overhead expenses, as well as legal compliance costs and accounting expenses) will require a substantial amount of additional capital and cash flow.

We may pursue sources of additional capital through various financing transactions or arrangements, including joint venturing of projects, debt financing, equity financing, or other means. We may not be successful in identifying suitable financing transactions in the time period required or at all, and we may not obtain the capital we require by other means. If we do not succeed in raising additional capital, our resources may not be sufficient to fund our planned operations.

Our ability to obtain financing, if and when necessary, may be impaired by such factors as the capital markets (both generally and in the oil and gas industry in particular), our limited operating history, the location of our oil and natural gas properties and prices of oil and natural gas on the commodities markets (which will impact the amount of asset-based financing available to us, if any) and the departure of key employees. Further, if oil or natural gas prices on the commodities markets decline, our future revenues, if any, will likely decrease and such decreased revenues may increase our requirements for capital. If the amount of capital we are able to raise from financing activities, together with our revenues from operations, is not sufficient to satisfy our capital needs (even to the extent that we reduce our operations), we may be required to cease our operations, divest our assets at unattractive prices or obtain financing on unattractive terms.

Any additional capital raised through the sale of equity may dilute the ownership percentage of our stockholders. Raising any such capital could also result in a decrease in the fair market value of our equity securities because our assets would be owned by a larger pool of outstanding equity. The terms of securities we issue in future capital transactions may be more favorable to our new investors, and may include preferences, superior voting rights and the issuance of other derivative securities, and issuances of incentive awards under equity employee incentive plans, which may have a further dilutive effect.

We may incur substantial costs in pursuing future capital financing, including investment banking fees, legal fees, accounting fees, securities law compliance fees, printing and distribution expenses and other costs. We may also be required to recognize non-cash expenses in connection with certain securities we may issue, which may adversely impact our financial condition.

Our auditor indicated that certain factors raise substantial doubt about our ability to continue as a going concern.

The financial statements included with this report are presented under the assumption that we will continue as a going concern, which contemplates the realization of assets and the satisfaction of liabilities in the normal course of business over a reasonable length of time. We had a net loss of approximately \$.9 million for the year ended December 31, 2017 and an accumulated deficit in aggregate of approximately \$83.5 million at year end. We are not generating sufficient operating cash flows to support continuing operations, and expect to incur further losses in the development of our business.

In our financial statements for the year ended December 31, 2017, our auditor indicated that certain factors raised substantial doubt about our ability to continue as a going concern. These factors included our accumulated deficit, as well as the fact that we were not generating sufficient cash flows to meet our regular working capital requirements. Our ability to continue as a going concern is dependent upon our ability to generate future profitable operations and/or to obtain the necessary financing to meet our obligations and repay our liabilities arising from normal business operations when they come due. Management's plan to address our ability to continue as a going concern includes: (1) obtaining debt or equity funding from private placement or institutional sources; (2) obtaining loans from financial institutions, where possible, or (3) participating in joint venture transactions with third parties. Although management believes that it will be able to obtain the necessary funding to allow us to remain a going concern through the methods discussed above, there can be no assurances that such methods will prove successful. The accompanying financial statements do not include any adjustments that might result from the outcome of this uncertainty.



ITEM 1A. RISK FACTORS - continued

As a non-operator, our development of successful operations relies extensively on third-parties who, if not successful, could have a material adverse effect on our results of operation.

We expect to primarily participate in wells operated by third-parties. As a result, we will not control the timing of the development, exploitation, production and exploration activities relating to leasehold interests we acquire. We do, however, have certain rights as granted in our Joint Operating Agreements that allow us a certain degree of freedom such as, but not limited to, the ability to propose the drilling of wells. If our drilling partners are not successful in such activities relating to our leasehold interests, or are unable or unwilling to perform, our financial condition and results of operation could have an adverse material effect.

Further, financial risks are inherent in any operation where the cost of drilling, equipping, completing and operating wells is shared by more than one person. We could be held liable for the joint activity obligations of the operator or other working interest owners such as nonpayment of costs and liabilities arising from the actions of the working interest owners. In the event the operator or other working interest owners do not pay their share of such costs, we would likely have to pay those costs. In such situations, if we were unable to pay those costs, there could be a material adverse effect to our financial position.

Because of the speculative nature of oil and gas exploration, there is risk that we will not find commercially exploitable oil and gas and that our business will fail.

The search for commercial quantities of oil and natural gas as a business is extremely risky. We cannot provide investors with any assurance that any properties in which we obtain a mineral interest will contain commercially exploitable quantities of oil and/or gas. The exploration expenditures to be made by us may not result in the discovery of commercial quantities of oil and/or gas. Problems such as unusual or unexpected formations or pressures, premature declines of reservoirs, invasion of water into producing formations and other conditions involved in oil and gas exploration often result in unsuccessful exploration efforts. If we are unable to find commercially exploitable quantities of oil and gas, and/or we are unable to commercially extract such quantities, we may be forced to abandon or curtail our business plan, and as a result, any investment in us may become worthless.

Strategic relationships upon which we may rely are subject to change, which may diminish our ability to conduct our operations.

Our ability to successfully acquire oil and gas interests, to build our reserves, to participate in drilling opportunities and to identify and enter into commercial arrangements with customers will depend on developing and maintaining close working relationships with industry participants and our ability to select and evaluate suitable properties and to consummate transactions in a highly competitive environment. These realities are subject to change and our inability to maintain close working relationships with industry participants or continue to acquire suitable property may impair our ability to execute our business plan.

To continue to develop our business, we will endeavor to use the business relationships of our management to enter into strategic relationships, which may take the form of joint ventures with other private parties and contractual arrangements with other oil and gas companies, including those that supply equipment and other resources that we will use in our business. We may not be able to establish these strategic relationships, or if established, we may not be able to maintain them. In addition, the dynamics of our relationships with strategic partners may require us to incur expenses or undertake activities we would not otherwise be inclined to in order to fulfill our obligations to these partners or maintain our relationships. If our strategic relationships are not established or maintained, our business prospects may be limited, which could diminish our ability to conduct our operations.

The price of oil and natural gas has historically been volatile. If it were to decrease substantially, our projections, budgets, and revenues would be adversely affected, potentially forcing us to make changes in our operations.

Our future financial condition, results of operations and the carrying value of any oil and natural gas interests we acquire will depend primarily upon the prices paid for oil and natural gas production. Oil and natural gas prices historically have been volatile and likely will continue to be volatile in the future, especially given current world geopolitical conditions. Our cash flows from operations are highly dependent on the prices that we receive for oil and natural gas. This price volatility also affects the amount of our cash flows available for capital expenditures and our ability to borrow money or raise additional capital. The prices for oil and natural gas are subject to a variety of additional factors that are beyond our control. These factors include:

- the level of consumer demand for oil and natural gas;
- the domestic and foreign supply of oil and natural gas;
- the ability of the members of the Organization of Petroleum Exporting Countries ("OPEC") to agree to and maintain oil price and production controls;
- the price of foreign oil and natural gas;
- domestic governmental regulations and taxes;
- the price and availability of alternative fuel sources;
- weather conditions;
- market uncertainty due to political conditions in oil and natural gas producing regions, including the Middle East;
- and
- worldwide economic conditions.



ITEM 1A. RISK FACTORS - continued

These factors as well as the volatility of the energy markets generally make it extremely difficult to predict future oil and natural gas price movements with any certainty. Declines in oil and natural gas prices affect our revenues, and could reduce the amount of oil and natural gas that we can produce economically. Accordingly, such declines could have a material adverse effect on our financial condition, results of operations, oil and natural gas reserves and the carrying values of our oil and natural gas properties. If the oil and natural gas industry experiences significant price declines, we may be unable to make planned expenditures, among other things. If this were to happen, we may be forced to abandon or curtail our business operations, which would cause the value of an investment in us to decline or become worthless.

If oil or natural gas prices remain depressed or drilling efforts are unsuccessful, we may be required to record additional write downs of our oil and natural gas properties.

If oil or natural gas prices remain depressed or drilling efforts are unsuccessful, we could be required to write down the carrying value of certain of our oil and natural gas properties. Write downs may occur when oil and natural gas prices are low, or if we have downward adjustments to our estimated proved reserves, increases in our estimates of operating or development costs, deterioration in drilling results or mechanical problems with wells where the cost to re drill or repair is not supported by the expected economics.

Under the full cost method of accounting, capitalized oil and gas property costs less accumulated depletion and net of deferred income taxes may not exceed an amount equal to the present value, discounted at 10%, of estimated future net revenues from proved oil and gas reserves plus the cost of unproved properties not subject to amortization (without regard to estimates of fair value), or estimated fair value, if lower, of unproved properties that are subject to amortization. Should capitalized costs exceed this ceiling, an impairment would be recognized.

The Company recognized an impairment charge of \$70,080 for the year 2016.

During the year ended December 31, 2017 the Company performed assessments of evaluated and unevaluated costs in the cost pool to conform the cumulative value of the Full Cost Pool to the combined amount of Reserve Value of evaluated, producing properties (as determined by independent analysis at December 31, 2017), plus the lesser of cumulative historical cost or estimated realizable value of unevaluated leases and projects expected to commence production in future operating periods. The Company identified impairment of \$2,300,626 in 2017 related to its unevaluated properties. Although we had no recognized impairment expense in 2017, the Company has adjusted the separation of evaluated versus unevaluated costs within its full cost pool to recognize the value impairment related to the expiration of unevaluated leases in 2017 in the amount of \$2,300,626. The impact of this change will be to increase the basis for calculation of future period's depletion, depreciation and amortization to include \$2,300,626 of cost which will effectively recognize the impairment on the Statement of Income over future periods. The \$2,300,626 has also become an evaluated cost for purposes of future period's Ceiling Tests and which may further recognize the impairment expense recognized in future periods.

Because of the inherent dangers involved in oil and gas operations, there is a risk that we may incur liability or damages as we conduct our business operations, which could force us to expend a substantial amount of money in connection with litigation and/or a settlement.

The oil and natural gas business involves a variety of operating hazards and risks such as well blowouts, pipe failures, casing collapse, explosions, uncontrollable flows of oil, natural gas or well fluids, fires, spills, pollution, releases of toxic gas and other environmental hazards and risks. These hazards and risks could result in substantial losses to us from, among other things, injury or loss of life, severe damage to or destruction of property, natural resources and

equipment, pollution or other environmental damage, cleanup responsibilities, regulatory investigation and penalties and suspension of operations. In addition, we may be liable for environmental damages caused by previous owners of property purchased and leased by us. In recent years, there has also been increased scrutiny on the environmental risk associated with hydraulic fracturing, such as underground migration and surface spillage or mishandling of fracturing fluids including chemical additives. As a result, substantial liabilities to third parties or governmental entities may be incurred, the payment of which could reduce or eliminate the funds available for exploration, development or acquisitions or result in the loss of our properties and/or force us to expend substantial monies in connection with litigation or settlements. We currently have no insurance to cover such losses and liabilities, and even if insurance is obtained, there can be no assurance that it will be adequate to cover any losses or liabilities. We cannot predict the availability of insurance or the availability of insurance at premium levels that justify our purchase. The occurrence of a significant event not fully insured or indemnified against could materially and adversely affect our financial condition and operations. We may elect to self-insure if management believes that the cost of insurance, although available, is excessive relative to the risks presented. In addition, pollution and environmental risks generally are not fully insurable. The occurrence of an event not fully covered by insurance could have a material adverse effect on our financial condition and results of operations, which could lead to any investment in us becoming worthless.

The market for oil and gas is intensely competitive, and competition pressures could force us to abandon or curtail our business plan.

The market for oil and gas exploration services is highly competitive, and we only expect competition to intensify in the future. Numerous well-established companies are focusing significant resources on exploration and are currently competing with us for oil and gas opportunities. Other oil and gas companies may seek to acquire oil and gas leases and properties that we have targeted. Additionally, other companies engaged in our line of business may compete with us from time to time in obtaining capital from investors. Competitors include larger companies which, in particular, may have access to greater resources, may be more successful in the recruitment and retention of qualified employees and may conduct their own refining and petroleum marketing operations, which may give them a competitive advantage. Actual or potential competitors may be strengthened through the acquisition of additional assets and interests. Additionally, there are numerous companies focusing their resources on creating fuels and/or materials which serve the same purpose as oil and gas, but are manufactured from renewable resources.



ITEM 1A. RISK FACTORS - continued

As a result, there can be no assurance that we will be able to compete successfully or that competitive pressures will not adversely affect our business, results of operations, and financial condition. If we are not able to successfully compete in the marketplace, we could be forced to curtail or even abandon our current business plan, which could cause any investment in us to become worthless.

We may not be able to successfully manage our growth, which could lead to our inability to implement our business plan.

Our growth may place a significant strain on our managerial, operational and financial resources, especially considering that we currently only have a small number of executive officers, employees and advisors. Further, as we enter into additional contracts, we will be required to manage multiple relationships with various consultants, businesses and other third parties. These requirements will be exacerbated in the event of our further growth or in the event that the number of our drilling and/or extraction operations increases. There can be no assurance that our systems, procedures and/or controls will be adequate to support our operations or that our management will be able to achieve the rapid execution necessary to successfully implement our business plan. If we are unable to manage our growth effectively, our business, results of operations and financial condition will be adversely affected, which could lead to us being forced to abandon or curtail our business plan and operations.

Our operations are heavily dependent on current environmental regulation, changes in which we cannot predict.

Oil and natural gas activities that we will engage in, including production, processing, handling and disposal of hazardous materials, such as hydrocarbons and naturally occurring radioactive materials (if any), are subject to stringent regulation. We could incur significant costs, including cleanup costs resulting from a release of hazardous material, third-party claims for property damage and personal injuries fines and sanctions, as a result of any violations or liabilities under environmental or other laws. Changes in or more stringent enforcement of environmental laws could force us to expend additional operating costs and capital expenditures to stay in compliance.

Various federal, state and local laws regulating the discharge of materials into the environment, or otherwise relating to the protection of the environment, directly impact oil and gas exploration, development and production operations, and consequently may impact our operations and costs. These regulations include, among others, (i) regulations by the Environmental Protection Agency and various state agencies regarding approved methods of disposal for certain hazardous and non-hazardous wastes; (ii) the Comprehensive Environmental Response, Compensation, and Liability Act, Federal Resource Conservation and Recovery Act and analogous state laws which regulate the removal or remediation of previously disposed wastes (including wastes disposed of or released by prior owners or operators), property contamination (including groundwater contamination), and remedial plugging operations to prevent future contamination; (iii) the Clean Air Act and comparable state and local requirements which may result in the gradual imposition of certain pollution control requirements with respect to air emissions from our operations; (iv) the Oil Pollution Act of 1990 which contains numerous requirements relating to the prevention of and response to oil spills into waters of the United States; (v) the Resource Conservation and Recovery Act which is the principal federal statute governing the treatment, storage and disposal of hazardous wastes; and (vi) state regulations and statutes governing the handling, treatment, storage and disposal of naturally occurring radioactive material.

Management believes that we will be in substantial compliance with applicable environmental laws and regulations. To date, we have not expended any amounts to comply with such regulations, and management does not currently anticipate that future compliance will have a materially adverse effect on our consolidated financial position, results of operations or cash flows. However, if we are deemed to not be in compliance with applicable environmental laws, we could be forced to expend substantial amounts to be in compliance, which would have a materially adverse effect on

our financial condition. If this were to happen, any investment in us could be lost.

Government regulatory initiatives relating to hydraulic fracturing could result in increased costs and additional operating restrictions or delays.

Vast quantities of natural gas, natural gas liquids and oil deposits exist in deep shale and other unconventional formations. It is customary in our industry to recover these resources through the use of hydraulic fracturing, combined with horizontal drilling. Hydraulic fracturing is the process of creating or expanding cracks, or fractures, in deep underground formations using water, sand and other additives pumped under high pressure into the formation. As with the rest of the industry, our third-party operating partners use hydraulic fracturing as a means to increase the productivity of most of the wells they drill and complete. These formations are generally geologically separated and isolated from fresh ground water supplies by thousands of feet of impermeable rock layers.

We believe our third-party operating partners follow applicable legal requirements for groundwater protection in their operations that are subject to supervision by state and federal regulators. Furthermore, we believe our third-party operating partners' well construction practices are specifically designed to protect freshwater aquifers by preventing the migration of fracturing fluids into aquifers.

Hydraulic fracturing is typically regulated by state oil and gas commissions. Some states have adopted, and other states are considering adopting, regulations that could impose more stringent permitting, public disclosure, and/or well construction requirements on hydraulic fracturing operations.



ITEM 1A. RISK FACTORS - continued

In addition to state laws, some local municipalities have adopted or are considering adopting land use restrictions, such as city ordinances, that may restrict or prohibit the performance of well drilling in general and/or hydraulic fracturing in particular. There are also certain governmental reviews either underway or being proposed that focus on deep shale and other formation completion and production practices, including hydraulic fracturing. Depending on the outcome of these studies, federal and state legislatures and agencies may seek to further regulate such activities. Certain environmental and other groups have also suggested that additional federal, state and local laws and regulations may be needed to more closely regulate the hydraulic fracturing process.

Further, the EPA has asserted federal regulatory authority over hydraulic fracturing involving “diesel fuels” under the SWDA’s UIC Program. The EPA is also engaged in a study of the potential impacts of hydraulic fracturing activities on drinking water resources in the states where the EPA is the permitting authority. These actions, in conjunction with other analyses by federal and state agencies to assess the impacts of hydraulic fracturing could spur further action toward federal and/or state legislation and regulation of hydraulic fracturing activities.

We cannot predict whether additional federal, state or local laws or regulations applicable to hydraulic fracturing will be enacted in the future and, if so, what actions any such laws or regulations would require or prohibit. Restrictions on hydraulic fracturing could make it prohibitive for our third-party operating partners to conduct operations, and also reduce the amount of oil, natural gas liquids and natural gas that we are ultimately able to produce in commercial quantities from our properties. If additional levels of regulation or permitting requirements were imposed on hydraulic fracturing operations, our business and operations could be subject to delays, increased operating and compliance costs and process prohibitions.

Our estimates of the volume of reserves could have flaws, or such reserves could turn out not to be commercially extractable. As a result, our future revenues and projections could be incorrect.

Estimates of reserves and of future net revenues prepared by different petroleum engineers may vary substantially depending, in part, on the assumptions made and may be subject to adjustment either up or down in the future. Our actual amounts of production, revenue, taxes, development expenditures, operating expenses, and quantities of recoverable oil and gas reserves may vary substantially from the estimates. Oil and gas reserve estimates are necessarily inexact and involve matters of subjective engineering judgment. In addition, any estimates of our future net revenues and the present value thereof are based on assumptions derived in part from historical price and cost information, which may not reflect current and future values, and/or other assumptions made by us that only represent our best estimates. If these estimates of quantities, prices and costs prove inaccurate, we may be unsuccessful in expanding our oil and gas reserves base with our acquisitions. Additionally, if declines in and instability of oil and gas prices occur, then write downs in the capitalized costs associated with any oil and gas assets we obtain may be required. Because of the nature of the estimates of our reserves and estimates in general, we can provide no assurance that reductions to our estimated proved oil and gas reserves and estimated future net revenues will not be required in the future, and/or that our estimated reserves will be present and/or commercially extractable. If our reserve estimates are incorrect, the value of our common stock could decrease and we may be forced to write down the capitalized costs of our oil and gas properties.

Decommissioning costs are unknown and may be substantial. Unplanned costs could divert resources from other projects.

We may become responsible for costs associated with abandoning and reclaiming wells, facilities and pipelines which we use for production of oil and natural gas reserves. Abandonment and reclamation of these facilities and the costs associated therewith is often referred to as “decommissioning.” We accrue a liability for decommissioning costs

associated with our wells, but have not established any cash reserve account for these potential costs in respect of any of our properties. If decommissioning is required before economic depletion of our properties or if our estimates of the costs of decommissioning exceed the value of the reserves remaining at any particular time to cover such decommissioning costs, we may have to draw on funds from other sources to satisfy such costs. The use of other funds to satisfy such decommissioning costs could impair our ability to focus capital investment in other areas of our business.

We may have difficulty distributing production, which could harm our financial condition.

In order to sell the oil and natural gas that we are able to produce, if any, the operators of the wells we obtain interests in may have to make arrangements for storage and distribution to the market. We will rely on local infrastructure and the availability of transportation for storage and shipment of our products, but infrastructure development and storage and transportation facilities may be insufficient for our needs at commercially acceptable terms in the localities in which we operate. This situation could be particularly problematic to the extent that our operations are conducted in remote areas that are difficult to access, such as areas that are distant from shipping and/or pipeline facilities. These factors may affect our and potential partners' ability to explore and develop properties and to store and transport oil and natural gas production, increasing our expenses.

Furthermore, weather conditions or natural disasters, actions by companies doing business in one or more of the areas in which we will operate, or labor disputes may impair the distribution of oil and/or natural gas and in turn diminish our financial condition or ability to maintain our operations.

Our business will suffer if we cannot obtain or maintain necessary licenses.

Our operations will require licenses, permits and in some cases renewals of licenses and permits from various governmental authorities. Our ability to obtain, sustain or renew such licenses and permits on acceptable terms is subject to change in regulations and policies and to the discretion of the applicable governments, among other factors. Our inability to obtain, or our loss of or denial of extension of, any of these licenses or permits could hamper our ability to produce revenues from our operations.



ITEM 1A. RISK FACTORS - continued

Challenges to our properties may impact our financial condition.

Title to oil and gas interests is often not capable of conclusive determination without incurring substantial expense. While we intend to make appropriate inquiries into the title of properties and other development rights we acquire, title defects may exist. In addition, we may be unable to obtain adequate insurance for title defects, on a commercially reasonable basis or at all. If title defects do exist, it is possible that we may lose all or a portion of our right, title and interests in and to the properties to which the title defects relate. If our property rights are reduced, our ability to conduct our exploration, development and production activities may be impaired. To mitigate title problems, common industry practice is to obtain a title opinion from a qualified oil and gas attorney prior to the drilling operations of a well.

We rely on technology to conduct our business, and our technology could become ineffective or obsolete.

We rely on technology, including geographic and seismic analysis techniques and economic models, to develop our reserve estimates and to guide our exploration, development and production activities. We and our operator partners will be required to continually enhance and update our technology to maintain its efficacy and to avoid obsolescence. The costs of doing so may be substantial and may be higher than the costs that we anticipate for technology maintenance and development. If we are unable to maintain the efficacy of our technology, our ability to manage our business and to compete may be impaired. Further, even if we are able to maintain technical effectiveness, our technology may not be the most efficient means of reaching our objectives, in which case we may incur higher operating costs than we would were our technology more efficient.

The loss of key personnel would directly affect our efficiency and profitability.

Our future success is dependent, in a large part, on retaining the services of our current management team. Our executive officers possess a unique and comprehensive knowledge of our industry and related matters that are vital to our success within the industry. The knowledge, leadership and technical expertise of these individuals would be difficult to replace. The loss of one or more of our officers could have a material adverse effect on our operating and financial performance, including our ability to develop and execute our long-term business strategy. We do not maintain key-man life insurance with respect to any employees. We do have employment agreements with each of our executive officers. There can be no assurance, however, that any of our officers will continue to be employed by us.

Our officers and directors control a significant percentage of our current outstanding common stock and their interests may conflict with those of our stockholders.

As of the date of this report, our executive officers and directors collectively and beneficially own approximately 32% of our outstanding common stock (see Item 12 of this report for an explanation of how this number is computed). This concentration of voting control gives these affiliates substantial influence over any matters which require a stockholder vote, including without limitation the election of directors and approval of merger and/or acquisition transactions, even if their interests may conflict with those of other stockholders. It could have the effect of delaying or preventing a change in control or otherwise discouraging a potential acquirer from attempting to obtain control of us. This could have a material adverse effect on the market price of our common stock or prevent our stockholders from realizing a premium over the then prevailing market prices for their shares of common stock.

In the future, we may incur significant increased costs as a result of operating as a public company, and our management may be required to devote substantial time to new compliance initiatives.

In the future, we may incur significant legal, accounting, and other expenses as a result of operating as a public company. The Sarbanes-Oxley Act of 2002 (the “Sarbanes-Oxley Act”), as well as new rules subsequently implemented by the SEC, have imposed various requirements on public companies, including requiring changes in corporate governance practices. Our management and other personnel will need to devote a substantial amount of time to these new compliance initiatives. Moreover, these rules and regulations will increase our legal and financial compliance costs and will make some activities more time-consuming and costly. For example, we expect these new rules and regulations to make it more difficult and more expensive for us to obtain director and officer liability insurance, and we may be required to incur substantial costs to maintain the same or similar coverage.

In addition, the Sarbanes-Oxley Act requires, among other things, that we maintain effective internal controls for financial reporting and disclosure controls and procedures. In particular, we are required to perform system and process evaluation and testing on the effectiveness of our internal controls over financial reporting, as required by Section 404 of the Sarbanes-Oxley Act. In performing this evaluation and testing, management concluded that our internal control over financial reporting is effective as of December 31, 2017. Our continued compliance with Section 404, will require that we incur substantial accounting expense and expend significant management efforts. We do not have an internal audit group. We have however, engaged independent professional assistance for the evaluation and testing of internal controls.

Terrorist attacks or cyber-incidents could result in information theft, data corruption, operational disruption and/or financial loss.

Like most companies, we have become increasingly dependent upon digital technologies, including information systems, infrastructure and cloud applications and services, to operate our businesses, to process and record financial and operating data, communicate with our business partners, analyze mine and mining information, estimate quantities of coal reserves, as well as other activities related to our businesses. Strategic targets, such as energy-related assets, may be at greater risk of future terrorist or cyber-attacks than other targets in the United States. Deliberate attacks on, or security breaches in, our systems or infrastructure, or the systems or infrastructure of third parties, or cloud-based applications could lead to corruption or loss of our proprietary data and potentially sensitive data, delays in production or delivery, difficulty in completing and settling transactions, challenges in maintaining our books and records, environmental damage, communication interruptions, other operational disruptions and third-party liability. Our insurance may not protect us against such occurrences. Consequently, it is possible that any of these occurrences, or a combination of them, could have a material adverse effect on our business, financial condition, results of operations and cash flows. Further, as cyber incidents continue to evolve, we may be required to expend additional resources to continue to modify or enhance our protective measures or to investigate and remediate any vulnerability to cyber incidents.



## ITEM 1A. RISK FACTORS - continued

### Certain Factors Related to Our Common Stock

There presently is a limited market for our common stock, and the price of our common stock may be volatile.

Our common stock is currently quoted on The NASDAQ Stock Market LLC. There could be volatility in the volume and market price of our common stock moving forward. This volatility may be caused by a variety of factors, including the lack of readily available quotations, the absence of consistent administrative supervision of “bid” and “ask” quotations, and generally lower trading volume. In addition, factors such as quarterly variations in our operating results, changes in financial estimates by securities analysts, or our failure to meet our or their projected financial and operating results, litigation involving us, factors relating to the oil and gas industry, actions by governmental agencies, national economic and stock market considerations, as well as other events and circumstances beyond our control could have a significant impact on the future market price of our common stock and the relative volatility of such market price.

Offers or availability for sale of a substantial number of shares of our common stock may cause the price of our common stock to decline.

Our stockholders could sell substantial amounts of common stock in the public market, including shares sold upon the filing of a registration statement that registers such shares and/or upon the expiration of any statutory holding period under Rule 144 of the Securities Act of 1933 (the “Securities Act”), if available, or upon the expiration of trading limitation periods. Such volume could create a circumstance commonly referred to as a market “overhang” and in anticipation of which the market price of our common stock could fall. Additionally, we have a large number of warrants that are presently exercisable. The exercise of a large amount of these securities followed by the subsequent sale of the underlying stock in the market would likely have a negative effect on our common stock’s market price. The existence of an overhang, whether or not sales have occurred or are occurring, also could make it more difficult for us to secure additional financing through the sale of equity or equity-related securities in the future at a time and price that we deem reasonable or appropriate.

Our directors and officers have rights to indemnification.

Our Bylaws provide, as permitted by governing Nevada law, that we will indemnify our directors, officers, and employees, whether or not then in service as such, against all reasonable expenses actually and necessarily incurred by him or her in connection with the defense of any litigation to which the individual may have been made a party because he or she is or was a director, officer, or employee of the company. The inclusion of these provisions in the Bylaws may have the effect of reducing the likelihood of derivative litigation against directors and officers, and may discourage or deter stockholders or management from bringing a lawsuit against directors and officers for breach of their duty of care, even though such an action, if successful, might otherwise have benefited us and our stockholders.

We do not anticipate paying any cash dividends on our common stock.

We do not anticipate paying cash dividends on our common stock for the foreseeable future. The payment of dividends, if any, would be contingent upon our revenues and earnings, if any, capital requirements, and general financial condition. The payment of any dividends will be within the discretion of our Board of Directors. We presently intend to retain all earnings, if any, to implement our business strategy; accordingly, we do not anticipate the declaration of any dividends in the foreseeable future.

## ITEM 1B. UNRESOLVED STAFF COMMENTS

Not Applicable.

## ITEM 2. PROPERTIES

Our principal executive offices are located at 5700 W. Plano Parkway, Suite 3600, Plano, Texas 75093. We currently lease this office space which totals approximately 3,181 square feet. We believe that the condition and size of our offices are adequate for our current needs.

Investment in oil and gas properties during the years ended December 31, 2017 and 2016 is detailed as follows:

|                            | 2017         | 2016        |
|----------------------------|--------------|-------------|
| Property acquisition costs | \$7,227,362  | \$3,265,807 |
| Development costs          | \$8,034,962  | \$2,055,526 |
| Exploratory costs          | \$-          | \$-         |
| Totals                     | \$15,262,324 | \$5,321,333 |

Property acquisition costs presented above exclude interest capitalized into the full cost pool of \$1,010,868 in 2017 and \$215,938 in 2016.



## ITEM 2. PROPERTIES - continued

Property acquisition cost relates to the Company's acquisition of additional working interests in the Hazel Project in west Texas and the acquisition of the Warwink Project, also in west Texas. The development costs include work in the Orogrande and Hazel projects in west Texas. No development costs were incurred for Oklahoma properties in 2017.

## Oil and Natural Gas Reserves

## Reserve Estimates

SEC Case. The following tables sets forth, as of December 31, 2017, our estimated net proved oil and natural gas reserves, the estimated present value (discounted at an annual rate of 10%) of estimated future net revenues before future income taxes (PV-10) and after future income taxes (Standardized Measure) of our proved reserves and our estimated net probable oil and natural gas reserves, each prepared using standard geological and engineering methods generally accepted by the petroleum industry and in accordance with assumptions prescribed by the Securities and Exchange Commission ("SEC"). All of our reserves are located in the United States.

The PV-10 value is a widely used measure of value of oil and natural gas assets and represents a pre-tax present value of estimated cash flows discounted at ten percent. PV-10 is considered a non-GAAP financial measure as defined by the SEC. We believe that our PV-10 presentation is relevant and useful to our investors because it presents the estimated discounted future net cash flows attributable to our proved reserves before taking into account the related future income taxes, as such taxes may differ among various companies. We believe investors and creditors use PV-10 as a basis for comparison of the relative size and value of our proved reserves to the reserve estimates of other companies. PV-10 is not a measure of financial or operating performance under GAAP and neither it nor the Standardized Measure is intended to represent the current market value of our estimated oil and natural gas reserves. PV-10 should not be considered in isolation or as a substitute for the standardized measure of discounted future net cash flows as defined under GAAP.

The estimates of our proved reserves and the PV-10 set forth herein reflect estimated future gross revenue to be generated from the production of proved reserves, net of estimated production and future development costs, using prices and costs under existing economic conditions at December 31, 2017. For purposes of determining prices, we used the average of prices received for each month within the 12-month period ended December 31, 2017, adjusted for quality and location differences, which was \$48.53 per barrel of oil and \$2.58 per MCF of gas. This average historical price is not a prediction of future prices. The amounts shown do not give effect to non-property related expenses, such as corporate general administrative expenses and debt service, future income taxes or to depreciation, depletion and amortization.

December 31, 2017

December 31, 2017

Reserves

Future Net Revenue (M\$)

Present Value Discounted

| Category | Oil (Bbls) | Gas (Mcf) | Total (BOE) | Total | at 10% |
|----------|------------|-----------|-------------|-------|--------|
|----------|------------|-----------|-------------|-------|--------|

|                     |       |        |       |       |      |
|---------------------|-------|--------|-------|-------|------|
| Proved Producing    | 2,300 | 43,800 | 9,600 | \$132 | \$96 |
| Proved Nonproducing | 0     | 0      | 0     | \$-   | \$-  |
| Total Proved        | 2,300 | 43,800 | 9,600 | \$132 | \$96 |

Standardized Measure of Future Net Cash Flows Related to Proved Oil and Gas Properties \$123

|                      |   |   |   |     |     |
|----------------------|---|---|---|-----|-----|
| Probable Undeveloped | 0 | 0 | 0 | \$- | \$- |
|----------------------|---|---|---|-----|-----|



## ITEM 2. PROPERTIES - continued

| December 31, 2016                                                                      |            |           |             | December 31, 2016        |        |
|----------------------------------------------------------------------------------------|------------|-----------|-------------|--------------------------|--------|
| Reserves                                                                               |            |           |             | Future Net Revenue (M\$) |        |
|                                                                                        |            |           |             | Present Value Discounted |        |
| Category                                                                               | Oil (Bbls) | Gas (Mcf) | Total (BOE) | Total                    | at 10% |
| Proved Producing                                                                       | 1,400      | 23,300    | 5,284       | \$31                     | \$29   |
| Proved Nonproducing                                                                    | 46,800     | 467,600   | 124,733     | \$776                    | \$301  |
| Total Proved                                                                           | 48,200     | 490,900   | 130,017     | \$807                    | \$330  |
| Standardized Measure of Future Net Cash Flows Related to Proved Oil and Gas Properties |            |           |             | \$341                    |        |
| Probable Undeveloped                                                                   | 0          | 0         | 0           | \$-                      | \$-    |

The upward revisions of previous estimates from 2016 to 2017 of proved producing reserves of 900 BBLS and 20,500 MCF results primarily from 2017 reserve report calculations for the Company's properties driven by industry conditions and the change in the proportional quantities of oil and gas in production from the Judy well in Oklahoma from 2016 to 2017.

Reserve values as of December 31, 2017 are related to a single producing well in Oklahoma – the Judy well in the Prairie Grove AMI.

BOE equivalents are determined by combining barrels of oil with MCF of gas divided by six.

Standardized Measure of  
Oil & Gas Quantities -  
Volume Rollforward  
Year Ended December  
31, 2017

The following table sets  
forth the Company's net  
proved reserves,  
including the changes  
therein, and proved

developed reserves:

Crude Oil (Bbls)    Natural Gas (Mcf)    BOE

**TOTAL PROVED RESERVES:**

|                                             |          |           |           |
|---------------------------------------------|----------|-----------|-----------|
| Beginning of period                         | 48,200   | 490,900   | 130,017   |
| Revisions of previous estimates             | (35,509) | (437,841) | (108,483) |
| Extensions, discoveries and other additions | -        | -         | -         |
| Divestiture of Reserves                     | -        | -         | -         |
| Acquisition of Reserves                     | -        | -         | -         |
| Production                                  | (10,391) | (9,259)   | (11,934)  |
| End of period                               | 2,300    | 43,800    | 9,600     |

**PROVED DEVELOPED RESERVES**

|                            |       |        |       |
|----------------------------|-------|--------|-------|
| Proved developed producing | 2,300 | 43,800 | 9,600 |
| Proved nonproducing        | -     | -      | -     |
| Total                      | 2,300 | 43,800 | 9,600 |



## ITEM 2. PROPERTIES - continued

## Standardized Measure of Oil &amp; Gas Quantities

Year Ended December 31, 2017 &amp; 2016

The standardized measure of discounted future net cash flows relating

to proved oil and natural gas reserves is as follows :      2017              2016

|                                                                                     |           |             |
|-------------------------------------------------------------------------------------|-----------|-------------|
| Future cash inflows                                                                 | \$240,370 | \$3,156,970 |
| Future production costs                                                             | (108,000) | (1,000,410) |
| Future development costs                                                            | -         | (1,350,000) |
| Future income tax expense                                                           | -         | -           |
| Future net cash flows                                                               | 132,370   | 806,560     |
| 10% annual discount for estimated timing of cash flows                              | (9,102)   | (465,644)   |
| Standardized measure of discounted future net cash flows related to proved reserves | \$123,268 | \$340,916   |

A summary of the changes in the standardized measure of discounted future net cash flows applicable to proved oil and natural gas reserves

is as follows :

|                                                                                                        | 2017      | 2016        |
|--------------------------------------------------------------------------------------------------------|-----------|-------------|
| Balance, beginning of period                                                                           | \$340,916 | \$5,935,188 |
| Net change in sales and transfer prices and in production (lifting) costs related to future production | 207,241   | (482,569)   |
| Changes in estimated future development costs                                                          | 116,934   | (791,630)   |
| Net change due to revisions in quantity estimates                                                      | (129,565) | 482,272     |
| Accretion of discount                                                                                  | 28,604    | 80,393      |
| Other                                                                                                  | (43,372)  | 172,169     |
| Net change due to extensions and discoveries                                                           | -         | -           |
| Net change due to sales of minerals in place                                                           | -         | (191,470)   |

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|                                                                   |           |             |
|-------------------------------------------------------------------|-----------|-------------|
| Sales and transfers of oil and gas produced during the period     | (397,490) | (29,749)    |
| Previously estimated development costs incurred during the period | -         | 58,575      |
| Net change in income taxes                                        | -         | (4,892,263) |
| Balance, end of period                                            | \$123,268 | \$340,916   |

Due to the inherent uncertainties and the limited nature of reservoir data, both proved and probable reserves are subject to change as additional information becomes available. The estimates of reserves, future cash flows, and present value are based on various assumptions, including those prescribed by the SEC, and are inherently imprecise. Although we believe these estimates are reasonable, actual future production, cash flows, taxes, development expenditures, operating expenses, and quantities of recoverable oil and natural gas reserves may vary substantially from these estimates.

In estimating probable reserves, it should be noted that those reserve estimates inherently involve greater risk and uncertainty than estimates of proved reserves. While analysis of geoscience and engineering data provides reasonable certainty that proved reserves can be economically producible from known formations under existing conditions and within a reasonable time, probable reserves involve less certainty than reserves with a higher classification due to less data to support their ultimate recovery. Probable reserves have not been discounted for the additional risk associated with future recovery. Prospective investors should be aware that as the categories of reserves decrease with certainty, the risk of recovering reserves at the PV-10 calculation increases. The reserves and net present worth discounted at 10% relating to the different categories of proved and probable have not been adjusted for risk due to their uncertainty of recovery and thus are not comparable and should not be summed into total amounts.

#### Reserve Estimation Process, Controls and Technologies

The reserve estimates, including PV-10 estimates, set forth above were prepared by PeTech Enterprises, Inc. for the Company's Properties in Oklahoma. A copy of their full reports with regard to our reserves is attached as Exhibit 99.1 to this annual report on Form 10-K. These calculations were prepared using standard geological and engineering methods generally accepted by the petroleum industry and in accordance with SEC financial accounting and reporting standards.



## ITEM 2. PROPERTIES - continued

We do not have any employees with specific reservoir engineering qualifications in the company. Our Chairman and Chief Executive Officer worked closely with PeTech Enterprises Inc. in connection with their preparation of our reserve estimates, including assessing the integrity, accuracy, and timeliness of the methods and assumptions used in this process.

PeTech Enterprises, Inc. ("PeTech"), who provided 2017 reserve estimates for our Oklahoma Properties, is a Texas based family owned oil and gas production and investment company that provides reservoir engineering, economics and valuation support to energy banks, energy companies and law firms as an expert witness. PeTech has been in business since 1982. Amiel David is the President of PeTech and the primary technical person in charge of the estimates of reserves and associated cash flow and economics on behalf of the company for the results presented in its reserves report to us. He has a PhD in Petroleum Engineering from Stanford University. He is a registered Professional Engineer in the state of Texas (PE #50970), granted in 1982, a member of the Society of Petroleum Engineers and a member of the Society of Petroleum Evaluation Engineers.

### Proved Nonproducing Reserves

As of December 31, 2017, our proved nonproducing reserves totaled -0- barrels of oil equivalents (BOE) compared to 124,733 as of December 31, 2016, a decrease of 124,733 BOE. The proved nonproducing reserves at December 31, 2016 were associated with our Hunton project Judy and Loki wells located in Oklahoma. The Loki well was determined to be uneconomic at 12/31/17. The change consists of a decrease of 124,733 BOE based on the 2017 engineering. These numbers are taken from the third party reserves studies prepared by PeTech for 2017 and 2016. The net reserves change associated with nonproducing reserves from this property is a decrease of approximately 46,800 bbls of oil and a decrease of approximately 467,600 Mcf of gas (calculated with a gas-oil equivalency factor of six). The Company does not intend to pursue any behind pipe reserves which may exist and there is no additional acreage available to consider future development.

We made investments and development progress during 2017 to further develop proved producing reserves in the Orogrande and Hazel Projects in the Permian Basin in West Texas. As of December 31, 2017 three test wells have been developed in the Orogrande Project and four test wells have been developed in the Hazel Project. Although the Hazel wells have each produced a quantity of oil (the Flying B #3 is in continuous production at December 31, 2017), the wells remain categorized as test wells for 2017.

Our current drilling plans, subject to sufficient capital resources and the periodic evaluation of interim drilling results and other potential investment opportunities, include drilling additional evaluation wells in the Orogrande and Hazel AMI's to continue to derisk the prospects and obtain initial production from the development efforts. The next scheduled well in the Hazel Project is scheduled to spud near the end of May, 2018. The first horizontal well in the Orogrande Project was spudded in November, 2017 and was in development as of December 31, 2017.

### Production, Price, and Production Cost History

During the year ended December 31, 2017, we produced and sold 10,391 barrels of oil net to our interest at an average sale price of \$52.37 per bbl. We produced and sold 9,259 MCF of gas net to our interest at an average sales price of \$2.84 per MCF. Our average production cost including lease operating expenses and direct production taxes was \$14.51 per BOE. Our depreciation, depletion, and amortization expense was \$7.39 per BOE.

During the year ended December 31, 2016, we produced and sold 8,488 barrels of oil net to our interest at an average sale price of \$34.15 per bbl. We produced and sold 36,513 MCF of gas net to our interest at an average sales price of

\$1.77 per MCF. Our average production cost including lease operating expenses and direct production taxes was \$22.54 per BOE. Our depreciation, depletion, and amortization expense was \$43.67 per BOE.

The changes in production were impacted by the divestiture of the Oklahoma Cimmaron and the Texas Marcelina properties early in 2016 and by the production from the Flying B #3 well in the Hazel Project beginning in late September, 2017.

Our 2017 production was from properties located in central Oklahoma and in west Texas. Reserves at the beginning of 2017 from central Oklahoma comprised more than 15% of total reserves. For 2017, approximately 2,000 BOE was produced in Oklahoma and 9,935 BOE produced in Texas, or 17% from Oklahoma and 83% from wells in west Texas.



## ITEM 2. PROPERTIES - continued

Quarterly Revenue and Production by State for 2017 and 2016 are detailed as follows:

| Property            | Quarter   | Oil Production<br>{BBLs} | Gas Production<br>{MCF} | Oil Revenue | Gas Revenue | Total<br>Revenue |
|---------------------|-----------|--------------------------|-------------------------|-------------|-------------|------------------|
| Oklahoma            | Q1 - 2017 | 101                      | 2,303                   | \$5,346     | \$7,604     | \$12,950         |
| Hazel (TX)          | Q1 - 2017 | 0                        | 0                       | -           | -           | -                |
| Total Q1-2017       |           | 101                      | 2,303                   | \$5,346     | \$7,604     | \$12,950         |
| Oklahoma            | Q2 - 2017 | 140                      | 2,332                   | 6,594       | 6,709       | 13,303           |
| Hazel (TX)          | Q2 - 2017 | 0                        | 0                       | -           | -           | -                |
| Total Q2-2017       |           | 140                      | 2,332                   | \$6,594     | \$6,709     | \$13,303         |
| Oklahoma            | Q3 - 2017 | 132                      | 2,041                   | 5,733       | 3,727       | 9,460            |
| Hazel (TX)          | Q3 - 2017 | 204                      | 0                       | 8,836       | -           | 8,836            |
| Total Q3-2017       |           | 336                      | 2,041                   | \$14,569    | \$3,727     | \$18,296         |
| Oklahoma            | Q4 - 2017 | 84                       | 2,583                   | 4,739       | 8,227       | 12,966           |
| Hazel (TX)          | Q4 - 2017 | 9,730                    | 0                       | 512,984     | -           | 512,984          |
| Total Q4-2017       |           | 9,814                    | 2,583                   | \$517,723   | \$8,227     | \$525,950        |
| Year Ended 12/31/17 |           | 10,391                   | 9,259                   | \$544,232   | \$26,267    | \$570,499        |
| Marcelina<br>(TX)   | Q1 - 2016 | 3,000                    | 0                       | \$92,546    | \$-         | \$92,546         |
| Oklahoma            | Q1 - 2016 | 2,026                    | 21,148                  | 54,289      | 38,624      | 92,913           |
| Kansas              | Q1 - 2016 | 312                      | 0                       | 8,854       | -           | 8,854            |
| Total Q1-2016       |           | 5,338                    | 21,148                  | \$155,689   | \$38,624    | \$194,313        |
| Marcelina<br>(TX)   | Q2 - 2016 | 917                      | 0                       | \$38,812    | \$-         | \$38,812         |
| Oklahoma            | Q2 - 2016 | 675                      | 9,689                   | 30,411      | 11,142      | 41,553           |
| Kansas              | Q2 - 2016 | 731                      | 0                       | 28,834      | -           | 28,834           |
| Total Q2-2016       |           | 2,323                    | 9,689                   | \$98,057    | \$11,142    | \$109,199        |
| Marcelina<br>(TX)   | Q3 - 2016 | 464                      | 0                       | \$20,190    | \$-         | \$20,190         |

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|                     |           |       |        |           |          |           |
|---------------------|-----------|-------|--------|-----------|----------|-----------|
| Oklahoma            | Q3 - 2016 | 180   | 2,830  | 7,925     | 6,170    | 14,095    |
| Kansas              | Q3 - 2016 | 0     | 0      | -         | -        | -         |
| Total Q3-2016       |           | 644   | 2,830  | \$28,115  | \$6,170  | \$34,285  |
| Marcelina<br>(TX)   | Q4 - 2016 | 0     | 0      | \$-       | \$-      | \$-       |
| Oklahoma            | Q4 - 2016 | 184   | 2,845  | 8,024     | 8,569    | 16,593    |
| Kansas              | Q4 - 2016 | 0     | 0      | -         | -        | -         |
| Total Q4-2016       |           | 184   | 2,845  | \$8,024   | \$8,569  | \$16,593  |
| Year Ended 12/31/16 |           | 8,488 | 36,513 | \$289,885 | \$64,505 | \$354,390 |



## ITEM 2. PROPERTIES - continued

## Drilling Activity and Productive Wells

## Central Oklahoma Projects

Having sold the Chisholm Trail and Cimarron wells and acreage in previous years, the only remaining producing wells in Oklahoma are the Judy and the Loki wells as of December 31, 2017. The Company retains ownership of the Viking, Rosedale, and Thunderbird AMI's at December 31, 2017

## Combined Well Status

The following table summarizes drilling activity and Well Status as of December 31, 2017:

|                               | Cumulative<br>Well Status |  | Wells Drilled |  | Cumulative<br>Well Status |  |
|-------------------------------|---------------------------|--|---------------|--|---------------------------|--|
| Drilling Activity/Well Status | at 12/31/2017             |  | 2017          |  | at 12/31/2016             |  |

|  | Gross | Net | Gross | Net | Gross | Net |
|--|-------|-----|-------|-----|-------|-----|
|--|-------|-----|-------|-----|-------|-----|

## Development Wells:

|                              |      |      |      |      |      |      |
|------------------------------|------|------|------|------|------|------|
| Productive -Texas (Hazel)    | 1.00 | 0.80 | 1.00 | 0.80 | -    | -    |
| Productive - Okla            | 2.00 | 0.40 | -    | -    | 2.00 | 0.40 |
| Test Wells (Dry) - Orogrande | 2.00 | 0.95 | -    | -    | 2.00 | 0.95 |
| Test Wells (Dry) - Hazel     | 2.00 | 1.60 | 2.00 | 1.60 | -    | -    |

## Exploration Wells:

|            |   |   |   |   |   |   |
|------------|---|---|---|---|---|---|
| Productive | - | - | - | - | - | - |
| Dry        | - | - | - | - | - | - |

## Total Drilled Wells:

|                   |      |      |      |      |      |      |
|-------------------|------|------|------|------|------|------|
| Productive -Texas | 1.00 | 0.80 | 1.00 | 0.80 | -    | -    |
| Productive - Okla | 2.00 | 0.40 | -    | -    | 2.00 | 0.40 |
| Test Wells (Dry)  | 4.00 | 2.55 | 2.00 | 1.60 | 2.00 | 0.95 |

Acquired Wells:

|                   |   |   |   |   |   |   |
|-------------------|---|---|---|---|---|---|
| Productive -Texas | - | - | - | - | - | - |
| Productive - Okla | - | - | - | - | - | - |

Total Wells:

|                   |      |      |      |      |      |      |
|-------------------|------|------|------|------|------|------|
| Productive -Texas | 1.00 | 0.80 | 1.00 | 0.80 | -    | -    |
| Productive - Okla | 2.00 | 0.40 | -    | -    | 2.00 | 0.40 |
| Test Wells (Dry)  | 4.00 | 2.55 | 2.00 | 1.60 | 2.00 | 0.95 |
| Total             | 7.00 | 3.75 | 3.00 | 2.40 | 4.00 | 1.35 |

Well Type:

|                          |      |      |      |      |      |      |
|--------------------------|------|------|------|------|------|------|
| Oil                      | -    | -    | -    | -    | -    | -    |
| Gas                      | -    | -    | -    | -    | -    | -    |
| Combination -Oil and Gas | 3.00 | 1.20 | 1.00 | 0.80 | 2.00 | 0.40 |
| Test Wells (Dry)         | 4.00 | 2.55 | 2.00 | 1.60 | 2.00 | 0.95 |
| Total                    | 7.00 | 3.75 | 3.00 | 2.40 | 4.00 | 1.35 |



## ITEM 2. PROPERTIES - continued

Our acreage positions at December 31, 2017 are summarized as follows:

|                                  | Total Acres |        | Developed Acres |     | Undeveloped Acres |        |
|----------------------------------|-------------|--------|-----------------|-----|-------------------|--------|
|                                  | Gross       | Net    | Gross           | Net | Gross             | Net    |
| Leasehold Interests - 12/31/2017 |             |        |                 |     |                   |        |
| Texas -                          |             |        |                 |     |                   |        |
| Orogrande                        | 133,000     | 90,108 | -               | -   | 133,000           | 90,108 |
| Hazel Project                    | 12,000      | 9,600  | -               | -   | 12,000            | 9,600  |
| Oklahoma -                       |             |        |                 |     |                   |        |
| Viking                           | 640         | 192    | 640             | 192 | -                 | -      |
| Prairie Grove                    | 640         | 64     | 640             | 64  | -                 | -      |
| Total                            | 146,280     | 99,964 | 1,280           | 256 | 145,000           | 99,708 |

## Current Projects

As of December 31, 2017 the Company had interests in four oil and gas projects:, the Orogrande Project in Hudspeth County, Texas, and the Hazel Project in Sterling, Tom Green, and Irion Counties, Texas, the Winkler Project in Winkler County, Texas, and the Hunton wells in partnership with Husky Ventures in Central Oklahoma ..

## Orogrande Project, West Texas

On August 7, 2014, we entered into a Purchase Agreement with Hudspeth Oil Corporation (“Hudspeth”), McCabe Petroleum Corporation (“MPC”), and Greg McCabe. Mr. McCabe was the sole owner of both Hudspeth and MPC. Under the terms and conditions of the Purchase Agreement, at closing, we purchased 100% of the capital stock of Hudspeth which holds certain oil and gas assets, including a 100% working interest in 172,000 mostly contiguous acres in the Orogrande Basin in West Texas. As of December 31, 2017, leases covering 133,000 acres remain in effect. This acreage is in the primary term under five-year leases that carry additional five-year extension provisions. As consideration, at closing we issued 868,750 shares of our common stock to Mr. McCabe and paid a total of \$100,000 in geologic origination fees to third parties. Additionally, Mr. McCabe has, at his option, a 10% working interest back-in after payout and a reversionary interest if drilling obligations are not met, all under the terms and conditions of a participation and development agreement. All drilling obligations through December 31, 2017 have been met.

On September 23, 2015, our subsidiary, Hudspeth Oil Corporation (“HOC”), entered into a Farmout Agreement by and between HOC, Pandora Energy, LP (“Pandora”), Founders Oil & Gas, LLC (“Founders”), McCabe Petroleum Corporation and Greg McCabe (McCabe Petroleum Corporation and Greg McCabe are parties to the Farmout Agreement for limited purposes) for the entire Orogrande Project in Hudspeth County, Texas. The Farmout Agreement provided for Founders to earn from HOC and Pandora (collectively, the “Farmor”) an undivided 50% of the leasehold interest in the Orogrande Project by Founder’s spending a minimum of \$45 million on actual drilling operations on the Orogrande Project in the following two years.

Under a joint operating agreement (on A.A.P.L. Form 610 – 1989 Model Form Operating Agreement with COPAS 2005 Accounting Procedures) (“JOA”) also entered into on September 23, 2015, Founders is designated as operator of the leases.

On March 22, 2017, the Company, along with Founders, their operating partner, signed a Drilling and Development Unit (DDU) Agreement with University Lands on its Orogrande Basin Project. The agreement has an effective date of January 1, 2017 and required a payment from both Torchlight and Founders of \$335,323 as part of the extension fee. Torchlight's portion of the fee was paid by Founders in April 2017 and will be deducted from the required spud fee payable to Torchlight at commencement of the next well drilled.

The DDU agreement allows for all 192 existing leases covering the 133,000 net acres leased from University Lands to be combined into one lease for development purposes. The time to drill on the unit is extended through April of 2023 on the first extension. The agreement also grants exclusive right to continue through April of 2028 if compliance with the agreement is met and extension fee associated with the additional time paid. The Company's drilling obligations begin with one well in the first year, and increase to five wells per year by year 2023. The drilling obligation set is a minimum requirement and may be exceeded if acceleration is desired. The DDU agreement replaces all prior agreements and will govern future drilling obligations on the lease.



ITEM 2. PROPERTIES - continued

The Orogrande Rich A-11 test well that was drilled by Torchlight in second quarter, 2015 was evaluated and numerous scientific tests were performed to provide key data for the field development thesis. Future utility of this well may be conversion to a salt water disposal well in the course of further development of the Orogrande acreage.

The second test well, the University Founders B-19 #1, was spudded on April 24, 2016 and drilled in second quarter, 2016. The well successfully pumped down completion fluid in the third quarter of 2016 and indications of hydrocarbons were seen at the surface on this second Orogrande Project test well. Future utility of this well may be conversion to a salt water disposal well in the course of further development of the Orogrande acreage.

During the fourth quarter, 2017, the Company took back operational control from Founders Oil and Gas on the Orogrande Basin Project. Torchlight was joined by Wolfbone Investments, LLC, ("Wolfbone"), a company owned by Greg McCabe, Torchlight's Chairman. The two entities have entered into an Assignment of Farmout Agreement with Founders and will share the remaining commitments under the prior agreement with Founders. All original provisions of Torchlight's carried interest will remain in place including reimbursement to the Company on each wellbore. Founders will remain a 9.5% Working Interest owner in the project under the agreement for the \$9.5 million it has spent to date and be carried until the remaining \$40.5 million is spent by Wolfbone and Torchlight, with each contributing 50% of that capital spend, under the existing agreement. Torchlight's interest in the Project thereby increased by 20.25% Working Interest to a total of 67.75% and Wolfbone now owns 20.25%.

Founders will operate a newly drilled well called the University Founders #A25 with supervision from Torchlight and its Partners. The University Founders #A25 was spudded on the 27th of November and satisfies the obligation under the University Lands D&D Agreement. Once the #A25 is completed Torchlight will assume full operational control including managing drilling plans and timing for all future wells drilled in the Project.

Hazel Project in the Midland Basin in West Texas

Effective April 1, 2016, Torchlight Energy Inc. acquired from McCabe Petroleum Corporation, a 66.66% working interest in approximately 12,000 acres in the Midland Basin in exchange for 1,500,000 warrants to purchase our common stock with an exercise price of \$1.00 for five years and a back-in after payout of a 25% working interest to the seller.

Initial development of the first well on the property, the Flying B Ranch #1, began July 10, 2016 and development continued through September 30, 2016. This well is classified as a test well in the development pursuit of the Hazel Project. It is anticipated that this wellbore will be utilized as a salt water disposal well in support of future development.

In October, 2016, the holders of the Company's Series C Preferred shares (which were issued in July, 2016) elected to convert into a 33.33% Working Interest in the Company's Hazel Project, reducing Torchlight's ownership from 66.66% to a 33.33% Working Interest.

On December 27, 2016, drilling activities commenced on the second Hazel Project well, the Flying B Ranch #2. The well is a vertical test similar to the Company's first Hazel Project well, the Flying B Ranch #1. Recompletion in an alternative geological formation for this well was performed during the three months ended September 30, 2017 however the results were uneconomic for continuing production. It is anticipated that this wellbore will be utilized as a salt water disposal well in support of future development.

The Company commenced planning to drill a horizontal well in the Project in June, 2017 in compliance with the continuous drilling obligation. The well, the Flying B Ranch #3, was spudded on June 10, 2017. The well was completed and began production in late September, 2017.

#### Acquisition of Additional Interests in Hazel Project

On January 30, 2017, we and our wholly-owned subsidiary, Torchlight Acquisition Corporation, a Texas corporation (“TAC”), entered into and closed an Agreement and Plan of Reorganization and Plan of Merger with Line Drive Energy, LLC, a Texas limited liability company (“Line Drive”), under which agreements TAC merged with and into Line Drive and the separate existence of TAC ceased, with Line Drive being the surviving organization and becoming our wholly-owned subsidiary. Line Drive, which was wholly-owned by Gregory McCabe, our Chairman, owned certain assets and securities, including approximately 40.66% of 12,000 gross acres in the Hazel Project and 521,739 warrants to purchase our common stock (which warrants had been assigned by Mr. McCabe to Line Drive). Under the merger transaction, our shares of common stock of TAC converted into a membership interest of Line Drive, the membership interest in Line Drive held by Mr. McCabe immediately prior to the transaction ceased to exist, and we issued Mr. McCabe 3,301,739 restricted shares of common stock as consideration therefor. Immediately after closing, the 521,739 warrants held by Line Drive were cancelled, which warrants had an exercise price of \$1.40 per share and an expiration date of June 9, 2020. A Certificate of Merger for the merger transaction was filed with the Secretary of State of Texas on January 31, 2017. Subsequent to the closing the name of Line Drive Energy, LLC was changed to Torchlight Hazel, LLC.



## ITEM 2. PROPERTIES - continued

Also on January 30, 2017, our wholly-owned subsidiary, Torchlight Energy, Inc., a Nevada corporation (“TEI”), entered into and closed a Purchase and Sale Agreement with Wolfbone Investments, LLC, a Texas limited liability company (“Wolfbone”) which is wholly-owned by Gregory McCabe, our Chairman. Under the agreement, TEI acquired certain of Wolfbone’s Hazel Project assets, including its interest in the Flying B Ranch #1 well and the 40 acre unit surrounding the well, for consideration of \$415,000, and additionally, Wolfbone caused to be cancelled a total of 2,780,000 warrants to purchase our common stock, including 1,500,000 warrants held by McCabe Petroleum Corporation, an entity owned by Mr. McCabe, and 1,280,000 warrants held by Green Hill Minerals, an entity owned by Mr. McCabe’s son, which warrant cancellations were effected through certain Warrant Cancellation Agreements. The 1,500,000 warrants held by McCabe Petroleum Corporation had an exercise price of \$1.00 per share and an expiration date of April 4, 2021. The warrants held by Green Hill Minerals included 100,000 warrants with an exercise price of \$1.73 and an expiration date of September 30, 2018 and 1,180,000 warrants with an exercise price of \$0.70 and an expiration date of February 15, 2020.

Since Mr. McCabe held the controlling interest in both Line Drive and Wolfbone Investments, LLC, the transactions were combined for accounting purposes. The working interest in the Hazel Project was the only asset held by Line Drive. The warrant cancellation was treated in the aggregate as an exercise of the warrants with the transfer of the working interests as the consideration. The Company recorded the transactions as an increase in its investment in the Hazel project working interests of \$3,644,431 which is equal to the exercise price of the warrants plus the cash paid to Wolfbone.

Upon the closing of the transactions, the Company’s working interest in the Hazel project increased by 40.66% to a total ownership of 74%.

Effective June 1, 2017, the Company acquired an additional 6% working interest from unrelated working interest owners in exchange for 268,656 shares of common stock valued at \$373,430, increasing its working interest in the Hazel project to 80%.

### Winkler Project, Winkler County, Texas

On December 1, 2017, the Agreement and Plan of Reorganization that we and our newly formed wholly-owned subsidiary, Torchlight Wolfbone Properties, Inc., a Texas corporation (“TWP”), entered into with McCabe Petroleum Corporation, a Texas corporation (“MPC”), and Warwink Properties, LLC, a Texas limited liability company (“Warwink Properties”) closed. Under the agreement, which was entered into on November 14, 2017, TWP merged with and into Warwink Properties and the separate existence of TWP ceased, with Warwink Properties becoming the surviving organization and our wholly-owned subsidiary. Warwink Properties was wholly owned by MPC which is wholly owned by Gregory McCabe, our Chairman. Warwink Properties owns certain assets, including a 10.71875% working interest in 640 acres in Winkler County, Texas. At closing of the merger transaction, our shares of common stock of TWP converted into a membership interest of Warwink Properties, the membership interest in Warwink Properties held by MPC ceased to exist, and we issued MPC 2,500,000 restricted shares of common stock as consideration. Also on December 1, 2017, MPC closed its transaction with MECO IV, LLC (“MECO”) for the purchase and sale of certain assets as contemplated by the Purchase and Sale Agreement dated November 9, 2017 (the “MECO PSA”), to which we are not a party. Under the MECO PSA, Warwink Properties received a carry from MECO (through the tanks) of up to \$1,475,000 in the next well drilled on the Winkler County leases. A Certificate of Merger for the merger transaction was filed with the Secretary of State of Texas on December 5, 2017.

Also on December 1, 2017, the transactions contemplated by the Purchase Agreement that our wholly-owned subsidiary, Torchlight Energy, Inc., a Nevada corporation (“TEI”), entered into with MPC closed. Under the Purchase

Agreement, which was entered into on November 14, 2017, TEI acquired beneficial ownership of certain of MPC's assets, including acreage and wellbores located in Ward County, Texas (the "Ward County Assets"). As consideration under the Purchase Agreement, at closing TEI issued to MPC an unsecured promissory note in the principal amount of \$3,250,000, payable in monthly installments of interest only beginning on January 1, 2018, at the rate of 5% per annum, with the entire principal amount together with all accrued interest due and payable on December 31, 2020. In connection with TEI's acquisition of beneficial ownership in the Ward County Assets, MPC sold those same assets, on behalf of TEI, to MECO at closing of the MECO PSA, and accordingly, TEI received \$3,250,000 in cash for its beneficial interest in the Ward County Assets. Additionally, at closing of the MECO PSA, MPC paid TEI a performance fee of \$2,781,500 in cash as compensation for TEI's marketing and selling the Winkler County assets of MPC and the Ward County Assets as a package to MECO.

#### Hunton Play, Central Oklahoma

As of December 31, 2017, we were producing from one well in the Viking AMI, and one well in Prairie Grove.

#### Central Oklahoma Projects

The Company retains any leases remaining effective in the three AMI's (Viking, Rosedale, and Thunderbird), the Loki well in the Viking AMI, and the Judy well in the Prairie Grove AMI as of December 31, 2017 pending information which will come from and results of, the Husky legal matter. The Judy and the Loki wells are producing at December 31, 2017. Reserve value at December 31, 2017 is only from the Judy well.



### ITEM 3. LEGAL PROCEEDINGS

Torchlight Energy Resources, Inc. and its subsidiary Torchlight Energy, Inc. has pending in the 429th judicial district court in Collin County, Texas a lawsuit against Husky Ventures, Inc., Charles V. Long, Silverstar of Nevada, Inc., Gastar Exploration Inc., J. Russell Porter, Michael A. Gerlich, and Jerry R. Schuyler that was originally filed in May 2016 (previous defendants April Glidewell, Maximus Exploration, LLC, Atwood Acquisitions, LLC and John M. Selser, Sr have been non-suited without prejudice to re-filing the claims). In the lawsuit, we allege, among other things, that the defendants acted improperly in connection with multiple transactions, and that the defendants misrepresented and omitted material information to us with respect to these transactions. The lawsuit seeks damages arising from 15 different causes of action, including without limitation, violations of the Texas Securities Act, fraud, negligent misrepresentation, breach of fiduciary duty, breach of contract, unjust enrichment and tortious interference.

On April 13, 2017, Husky Ventures, Inc. filed in the above lawsuit a counterclaim against Torchlight Energy Resources, Inc. and its subsidiary Torchlight Energy, Inc., and a third-party petition against John Brda, the Chief Executive Officer of Torchlight Energy Resources, Inc., and Willard McAndrew III, a former officer of Torchlight Energy Resources, Inc. (“Husky Counterclaim”). The Husky Counterclaim asserts breach of contract against Torchlight Energy Resources, Inc. and its subsidiary Torchlight Energy, Inc. and asserts a claim for tortious interference with Husky’s contractual relationship with Torchlight and a claim for conspiracy to tortiously interfere with unspecified Husky business and contractual relationships against Torchlight Energy Resources, Inc. and its subsidiary Torchlight Energy, Inc., John Brda and Willard McAndrew III. We believe the Husky Counterclaim is without merit and intend to vigorously defend against it.

On May 22, 2017, the Court granted Gastar Exploration, Inc., J. Russell Porter, Michael A. Gerlich, and Jerry R. Schuyler’s (“Gastar Defendants”) motion for summary judgment dismissing all of Torchlight’s claims against the Gastar Defendants with prejudice. The only claim remaining related to the Gastar Defendants is a counterclaim against Torchlight by Gastar Exploration, Inc. for Torchlight’s alleged breach of a release that Gastar Exploration, Inc. claims occurred because Torchlight filed this lawsuit against the Gastar Defendants. Torchlight alleges in its lawsuit that this release is unenforceable against all the Defendants including but not limited to Gastar Defendants. On January 12, 2018, the Court heard but has not yet ruled on cross-motions for summary judgment by Gastar and Torchlight to resolve Gastar’s remaining claims against Torchlight. The case is currently set for trial on May 30, 2018.

### ITEM 4. MINE SAFETY DISCLOSURES

Not Applicable.





## PART II

## ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY AND RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

Our common stock is quoted on The NASDAQ Stock Market LLC under the symbol, "TRCH." Trading in our common stock has historically been limited and occasionally sporadic and the quotations set forth below are not necessarily indicative of actual market conditions. The high and low sales prices for the common stock for each quarter of the fiscal years ended December 31, 2017 and 2016, according to NASDAQ, were as follows:

| Quarter Ended | High | Low |
|---------------|------|-----|
|---------------|------|-----|

|            |        |        |
|------------|--------|--------|
| 12/31/2017 | \$1.51 | \$1.06 |
| 9/30/2017  | \$1.81 | \$0.95 |
| 6/30/2017  | \$1.96 | \$1.16 |
| 3/31/2017  | \$1.88 | \$1.06 |

|            |        |        |
|------------|--------|--------|
| 12/31/2016 | \$1.48 | \$0.66 |
| 9/30/2016  | \$1.75 | \$0.55 |
| 6/30/2016  | \$0.94 | \$0.55 |
| 3/31/2016  | \$1.13 | \$0.42 |

## Record Holders

As of March 8, 2018, there were approximately 239 stockholders of record of our common stock, and we estimate that there were approximately 3,900 additional beneficial stockholders who hold their shares in "street name" through a brokerage firm or other institution. As of March 15, 2018, we have a total of 63,640,034 shares of common stock issued and outstanding.

The holders of the common stock are entitled to one vote for each share held of record on all matters submitted to a vote of stockholders. Holders of the common stock have no preemptive rights and no right to convert their common stock into any other securities. There are no redemption or sinking fund provisions applicable to the common stock.

## Dividends

We have not declared any cash dividends on our common stock since inception and do not anticipate paying any dividends in the foreseeable future. The payment of dividends is within the discretion of the Board of Directors and will depend on our earnings, capital requirements, financial condition, and other relevant factors. There are no restrictions that currently limit our ability to pay dividends on our common stock other than those generally imposed by applicable state law. The Company issued preferred stock in 2016 and 2015 on which dividends were paid. No preferred stock is outstanding as of December 31, 2017.

## Equity Compensation Plan Information

The following table sets forth all equity compensation plans as of December 31, 2017:

| Plan Category                                          | Number of securities to be issued upon exercise of outstanding options, warrants and rights | Weighted-average exercise price of outstanding options, warrants and rights | Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a)) |
|--------------------------------------------------------|---------------------------------------------------------------------------------------------|-----------------------------------------------------------------------------|---------------------------------------------------------------------------------------------------------------------------------------------|
| Equity compensation plans approved by security holders | 7,414,931                                                                                   | \$ 1.51                                                                     | 1,085,069                                                                                                                                   |



## ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY AND RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES - continued

### Sales of Unregistered Securities

Other than the sales below, all equity securities that we have sold during the period covered by this report that were not registered under the Securities Act have previously been included in a Quarterly Report on Form 10-Q or in a Current Report on Form 8-K.

In November 2017, we issued a total of 350,000 shares of common stock to a total of four consultants in connection with the acquisition of mineral interests.

During the three months ended December 31, 2017, we issued 278,099 shares of common stock in warrant exercises.

All of the above sales of securities described in this Item 2 were sold under the exemption from registration provided by Section 4(a)(2) of the Securities Act of 1933 and the rules and regulations promulgated thereunder. The issuances of securities did not involve a "public offering" based upon the following factors: (i) the issuances of securities were isolated private transactions; (ii) a limited number of securities were issued to a limited number of purchasers; (iii) there were no public solicitations; (iv) the investment intent of the purchasers; and (v) the restriction on transferability of the securities issued.

## ITEM 6. SELECTED FINANCIAL DATA

Under SEC rules and guidance, an issuer that no longer qualifies as a smaller reporting company at the determination date may continue to use the scaled disclosures permitted for a smaller reporting company through its annual report on Form 10-K and begin providing non-scaled larger company disclosure in the first Form 10-Q of the next fiscal year. Although we are filing as an accelerated filer, we are allowed to continue reporting as a smaller reporting company in this Form 10-K. As such, we are not required to provide information under this Item.

## ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Information set forth and discussed in this Management's Discussion and Analysis and Results of Operations is derived from our historical financial statements and the related notes thereto which are included in this Form 10-K. The following information and discussion should be read in conjunction with such financial statements and notes. Additionally, this Management's Discussion and Analysis and Plan of Operations contain certain statements that are not strictly historical and are "forward-looking" statements within the meaning of the Private Securities Litigation Reform Act of 1995 and involve a high degree of risk and uncertainty. Actual results may differ materially from those projected in the forward-looking statements due to other risks and uncertainties that exist in our operations, development efforts, and business environment, and due to other risks and uncertainties relating to our ability to obtain additional capital in the future to fund our planned expansion, the demand for oil and natural gas, and other general economic factors.

All forward-looking statements included herein are based on information available to us as of the date hereof, and we assume no obligation to update any such forward-looking statements.

### Summary of Key Results

#### Overview

We are engaged in the acquisition, exploration, exploitation, and/or development of oil and natural gas properties in the United States.

During the year ended December 31, 2016 the Board of Directors initiated a review of Company operations in view of the divestiture of its Oklahoma properties, which included the previous sale of the Chisholm Trail and Cimarron properties. During 2016 development had continued on the Orogrande Project in West Texas and in April, 2016, the Company acquired the Hazel Project in the Midland Basin also in West Texas. These West Texas properties demonstrate significant potential and future production capabilities based upon the analysis of scientific data being gathered in the day by day development activity. Therefore, the Board has determined to focus its efforts and capital on these projects to maximize shareholder value for the long run.

During 2017 the Company increased its commitment to the Orogrande and Hazel Projects. Additional working interests were acquired and test wells were drilled on the properties which is detailed in the Properties section of this filing. Near the end of 2017 the Warwink Project, also in West Texas, was acquired.

The strategy in divesting of projects other than the Orogrande and the Hazel Projects was to refocus on the greatest potential future value for the Company while systematically eliminating debt as noncore assets are sold and operations are streamlined.

The following discussion of our financial condition and results of operations should be read in conjunction with our audited financial statements for the years ended December 31, 2017 and 2016 included herewith. This discussion should not be construed to imply that the results discussed herein will necessarily continue into the future, or that any conclusion reached herein will necessarily be indicative of actual operating results in the future. Such discussion represents only the best present assessment by our management.



## ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS - continued

## Historical Results for the Years Ended December 31, 2017 and 2016

For the year ended December 31, 2017, we had a net loss of \$919,910 compared to a net loss of \$7,684,346 for the year ended December 31, 2016.

## Revenues and Cost of Revenues

For the year ended December 31, 2017, we had production revenue of \$570,499 compared to \$354,390 of production revenue for the year ended December 31, 2016. Refer to the table of production and revenue for 2017 included below. Our cost of revenue, consisting of lease operating expenses and production taxes, was \$173,187, and \$328,438 for the years ended December 31, 2017 and 2016, respectively.

The change in revenue was impacted by the new production from the Flying B #3 well in the Hazel Project that began in late September, 2017.

Total income for 2017 includes \$2,781,500 of Consulting Fees received by the Company in connection with the Warwink acquisition in the fourth quarter. Reference Item 1: Current Projects included in this filing.

Production and Revenue are detailed as follows:

| Property      | Quarter   | Oil Production<br>{BBLs} | Gas Production<br>{MCF} | Oil Revenue | Gas Revenue | Total<br>Revenue |
|---------------|-----------|--------------------------|-------------------------|-------------|-------------|------------------|
| Oklahoma      | Q1 - 2017 | 101                      | 2,303                   | \$5,346     | \$7,604     | \$12,950         |
| Hazel (TX)    | Q1 - 2017 | 0                        | 0                       | -           | -           | -                |
| Total Q1-2017 |           | 101                      | 2,303                   | \$5,346     | \$7,604     | \$12,950         |
| Oklahoma      | Q2 - 2017 | 140                      | 2,332                   | 6,594       | 6,709       | 13,303           |
| Hazel (TX)    | Q2 - 2017 | 0                        | 0                       | -           | -           | -                |
| Total Q2-2017 |           | 140                      | 2,332                   | \$6,594     | \$6,709     | \$13,303         |
| Oklahoma      | Q3 - 2017 | 132                      | 2,041                   | 5,733       | 3,727       | 9,460            |
| Hazel (TX)    | Q3 - 2017 | 204                      | 0                       | 8,836       | -           | 8,836            |
| Total Q3-2017 |           | 336                      | 2,041                   | \$14,569    | \$3,727     | \$18,296         |
| Oklahoma      | Q4 - 2017 | 84                       | 2,583                   | 4,739       | 8,227       | 12,966           |
| Hazel (TX)    | Q4 - 2017 | 9,730                    | 0                       | 512,984     | -           | 512,984          |
| Total Q4-2017 |           | 9,814                    | 2,583                   | \$517,723   | \$8,227     | \$525,950        |

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|                     |        |       |           |          |           |
|---------------------|--------|-------|-----------|----------|-----------|
| Year Ended 12/31/17 | 10,391 | 9,259 | \$544,232 | \$26,267 | \$570,499 |
|---------------------|--------|-------|-----------|----------|-----------|

|                |           |       |        |           |          |           |
|----------------|-----------|-------|--------|-----------|----------|-----------|
| Marcelina (TX) | Q1 - 2016 | 3,000 | 0      | \$92,546  | \$-      | \$92,546  |
| Oklahoma       | Q1 - 2016 | 2,026 | 21,148 | 54,289    | 38,624   | 92,913    |
| Kansas         | Q1 - 2016 | 312   | 0      | 8,854     | -        | 8,854     |
| Total Q1-2016  |           | 5,338 | 21,148 | \$155,689 | \$38,624 | \$194,313 |

|                |           |       |       |          |          |           |
|----------------|-----------|-------|-------|----------|----------|-----------|
| Marcelina (TX) | Q2 - 2016 | 917   | 0     | \$38,812 | \$-      | \$38,812  |
| Oklahoma       | Q2 - 2016 | 675   | 9,689 | 30,411   | 11,142   | 41,553    |
| Kansas         | Q2 - 2016 | 731   | 0     | 28,834   | -        | 28,834    |
| Total Q2-2016  |           | 2,323 | 9,689 | \$98,057 | \$11,142 | \$109,199 |



## ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS - continued

|                |           |     |       |          |         |          |
|----------------|-----------|-----|-------|----------|---------|----------|
| Marcelina (TX) | Q3 - 2016 | 464 | 0     | \$20,190 | \$-     | \$20,190 |
| Oklahoma       | Q3 - 2016 | 180 | 2,830 | 7,925    | 6,170   | 14,095   |
| Kansas         | Q3 - 2016 | 0   | 0     | -        | -       | -        |
| Total Q3-2016  |           | 644 | 2,830 | \$28,115 | \$6,170 | \$34,285 |

|                |           |     |       |         |         |          |
|----------------|-----------|-----|-------|---------|---------|----------|
| Marcelina (TX) | Q4 - 2016 | 0   | 0     | \$-     | \$-     | \$-      |
| Oklahoma       | Q4 - 2016 | 184 | 2,845 | 8,024   | 8,569   | 16,593   |
| Kansas         | Q4 - 2016 | 0   | 0     | -       | -       | -        |
| Total Q4-2016  |           | 184 | 2,845 | \$8,024 | \$8,569 | \$16,593 |

|                     |       |        |           |          |           |
|---------------------|-------|--------|-----------|----------|-----------|
| Year Ended 12/31/16 | 8,488 | 36,513 | \$289,885 | \$64,505 | \$354,390 |
|---------------------|-------|--------|-----------|----------|-----------|

We recorded depreciation, depletion and amortization expense of \$100,156 for the year ended December 31, 2017 compared to \$636,426 for 2016. Impairment expense recognized was \$-0- in 2017 compared to \$70,080 for 2016. Although we had no recognized impairment expense in 2017, the Company has adjusted the separation of evaluated versus unevaluated costs within its full cost pool to recognize the value impairment related to the expiration of unevaluated leases in 2017 in the amount of \$2,300,626. The impact of this change will be to increase the basis for calculation of future period's depletion, depreciation and amortization to include \$2,300,626 of cost which will effectively recognize the impairment on the Statement of Income over future periods. The \$2,300,626 will also become an evaluated cost for purposes of future period's Ceiling Tests and which may further recognize the impairment expense recognized in future periods.

## General and Administrative Expenses

Our general and administrative expenses for the years ended December 31, 2017 and 2016 were \$3,652,970 and \$6,447,706, respectively, a decrease of \$2,794,736. Our general and administrative expenses consisted of consulting and compensation expense, substantially all of which was non-cash or deferred, accounting and administrative costs, professional consulting fees, and other general corporate expenses. The decrease in general and administrative expenses for the year ended December 31, 2017 compared to 2016 is detailed as follows:

|                                                               |               |
|---------------------------------------------------------------|---------------|
| Increase(decrease) in non cash stock and warrant compensation | \$(2,509,404) |
| Increase(decrease) in consulting expense                      | \$(85,916)    |
| Increase(decrease) in professional fees                       | \$(71,387)    |
| Increase(decrease) in investor relations                      | \$94,183      |
| Increase(decrease) in travel expense                          | \$(18,760)    |
| Increase(decrease) in salaries and compensation               | \$(367,234)   |
| Increase(decrease) in legal fees                              | \$42,713      |
| Increase(decrease) in insurance                               | \$(16,932)    |
| Increase(decrease) in general corporate expenses              | \$14,463      |
| Increase(decrease) in audit fees                              | \$123,538     |
| Total (Decrease) in General and Administrative Expenses       | \$(2,794,736) |

The decrease in noncash stock and warrant compensation arises from the decrease in vested employee stock options expense and a reduction in outside services compensated with stock and warrants. Employee options were initially issued with 50% immediate vesting of option valuation at June, 2015. The balance of the vesting was set at 25% in June, 2016 and 25% in June, 2017. The valuation was recorded over the periods up to the full vesting date using the straight line method.

The decrease in consulting expense parallels the reduction in outside services compensated with stock and warrants as noted above.

The reduction in salaries and compensation arises from a reduction in staff size due to the resignation of our inside Petroleum Engineer and the resignation of our COO in 2016.



ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS - continued

Liquidity and Capital Resources

For the year ended December 31, 2017, we had a net loss of \$919,910 compared to a net loss of \$7,684,346 for the year ended December 31, 2016. The reduction in Net Loss is principally due to the receipt of Consulting Fee income of \$2,781,500 during the fourth quarter and the reduction in General and Administrative expense in 2017.

At December 31, 2017, we had current assets of \$3,165,951 and total assets of \$28,767,308. As of December 31, 2017, we had current liabilities of \$2,279,448. Stockholders' equity was \$15,959,305 at December 31, 2017.

Cash from operating activities for the year ended December 31, 2017, was \$465,594 compared to \$(4,826,089) for the year ended December 31, 2016, an increase of \$5,291,683. Cash from operating activities during 2017 can be attributed principally to net loss from operations of \$919,910 adjusted for noncash stock based compensation of \$1,151,061.

Cash used in operating activities during 2016 can be attributed principally to net losses from operations of \$7,684,346 adjusted for noncash stock based compensation of \$2,956,044.

Cash used in investing activities for year ended December 31, 2017 was \$9,458,648 compared to \$167,871 for the year ended December 31, 2016. Cash used in investing activities consisted primarily of investment in oil and gas properties during the year ended December 31, 2017. In 2016 the investment in properties was combined with proceeds from sale of leases in 2016.

Cash from financing activities for the year ended December 31, 2017 was \$8,275,275 as compared to \$5,736,859 for the year ended December 31, 2016. Cash from financing activities in 2016 consisted primarily of proceeds from common and preferred stock issues and warrant exercises. 2017 activity consisted principally of debt financing transactions. We expect to continue to have cash provided by financing activities as we seek new rounds of financing and continue to develop our oil and gas investments. Reference Note 11 to the Financial Statements regarding additional funding closed subsequent to December 31, 2017.

Our current assets are insufficient to satisfy our cash needs over the next twelve months and as such we will require additional debt or equity financing to meet our plans and needs. We face obstacles in continuing to attract new financing due to our history and current record of net losses and past working capital deficits. Despite our efforts, we can provide no assurance that we will be able to obtain the financing required to meet our stated objectives or even to continue as a going concern.

We do not expect to pay cash dividends on our common stock in the foreseeable future.

Critical Accounting Policies and Estimates

Oil and gas properties – The Company uses the full cost method of accounting for exploration and development activities as defined by the Securities and Exchange Commission ("SEC"). Under this method of accounting, the costs of unsuccessful, as well as successful, exploration and development activities are capitalized as properties and equipment. This includes any internal costs that are directly related to property acquisition, exploration and development activities but does not include any costs related to production, general corporate overhead or similar activities. Gain or loss on the sale or other disposition of oil and gas properties is not recognized, unless the gain or loss would significantly alter the relationship between capitalized costs and proved reserves.

Oil and gas properties include costs that are excluded from costs being depleted or amortized. Oil and natural gas property costs excluded represent investments in unevaluated properties and include non-producing leasehold, geological, and geophysical costs associated with leasehold or drilling interests and exploration drilling costs. The Company allocates a portion of its acquisition costs to unevaluated properties based on relative value. Costs are transferred to the full cost pool as the properties are evaluated over the life of the reservoir. Unevaluated properties are reviewed for impairment at least quarterly and are determined through an evaluation considering, among other factors, seismic data, requirements to relinquish acreage, drilling results, remaining time in the commitment period, remaining capital plan, and political, economic, and market conditions.

Gains and losses on the sale of oil and gas properties are not generally reflected in income unless the gain or loss would significantly alter the relationship between capitalized costs and proved reserves. Sales of less than 100% of the Company's interest in the oil and gas property are treated as a reduction of the capital cost of the field, with no gain or loss recognized, as long as doing so does not significantly affect the unit-of-production depletion rate. Costs of retired equipment, net of salvage value, are usually charged to accumulated depreciation.

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS - continued

Depreciation, depletion, and amortization – The depreciable base for oil and natural gas properties includes the sum of all capitalized costs net of accumulated depreciation, depletion, and amortization (“DD&A”), estimated future development costs and asset retirement costs not included in oil and natural gas properties, less costs excluded from amortization. The depreciable base of oil and natural gas properties is amortized on a unit-of-production method.

Ceiling test – Future production volumes from oil and gas properties are a significant factor in determining the full cost ceiling limitation of capitalized costs. Under the full cost method of accounting, the Company is required to periodically perform a “ceiling test” that determines a limit on the book value of oil and gas properties. If the net capitalized cost of proved oil and gas properties, net of related deferred income taxes, plus the cost of unproved oil and gas properties, exceeds the present value of estimated future net cash flows discounted at 10 percent, net of related tax affects, plus the cost of unproved oil and gas properties, the excess is charged to expense and reflected as additional accumulated DD&A. The ceiling test calculation uses a commodity price assumption which is based on the unweighted arithmetic average of the price on the first day of each month for each month within the prior 12 month period and excludes future cash outflows related to estimated abandonment costs.

The determination of oil and gas reserves is a subjective process, and the accuracy of any reserve estimate depends on the quality of available data and the application of engineering and geological interpretation and judgment. Estimates of economically recoverable reserves and future net cash flows depend on a number of variable factors and assumptions that are difficult to predict and may vary considerably from actual results. In particular, reserve estimates for wells with limited or no production history are less reliable than those based on actual production. Subsequent re-evaluation of reserves and cost estimates related to future development of proved oil and gas reserves could result in significant revisions to proved reserves. Other issues, such as changes in regulatory requirements, technological advances, and other factors which are difficult to predict could also affect estimates of proved reserves in the future.

Asset retirement obligations –The fair value of a liability for an asset’s retirement obligation (“ARO”) is recognized in the period in which it is incurred if a reasonable estimate of fair value can be made, with the corresponding charge capitalized as part of the carrying amount of the related long-lived asset. The liability is accreted to its then-present value each subsequent period, and the capitalized cost is depleted over the useful life of the related asset. Abandonment costs incurred are recorded as a reduction of the ARO liability.

Inherent in the fair value calculation of an ARO are numerous assumptions and judgments including the ultimate settlement amounts, inflation factors, credit adjusted discount rates, timing of settlement, and changes in the legal, regulatory, environmental, and political environments. To the extent future revisions to these assumptions impact the fair value of the existing ARO liability, a corresponding adjustment is made to the oil and gas property balance. Settlements greater than or less than amounts accrued as ARO are recorded as a gain or loss upon settlement.

Share-based compensation – Compensation cost for equity awards is based on the fair value of the equity instrument on the date of grant and is recognized over the period during which an employee is required to provide service in exchange for the award. Compensation cost for liability awards is based on the fair value of the vested award at the end of each period.

The Company accounts for stock option awards using the calculated value method. The expected term was derived using the simplified method provided in Securities and Exchange Commission release Staff Accounting Bulletin No. 110, which averages an awards weighted average vesting period and contractual term for “plain vanilla” share options.

The Company accounts for any forfeitures of options when they occur. Previously recognized compensation cost for an award is reversed in the period that the award is forfeited.

The Company also issues equity awards to non-employees. The fair value of these option awards is estimated when the award recipient completes the contracted professional services. The Company recognizes expense for the estimated total value of the awards during the period from their issuance until performance completion, at which time the estimated expense is adjusted to the final value of the award as measured at performance completion.

The Company values warrant and option awards using the Black-Scholes option pricing model.

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS - continued

Commitments and Contingencies

Leases

The Company has a noncancelable lease for its office premises that expires on November 30, 2019 and which requires the payment of base lease amounts and executory costs such as taxes, maintenance and insurance. Rental expense for lease was \$84,197 and \$81,595 for the year ended December 31, 2017 and 2016, respectively.

Approximate future minimum rental commitments under the office premises lease are:

Year Ending December 31, Rent

|                    |           |
|--------------------|-----------|
| 2018               | \$96,660  |
| To 2019 Expiration | 88,605    |
| Total              | \$185,265 |

As of December 31, 2017, the Company had interests in four oil and gas projects: the Orogrande Project in Hudspeth County, Texas, the Hazel Project in Sterling, Tom Green, and Irion Counties, Texas, the Warwink Project in Winkler County, Texas, and Hunton wells in Central Oklahoma, .

See the description under "Current Projects" above under "Item 1. Business" for more information and disclosure regarding commitments and contingencies relating to these projects which description is incorporated herein by reference.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Under SEC rules and guidance, an issuer that no longer qualifies as a smaller reporting company at the determination date may continue to use the scaled disclosures permitted for a smaller reporting company through its annual report on Form 10-K and begin providing non-scaled larger company disclosure in the first Form 10-Q of the next fiscal year. Although we are filing as an accelerated filer, we are allowed to continue reporting as a smaller reporting company in this Form 10-K. As such, we are not required to provide information under this Item.





## ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA.

### REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and  
Stockholders of Torchlight Energy Resources, Inc.  
Plano, Texas

#### Opinions on the Financial Statements and Internal Control over Financial Reporting

We have audited the accompanying consolidated balance sheets of Torchlight Energy Resources, Inc. (the Company) as of December 31, 2017 and 2016, and the related consolidated statements of operations, stockholders' equity, and cash flows for each of the years in the two-year period ended December 31, 2017, and the related notes (collectively referred to as the financial statements). We also have audited the Company's internal control over financial reporting as of December 31, 2017, based on criteria established in Internal Control—Integrated Framework (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Company as of December 31, 2017 and 2016, and the results of its operations and its cash flows for each of the years in the two-year period ended December 31, 2017, in conformity with accounting principles generally accepted in the United States of America. Also, in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2017, based on criteria established in Internal Control—Integrated Framework (2013) issued by COSO.

The accompanying consolidated financial statements have been prepared assuming that the Company will continue as a going concern. As discussed in Note 2 to the consolidated financial statements, the Company has incurred recurring losses from its operations and has a net capital deficiency which raises substantial doubt about its ability to continue as a going concern. Management's plans in regard to these matters are also described in Note 2. The consolidated financial statements do not include any adjustments that might result from the outcome of this uncertainty.

#### Basis for Opinion

The Company's management is responsible for these financial statements, for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting included in the accompanying Item 9A, "Management's Annual Report on Internal Control Over Financial Reporting." Our responsibility is to express an opinion on the Company's financial statements and an opinion on the Company's internal control over financial reporting based on our audits. We are a public accounting firm registered with the Public Company Accounting Oversight Board (United States) (PCAOB) and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether due to error or fraud, and whether effective internal control over financial reporting was maintained in all material respects.

Our audits of the financial statements included performing procedures to assess the risks of material misstatement of the financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the financial

statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the financial statements. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audits also included performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.



## Definition and Limitations of Internal Control over Financial Reporting

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

/s/ Briggs & Veselka Co.

We have served as the  
Company's auditor since  
2016.

Houston, Texas

March 16, 2018



## TORCHLIGHT ENERGY RESOURCES, INC.

## CONSOLIDATED BALANCE SHEETS

|                                                                                                   | December 31,<br>2017 | December 31,<br>2016 |
|---------------------------------------------------------------------------------------------------|----------------------|----------------------|
| <b>ASSETS</b>                                                                                     |                      |                      |
| Current assets:                                                                                   |                      |                      |
| Cash                                                                                              | \$1,051,720          | \$1,769,499          |
| Accounts receivable                                                                               | 596,141              | 603,446              |
| Production revenue receivable                                                                     | 142,932              | 7,325                |
| Prepayments - development costs                                                                   | 1,335,652            | 583,347              |
| Prepaid expenses                                                                                  | 39,506               | 26,829               |
| Total current assets                                                                              | 3,165,951            | 2,990,446            |
| Oil and gas properties, net                                                                       | 25,579,279           | 9,392,288            |
| Office equipment, net                                                                             | 15,716               | 29,848               |
| Other assets                                                                                      | 6,362                | 18,362               |
| <b>TOTAL ASSETS</b>                                                                               | <b>\$28,767,308</b>  | <b>\$12,430,944</b>  |
| <b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>                                                       |                      |                      |
| Current liabilities:                                                                              |                      |                      |
| Accounts payable                                                                                  | \$762,502            | \$422,684            |
| Funds received pending settlement                                                                 | 520,400              | 520,400              |
| Accrued payroll                                                                                   | 695,176              | 565,176              |
| Related party payables                                                                            | 45,000               | 237,044              |
| Convertible promissory notes (Series B) net of discount of                                        |                      |                      |
| \$94,083 at December 31, 2016                                                                     | -                    | 3,475,417            |
| Due to working interest owners                                                                    | 54,320               | 54,320               |
| Accrued interest payable                                                                          | 202,050              | 6,049                |
| Total current liabilities                                                                         | 2,279,448            | 5,281,090            |
| Unsecured promissory notes, net of discount and financing costs of \$795,017 at December 31, 2017 | 7,269,281            | -                    |
| Note payable                                                                                      | 3,250,000            | -                    |

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|                                                                           |              |              |
|---------------------------------------------------------------------------|--------------|--------------|
| Asset retirement obligation                                               | 9,274        | 7,051        |
| Total liabilities                                                         | 12,808,003   | 5,288,141    |
| Commitments and contingencies                                             |              |              |
| Stockholders' equity:                                                     |              |              |
| Preferred stock, par value \$.001, 10,000,000 shares authorized;          |              |              |
| -0- issued and outstanding at December 31, 2017 and 2016                  | -            | -            |
| Common stock, par value \$0.001 per share; 150,000,000 shares authorized; | 63,344       | 55,100       |
| 63,340,034 issued and outstanding at December 31, 2017                    |              |              |
| 55,096,503 issued and outstanding at December 31, 2016                    |              |              |
| Additional paid-in capital                                                | 99,403,654   | 89,675,488   |
| Accumulated deficit                                                       | (83,507,693) | (82,587,785) |
| Total stockholders' equity                                                | 15,959,305   | 7,142,803    |
| TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY                                | \$28,767,308 | \$12,430,944 |

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



TORCHLIGHT ENERGY RESOURCES, INC.

CONSOLIDATED STATEMENTS OF OPERATIONS

|                                          | YEAR              | YEAR              |
|------------------------------------------|-------------------|-------------------|
|                                          | ENDED             | ENDED             |
|                                          | December 31, 2017 | December 31, 2016 |
| Revenue                                  |                   |                   |
| Oil and gas sales                        | \$570,499         | \$354,390         |
| Cost of revenue                          | (173,187)         | (328,438)         |
| Gross profit                             | 397,312           | 25,952            |
| Operating expenses:                      |                   |                   |
| General and administrative expense       | (3,652,970)       | (6,447,706)       |
| Depreciation, depletion and amortization | (100,156)         | (636,426)         |
| Impairment expense                       | -                 | (70,080)          |
| Loss on sale of properties               | -                 | (283,285)         |
| Total operating expenses                 | (3,753,126)       | (7,437,497)       |
| Other income (expense)                   |                   |                   |
| Consulting income                        | 2,781,500         | -                 |
| Interest income                          | 454               | 36                |
| Interest and accretion expense           | (346,050)         | (272,837)         |
| Total other income (expense)             | 2,435,904         | (272,801)         |

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|                            |             |               |
|----------------------------|-------------|---------------|
| Loss before income taxes   | (919,910)   | (7,684,346)   |
| Provision for income taxes | -           | -             |
| Net loss                   | \$(919,910) | \$(7,684,346) |

|                        |          |          |
|------------------------|----------|----------|
| Loss per common share: |          |          |
| Basic and Diluted      | \$(0.02) | \$(0.19) |

Weighted average number of common shares outstanding:

|                   |            |            |
|-------------------|------------|------------|
| Basic and Diluted | 59,623,105 | 43,122,514 |
|-------------------|------------|------------|

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



TORCHLIGHT ENERGY RESOURCES, INC.  
CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY

|                                                        | Common     | Common Pref. | Pref.     | Additional |              |                |             |
|--------------------------------------------------------|------------|--------------|-----------|------------|--------------|----------------|-------------|
|                                                        | stock      | stock        | stock     | Stock      | paid-in      | Accumulated    |             |
|                                                        | shares     | amount       | shares    | Amt.       | capital      | deficit        | Total       |
| Balance, December 31, 2015                             | 33,166,344 | \$33,168     | 134,000   | \$134      | \$78,252,411 | \$(74,903,439) | \$3,382,274 |
| Issuance of common stock for cash                      | 3,750,000  | 3,750        | -         | -          | 2,996,250    | -              | 3,000,000   |
| Issuance of preferred stock for cash                   | -          | -            | -         | 10         | 999,990      | -              | 1,000,000   |
| Issuance of common stock for services                  | 768,832    | 769          | -         | -          | 669,305      | -              | 670,074     |
| Issuance of common stock - mineral interests           | 2,824,881  | 2,825        | -         | -          | 1,972,221    | -              | 1,975,046   |
| Issuance of common stock in warrant exercise           | 3,888,745  | 3,891        | -         | -          | 2,539,855    | -              | 2,543,746   |
| Issuance of common stock for note interest             | -          | -            | -         | -          | -            | -              | -           |
| Issuance of common stock for preferred dividends       | 440,262    | 440          | -         | -          | (440)        | -              | -           |
| Preferred dividends paid in cash                       | -          | -            | -         | -          | (320,724)    | -              | (320,724)   |
| Warrants issued with lease interests                   | -          | -            | -         | -          | 1,290,761    | -              | 1,290,761   |
| Warrants issued for services                           | -          | -            | -         | -          | 2,205,231    | -              | 2,205,231   |
| Lease interest issued in conversion of preferred stock | -          | -            | -         | (10)       | (999,990)    | -              | (1,000,000) |
| Common stock issued in conversion of preferred stock   | 10,257,439 | 10,257       | (134,000) | (134)      | (10,132)     | -              | (9)         |
| Warrants issued in connection with promissory note     | -          | -            | -         | -          | 80,750       | -              | 80,750      |
| Net loss                                               | -          | -            | -         | -          | -            | (7,684,346)    | (7,684,346) |
| Balance, December 31, 2016                             | 55,096,503 | \$55,100     | -         | -          | \$89,675,488 | \$(82,587,785) | \$7,142,803 |
| Issuance of common stock for services                  | 507,897    | 508          | -         | -          | 579,246      | -              | 579,754     |

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|                                                        |            |          |   |   |              |                |              |
|--------------------------------------------------------|------------|----------|---|---|--------------|----------------|--------------|
| Issuance of common stock for lease interests           | 6,420,395  | 6,421    | - | - | 6,805,941    |                | 6,812,362    |
| Issuance of common stock in warrant exercise           | 307,349    | 307      | - | - | 242,993      |                | 243,300      |
| Issuance of common stock-conversion of promissory note | 1,007,890  | 1,008    | - | - | 1,006,882    |                | 1,007,890    |
| Warrants issued for services                           | -          | -        | - | - | 161,560      |                | 161,560      |
| Stock options issued for services                      | -          | -        | - | - | 931,544      |                | 931,544      |
| Net loss                                               | -          | -        | - | - | -            | (919,910)      | (919,910)    |
| Balance, December 31, 2017                             | 63,340,034 | \$63,344 | - | - | \$99,403,654 | \$(83,507,693) | \$15,959,305 |

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



## TORCHLIGHT ENERGY RESOURCES, INC.

## CONSOLIDATED STATEMENTS OF CASH FLOW

|                                                                | YEAR              | YEAR              |
|----------------------------------------------------------------|-------------------|-------------------|
|                                                                | ENDED             | ENDED             |
|                                                                | December 31, 2017 | December 31, 2016 |
| Cash Flows From Operating Activities                           |                   |                   |
| Net loss                                                       | \$(919,910)       | \$(7,684,346)     |
| Adjustments to reconcile net loss to net cash from operations: |                   |                   |
| Stock based compensation                                       | 1,151,061         | 2,956,044         |
| Accretion of note discounts                                    | 291,386           | 186,532           |
| Loss on sale of assets                                         | -                 | 283,285           |
| Impairment expense                                             | -                 | 70,080            |
| Depreciation, depletion and amortization                       | 100,156           | 636,426           |
| Change in:                                                     |                   |                   |
| Accounts receivable                                            | 7,305             | 138,207           |
| Note receivable                                                | -                 | 613               |
| Production revenue receivable                                  | (135,607)         | 191,992           |
| Prepayment of development costs                                | (752,305)         | (1,583,347)       |
| Prepaid expenses                                               | (12,676)          | 11,946            |
| Other assets                                                   | 12,000            | 59,240            |
| Accounts payable and accrued liabilities                       | 519,818           | (396,456)         |
| Due to working interest owners                                 | -                 | (49,044)          |
| Funds received pending settlement                              | -                 | 520,400           |
| Interest payable                                               | 204,364           | (167,661)         |
| Net cash provided by (used) in operating activities            | 465,592           | (4,826,089)       |
| Cash Flows From Investing Activities                           |                   |                   |
| Investment in oil and gas properties                           | (9,460,830)       | (2,293,497)       |
| Acquisition of office equipment                                | 2,182             | (1,863)           |
| Proceeds from sale of leases                                   | -                 | 2,127,489         |
| Net cash provided by (used) in investing activities            | (9,458,648)       | (167,871)         |
| Cash Flows From Financing Activities                           |                   |                   |
| Proceeds from short term advance                               | -                 | 150,000           |

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|                                           |             |             |
|-------------------------------------------|-------------|-------------|
| Repayment of short term advance           | -           | (150,000)   |
| Proceeds from sale of common stock        | -           | 3,000,000   |
| Proceeds from sale of preferred stock     | -           | 1,000,000   |
| Preferred dividends paid in cash          | -           | (320,724)   |
| Proceeds from warrant exercise            | 243,300     | 1,999,310   |
| Proceeds from promissory notes            | 10,541,475  | 708,014     |
| Repayment of convertible notes            | (2,509,500) | -           |
| Repayment of promissory notes             | -           | (649,741)   |
| Net cash provided by financing activities | 8,275,275   | 5,736,859   |
| Net increase (decrease) in cash           | (717,781)   | 742,899     |
| Cash - beginning of period                | 1,769,499   | 1,026,600   |
| Cash - end of period                      | \$1,051,720 | \$1,769,499 |

Supplemental disclosure of cash flow information: (Non Cash Items)

|                                                                |             |             |
|----------------------------------------------------------------|-------------|-------------|
| Common stock issued for financing costs                        | \$279,754   | \$-         |
| Common stock issued for mineral interests                      | \$6,812,362 | \$1,975,046 |
| Common stock issued in conversion of promissory notes          | \$1,007,890 | \$-         |
| Accounts payable increase-Investment in oil and gas properties | \$375,000   | \$-         |
| Warrants issued for mineral interests                          | \$-         | \$1,290,761 |
| Cash paid for interest                                         | \$813,652   | \$603,157   |

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



## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

### 1. NATURE OF BUSINESS

Torchlight Energy Resources, Inc. (“Company”) was incorporated in October 2007 under the laws of the State of Nevada as Pole Perfect Studios, Inc. (“PPS”). From its incorporation to November 2010, the company was primarily engaged in business start-up activities.

On November 23, 2010, we entered into and closed a Share Exchange Agreement (the “Exchange Agreement”) between the major shareholders of PPS and the shareholders of Torchlight Energy, Inc. (“TEI”). As a result of the transactions effected by the Exchange Agreement, at closing TEI became our wholly-owned subsidiary, and the business of TEI became our sole business. TEI was incorporated under the laws of the State of Nevada in June 2010. We are engaged in the acquisition, exploitation and/or development of oil and natural gas properties in the United States. We operate our business through our subsidiaries Torchlight Energy Inc., Torchlight Energy Operating, LLC, and Hudspeth Oil Corporation, Torchlight Hazel LLC, and Winkler Properties LLC.

### 2. GOING CONCERN

At December 31, 2017, the Company had not yet achieved profitable operations. We had a net loss of \$919,910 for the year ended December 31, 2017 and had accumulated losses of \$83,507,693 since our inception. We expect to incur further losses in the development of our business. The Company had working capital as of December 31, 2017 of \$886,503. These conditions raise substantial doubt about the Company’s ability to continue as a going concern.

The Company’s ability to continue as a going concern is dependent on its ability to generate future profitable operations and/or to obtain the necessary financing to meet its obligations and repay its liabilities arising from normal business operations when they come due. Management’s plan to address the Company’s ability to continue as a going concern includes: (1) obtaining debt or equity funding from private placement or institutional sources; (2) obtain loans from financial institutions, where possible, or (3) participating in joint venture transactions with third parties. Although management believes that it will be able to obtain the necessary funding to allow the Company to remain a going concern through the methods discussed above, there can be no assurances that such methods will prove successful.

These consolidated financial statements have been prepared assuming that the Company will continue as a going concern and therefore, the financial statements do not include any adjustments to reflect the possible future effects on the recoverability and classification of assets or the amount and classifications of liabilities that may result from the outcome of this uncertainty.

### 3. SIGNIFICANT ACCOUNTING POLICIES

The Company maintains its accounts on the accrual method of accounting in accordance with accounting principles generally accepted in the United States of America. Accounting principles followed and the methods of applying those principles, which materially affect the determination of financial position, results of operations and cash flows are summarized below:

Use of estimates – The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and certain assumptions that affect the amounts reported in these consolidated financial statements and accompanying notes. Actual results could differ from these estimates.

Basis of presentation—The financial statements are presented on a consolidated basis and include all of the accounts of Torchlight Energy Resources Inc. and its wholly owned subsidiaries, Torchlight Energy, Inc., Torchlight Energy Operating, LLC, Hudspeth Oil Corporation, Torchlight Hazel LLC, and Warwink Properties LLC. All significant intercompany balances and transactions have been eliminated.

Risks and uncertainties – The Company’s operations are subject to significant risks and uncertainties, including financial, operational, technological, and other risks associated with operating an emerging business, including the potential risk of business failure.

Concentration of risks – At times the Company’s cash balances are in excess of amounts guaranteed by the Federal Deposit Insurance Corporation. The Company’s cash is placed with a highly rated financial institution, and the Company regularly monitors the credit worthiness of the financial institutions with which it does business.

Fair value of financial instruments – Financial instruments consist of cash, receivables, payables and promissory notes, if any. The estimated fair values of cash, receivables, and payables approximate the carrying amount due to the relatively short maturity of these instruments. The carrying amounts of any promissory notes approximate their fair value giving affect for the term of the note and the effective interest rates.



## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

### 3. SIGNIFICANT ACCOUNTING POLICIES - continued

For assets and liabilities that require re-measurement to fair value the Company categorizes them in a three-level fair value hierarchy as follows:

- Level 1 inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities.
- Level 2 inputs are quoted prices for similar assets and liabilities in active markets or inputs that are observable for the asset or liability, either directly or indirectly through market corroboration.
- Level 3 inputs are unobservable inputs based on management's own assumptions used to measure assets and liabilities at fair value.

A financial asset or liability's classification within the hierarchy is determined based on the lowest level input that is significant to the fair value measurement.

Cash and cash equivalents - Cash and cash equivalents include certain investments in highly liquid instruments with original maturities of three months or less.

Accounts receivable – Accounts receivable consist of uncollateralized oil and natural gas revenues due under normal trade terms, as well as amounts due from working interest owners of oil and gas properties for their share of expenses paid on their behalf by the Company. Management reviews receivables periodically and reduces the carrying amount by a valuation allowance that reflects management's best estimate of the amount that may not be collectible. As of December 31, 2017 and December 31, 2016, no valuation allowance was considered necessary.

As of December 31, 2017 and 2016 accounts receivable included \$419,839 the Company computed as being due from Husky Ventures with respect to the sale of Chisholm Trail properties in 2015 and in dispute as part of the Husky legal action in process at those dates. Additionally, a payment of \$520,400 made by Husky Ventures which is also disputed by the Company is included in current liabilities captioned "Funds received pending settlement".

Oil and gas properties – The Company uses the full cost method of accounting for exploration and development activities as defined by the Securities and Exchange Commission ("SEC"). Under this method of accounting, the costs of unsuccessful, as well as successful, exploration and development activities are capitalized as properties and equipment. This includes any internal costs that are directly related to property acquisition, exploration and development activities but does not include any costs related to production, general corporate overhead or similar activities. Gain or loss on the sale or other disposition of oil and gas properties is not recognized, unless the gain or loss would significantly alter the relationship between capitalized costs and proved reserves.

Oil and gas properties include costs that are excluded from costs being depleted or amortized. Oil and natural gas property costs excluded represent investments in unevaluated properties and include non-producing leasehold, geological, and geophysical costs associated with leasehold or drilling interests and exploration drilling costs. The Company allocates a portion of its acquisition costs to unevaluated properties based on relative value. Costs are transferred to the full cost pool as the properties are evaluated over the life of the reservoir. Unevaluated properties are reviewed for impairment at least quarterly and are determined through an evaluation considering, among other factors, seismic data, requirements to relinquish acreage, drilling results, remaining time in the commitment period, remaining capital plan, and political, economic, and market conditions.

Gains and losses on the sale of oil and gas properties are not generally reflected in income unless the gain or loss would significantly alter the relationship between capitalized costs and proved reserves. Sales of less than 100% of the Company's interest in the oil and gas property are treated as a reduction of the capital cost of the field, with no gain or loss recognized, as long as doing so does not significantly affect the unit-of-production depletion rate. Costs of retired equipment, net of salvage value, are usually charged to accumulated depreciation.

Capitalized interest – The Company capitalizes interest on unevaluated properties during the periods in which they are excluded from costs being depleted or amortized. During the years ended December 31, 2017 and 2016, the Company capitalized \$1,010,868 and \$215,938, respectively, of interest on unevaluated properties.

Depreciation, depletion, and amortization – The depreciable base for oil and natural gas properties includes the sum of all capitalized costs net of accumulated depreciation, depletion, and amortization ("DD&A"), estimated future development costs and asset retirement costs not included in oil and natural gas properties, less costs excluded from amortization. The depreciable base of oil and natural gas properties is amortized on a unit-of-production method.

Ceiling test – Future production volumes from oil and gas properties are a significant factor in determining the full cost ceiling limitation of capitalized costs. Under the full cost method of accounting, the Company is required to periodically perform a "ceiling test" that determines a limit on the book value of oil and gas properties. If the net capitalized cost of proved oil and gas properties, net of related deferred income taxes, plus the cost of unproved oil and gas properties, exceeds the present value of estimated future net cash flows discounted at 10 percent, net of related tax affects, plus the cost of unproved oil and gas properties, the excess is charged to expense and reflected as additional accumulated DD&A. The ceiling test calculation uses a commodity price assumption which is based on the unweighted arithmetic average of the price on the first day of each month for each month within the prior 12 month period and excludes future cash outflows related to estimated abandonment costs.



## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

### 3. SIGNIFICANT ACCOUNTING POLICIES - continued

The determination of oil and gas reserves is a subjective process, and the accuracy of any reserve estimate depends on the quality of available data and the application of engineering and geological interpretation and judgment. Estimates of economically recoverable reserves and future net cash flows depend on a number of variable factors and assumptions that are difficult to predict and may vary considerably from actual results. In particular, reserve estimates for wells with limited or no production history are less reliable than those based on actual production. Subsequent re-evaluation of reserves and cost estimates related to future development of proved oil and gas reserves could result in significant revisions to proved reserves. Other issues, such as changes in regulatory requirements, technological advances, and other factors which are difficult to predict could also affect estimates of proved reserves in the future.

**Asset retirement obligations** –The fair value of a liability for an asset’s retirement obligation (“ARO”) is recognized in the period in which it is incurred if a reasonable estimate of fair value can be made, with the corresponding charge capitalized as part of the carrying amount of the related long-lived asset. The liability is accreted to its then-present value each subsequent period, and the capitalized cost is depleted over the useful life of the related asset. Abandonment costs incurred are recorded as a reduction of the ARO liability.

Inherent in the fair value calculation of an ARO are numerous assumptions and judgments including the ultimate settlement amounts, inflation factors, credit adjusted discount rates, timing of settlement, and changes in the legal, regulatory, environmental, and political environments. To the extent future revisions to these assumptions impact the fair value of the existing ARO liability, a corresponding adjustment is made to the oil and gas property balance. Settlements greater than or less than amounts accrued as ARO are recorded as a gain or loss upon settlement.

**Income taxes** - Income taxes are accounted for under the asset and liability method. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss carry forwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. A valuation allowance is established to reduce deferred tax assets if it is more likely than not that the related tax benefits will not be realized.

Authoritative guidance for uncertainty in income taxes requires that the Company recognize the financial statement benefit of a tax position only after determining that the relevant tax authority would more likely than not sustain the position following an examination. Management has reviewed the Company’s tax positions and determined there were no uncertain tax positions requiring recognition in the consolidated financial statements. Company tax returns remain subject to Federal and State tax examinations. Generally, the applicable statutes of limitation are three to four years from their respective filings.

Estimated interest and penalties related to potential underpayment on any unrecognized tax benefits are classified as a component of tax expense in the statement of operation. The Company has not recorded any interest or penalties associated with unrecognized tax benefits for any periods covered by these financial statements.

**Share-based compensation** – Compensation cost for equity awards is based on the fair value of the equity instrument on the date of grant and is recognized over the period during which an employee is required to provide service in exchange for the award. Compensation cost for liability awards is based on the fair value of the vested award at the end of each period.

The Company accounts for stock option awards using the calculated value method. The expected term was derived using the simplified method provided in Securities and Exchange Commission release Staff Accounting Bulletin No. 110, which averages an awards weighted average vesting period and contractual term for “plain vanilla” share options.

The Company accounts for any forfeitures of options when they occur. Previously recognized compensation cost for an award is reversed in the period that the award is forfeited.

The Company also issues equity awards to non-employees. The fair value of these option awards is estimated when the award recipient completes the contracted professional services. The Company recognizes expense for the estimated total value of the awards during the period from their issuance until performance completion, at which time the estimated expense is adjusted to the final value of the award as measured at performance completion.

The Company values warrant and option awards using the Black-Scholes option pricing model.

Revenue recognition – The Company recognizes oil and gas revenues when production is sold at a fixed or determinable price, persuasive evidence of an arrangement exists, delivery has occurred and title has transferred, and collectability is reasonably assured.



## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

### 3. SIGNIFICANT ACCOUNTING POLICIES - continued

Basic and diluted earnings (loss) per share – Basic earnings (loss) per common share is computed by dividing net income (loss) available to common shareholders by the weighted average number of common shares outstanding during the period. Diluted earnings (loss) per common share is computed in the same way as basic earnings (loss) per common share except that the denominator is increased to include the number of additional common shares that would be outstanding if all potential common shares had been issued and if the additional common shares were dilutive. The calculation of diluted earnings per share excludes 20,882,132 shares issuable upon the exercise of outstanding warrants and options because their effect would be anti-dilutive.

Environmental laws and regulations – The Company is subject to extensive federal, state, and local environmental laws and regulations. Environmental expenditures are expensed or capitalized depending on their future economic benefit. The Company believes that it is in compliance with existing laws and regulations.

Recent accounting pronouncements – In May 2014, the FASB issued ASU 2014-09, Revenue From Contracts With Customers that introduces a new five-step revenue recognition model in which an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. This ASU also requires disclosures sufficient to enable users to understand the nature, amount, timing, and uncertainty of revenue and cash flows arising from contracts with customers, including qualitative and quantitative disclosures about contracts with customers, significant judgments and changes in judgments, and assets recognized from the costs to obtain or fulfill a contract. This standard is effective for fiscal years beginning after December 15, 2017, including interim periods within that reporting period. The Company adopted this standard on January 1, 2018 and has elected the modified retrospective method of adoption. The new standard is not expected to have a material impact on the financial statements but will require expanded disclosure of revenues.

In February 2016 the FASB, issued ASU, 2016-02, Leases. The ASU requires companies to recognize on the balance sheet the assets and liabilities for the rights and obligations created by leased assets. ASU 2016-02 will be effective for the Company in the first quarter of 2019, with early adoption permitted. The Company is currently evaluating the impact that the adoption of ASU 2016-02 will have on the Company's consolidated financial statements and related disclosures.

Other recently issued or adopted accounting pronouncements are not expected to have, or did not have, a material impact on the Company's financial position or results from operations.

Subsequent events – The Company evaluated subsequent events through March 15, 2018, the date of issuance of these financial statements. Subsequent events are disclosed in Note 11.

### 4. OIL & GAS PROPERTIES

The following table presents the capitalized costs for oil & gas properties of the Company as of December 31, 2017 and 2016:

| 2017 | 2016 |
|------|------|
|------|------|

|                                                           |              |             |
|-----------------------------------------------------------|--------------|-------------|
| Evaluated costs subject to amortization                   | \$5,022,129  | \$1,470,939 |
| Unevaluated costs                                         | 26,100,749   | 13,376,742  |
| Total capitalized costs                                   | 31,122,878   | 14,847,681  |
| Less accumulated depreciation, depletion and amortization | (5,543,599)  | (5,455,393) |
| Total oil and gas properties                              | \$25,579,279 | \$9,392,288 |

The Company identified impairment of \$2,300,626 in 2017 related to its unevaluated properties. Although we had no recognized impairment expense in 2017, the Company has adjusted the separation of evaluated versus unevaluated costs within its full cost pool to recognize the value impairment related to the expiration of unevaluated leases in 2017 in the amount of \$2,300,626. The impact of this change will be to increase the basis for calculation of future period's depletion, depreciation and amortization to include \$2,300,626 of cost which will effectively recognize the impairment on the Consolidated Statement of Income over future periods. The \$2,300,626 has also become an evaluated cost for purposes of future period's Ceiling Tests and which may further recognize the impairment expense recognized in future periods.



## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

## 4. OIL &amp; GAS PROPERTIES - continued

Due to the volatility of commodity prices, should oil and natural gas prices decline in the future, it is possible that a further write-down could occur. Proved reserves are estimated quantities of crude oil, natural gas, and natural gas liquids, which geological and engineering data demonstrate with reasonable certainty to be recoverable from known reservoirs under existing economic and operating conditions. The independent engineering estimates include only those amounts considered to be proved reserves and do not include additional amounts which may result from new discoveries in the future, or from application of secondary and tertiary recovery processes where facilities are not in place or for which transportation and/or marketing contracts are not in place. Estimated reserves to be developed through secondary or tertiary recovery processes are classified as unevaluated properties.

## Acquisition of Additional Interests in Hazel Project

On January 30, 2017, we and our wholly-owned subsidiary, Torchlight Acquisition Corporation, a Texas corporation (“TAC”), entered into and closed an Agreement and Plan of Reorganization and Plan of Merger with Line Drive Energy, LLC, a Texas limited liability company (“Line Drive”), under which agreements TAC merged with and into Line Drive and the separate existence of TAC ceased, with Line Drive being the surviving organization and becoming our wholly-owned subsidiary. Line Drive, which was wholly-owned by Gregory McCabe, our Chairman, owned certain assets and securities, including approximately 40.66% of 12,000 gross acres in the Hazel Project and 521,739 warrants to purchase our common stock (which warrants had been assigned by Mr. McCabe to Line Drive). Under the merger transaction, our shares of common stock of TAC converted into a membership interest of Line Drive, the membership interest in Line Drive held by Mr. McCabe immediately prior to the transaction ceased to exist, and we issued Mr. McCabe 3,301,739 restricted shares of common stock as consideration therefor. Immediately after closing, the 521,739 warrants held by Line Drive were cancelled, which warrants had an exercise price of \$1.40 per share and an expiration date of June 9, 2020. A Certificate of Merger for the merger transaction was filed with the Secretary of State of Texas on January 31, 2017. Subsequent to the closing the name of Line Drive Energy, LLC was changed to Torchlight Hazel, LLC.

Also on January 30, 2017, our wholly-owned subsidiary, Torchlight Energy, Inc., a Nevada corporation (“TEI”), entered into and closed a Purchase and Sale Agreement with Wolfbone Investments, LLC, a Texas limited liability company (“Wolfbone”) which is wholly-owned by Gregory McCabe, our Chairman. Under the agreement, TEI acquired certain of Wolfbone’s Hazel Project assets, including its interest in the Flying B Ranch #1 well and the 40 acre unit surrounding the well, for consideration of \$415,000, and additionally, Wolfbone caused to be cancelled a total of 2,780,000 warrants to purchase our common stock, including 1,500,000 warrants held by McCabe Petroleum Corporation, an entity owned by Mr. McCabe, and 1,280,000 warrants held by Green Hill Minerals, an entity owned by Mr. McCabe’s son, which warrant cancellations were effected through certain Warrant Cancellation Agreements. The 1,500,000 warrants held by McCabe Petroleum Corporation had an exercise price of \$1.00 per share and an expiration date of April 4, 2021. The warrants held by Green Hill Minerals included 100,000 warrants with an exercise price of \$1.73 and an expiration date of September 30, 2018 and 1,180,000 warrants with an exercise price of \$0.70 and an expiration date of February 15, 2020.

Since Mr. McCabe held the controlling interest in both Line Drive and Wolfbone Investments, LLC, the transactions were combined for accounting purposes. The working interest in the Hazel Project was the only asset held by Line Drive. The warrant cancellation was treated in the aggregate as an exercise of the warrants with the transfer of the working interests as the consideration. The Company recorded the transactions as an increase in its investment in the Hazel project working interests of \$3,644,431 which is equal to the exercise price of the warrants plus the cash paid to Wolfbone.

Upon the closing of the transactions, the Company's working interest in the Hazel project increased by 40.66% to a total ownership of 74%.

Effective June 1, 2017, the Company acquired an additional 6% working interest from unrelated working interest owners in exchange for 268,656 shares of common stock valued at \$373,430, increasing its working interest in the Hazel project to 80%.

#### Winkler Project, Winkler County, Texas

On December 1, 2017, the Agreement and Plan of Reorganization that we and our newly formed wholly-owned subsidiary, Torchlight Wolfbone Properties, Inc., a Texas corporation ("TWP"), entered into with McCabe Petroleum Corporation, a Texas corporation ("MPC"), and Warwink Properties, LLC, a Texas limited liability company ("Warwink Properties") closed. Under the agreement, which was entered into on November 14, 2017, TWP merged with and into Warwink Properties and the separate existence of TWP ceased, with Warwink Properties becoming the surviving organization and our wholly-owned subsidiary. Warwink Properties was wholly owned by MPC which is wholly owned by Gregory McCabe, our Chairman. Warwink Properties owns certain assets, including a 10.71875% working interest in 640 acres in Winkler County, Texas. At closing of the merger transaction, our shares of common stock of TWP converted into a membership interest of Warwink Properties, the membership interest in Warwink Properties held by MPC ceased to exist, and we issued MPC 2,500,000 restricted shares of common stock as consideration. Also on December 1, 2017, MPC closed its transaction with MECO IV, LLC ("MECO") for the purchase and sale of certain assets as contemplated by the Purchase and Sale Agreement dated November 9, 2017 (the "MECO PSA"), to which we are not a party. Under the MECO PSA, Warwink Properties received a carry from MECO (through the tanks) of up to \$1,475,000 in the next well drilled on the Winkler County leases. A Certificate of Merger for the merger transaction was filed with the Secretary of State of Texas on December 5, 2017.



## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

## 4. OIL &amp; GAS PROPERTIES - continued

Also on December 1, 2017, the transactions contemplated by the Purchase Agreement that our wholly-owned subsidiary, Torchlight Energy, Inc., a Nevada corporation ("TEI"), entered into with MPC closed. Under the Purchase Agreement, which was entered into on November 14, 2017, TEI acquired beneficial ownership of certain of MPC's assets, including acreage and wellbores located in Ward County, Texas (the "Ward County Assets"). As consideration under the Purchase Agreement, at closing TEI issued to MPC an unsecured promissory note in the principal amount of \$3,250,000, payable in monthly installments of interest only beginning on January 1, 2018, at the rate of 5% per annum, with the entire principal amount together with all accrued interest due and payable on December 31, 2020. In connection with TEI's acquisition of beneficial ownership in the Ward County Assets, MPC sold those same assets, on behalf of TEI, to MECO at closing of the MECO PSA, and accordingly, TEI received \$3,250,000 in cash for its beneficial interest in the Ward County Assets. Additionally, at closing of the MECO PSA, MPC paid TEI a performance fee of \$2,781,500 in cash as compensation for TEI's marketing and selling the Winkler County assets of MPC and the Ward County Assets as a package to MECO.

During 2016 the Company sold its Cimarron and Marcelina properties. Those sales of the Cimarron and the Marcelina properties in 2016 represented substantial percentages of reserves at the time of each sale and were presented on the Consolidated Statement of Operations for 2016. Proceeds from the sale of Cimarron and Marcelina properties were \$750,000 and \$877,489 respectively. The combined loss on sale for 2016 was \$283,285.

## 5. RELATED PARTY PAYABLES

As of December 31, 2017, related party payables consisted of accrued and unpaid compensation to one of our executive officers totaling \$45,000.

As of December 31, 2016, related party payables consisted of accrued and unpaid compensation to one of our executive officers totaling \$45,000 and \$192,044 in Director Fees payable to our Directors.

## 6. COMMITMENTS AND CONTINGENCIES

## Leases

The Company has a noncancelable lease for its office premises that expires on November 30, 2019 and which requires the payment of base lease amounts and executory costs such as taxes, maintenance and insurance. Rental expense for lease was \$84,197 and \$81,595 for the year ended December 31, 2017 and 2016, respectively.

Approximate future minimum rental commitments under the office premises lease are:

Year Ending December 31, Rent

|                    |           |
|--------------------|-----------|
| 2018               | \$96,660  |
| To 2019 Expiration | 88,605    |
| Total              | \$185,265 |

#### Environmental matters

The Company is subject to contingencies as a result of environmental laws and regulations. Present and future environmental laws and regulations applicable to the Company's operations could require substantial capital expenditures or could adversely affect its operations in other ways that cannot be predicted at this time. As of December 31, 2017 and 2016, no amounts had been recorded because no specific liability has been identified that is reasonably probable of requiring the Company to fund any future material amounts.

#### Litigation

Torchlight Energy Resources, Inc. and its subsidiary Torchlight Energy, Inc. has pending in the 429th judicial district court in Collin County, Texas a lawsuit against Husky Ventures, Inc., Charles V. Long, Silverstar of Nevada, Inc., Gastar Exploration Inc., J. Russell Porter, Michael A. Gerlich, and Jerry R. Schuyler that was originally filed in May 2016 (previous defendants April Glidewell, Maximus Exploration, LLC, Atwood Acquisitions, LLC and John M. Selser, Sr have been non-suited without prejudice to re-filing the claims). In the lawsuit, we allege, among other things, that the defendants acted improperly in connection with multiple transactions, and that the defendants misrepresented and omitted material information to us with respect to these transactions. The lawsuit seeks damages arising from 15 different causes of action, including without limitation, violations of the Texas Securities Act, fraud, negligent misrepresentation, breach of fiduciary duty, breach of contract, unjust enrichment and tortious interference.



## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

### 6. COMMITMENTS AND CONTINGENCIES - continued

On April 13, 2017, Husky Ventures, Inc. filed in the above lawsuit a counterclaim against Torchlight Energy Resources, Inc. and its subsidiary Torchlight Energy, Inc., and a third-party petition against John Brda, the Chief Executive Officer of Torchlight Energy Resources, Inc., and Willard McAndrew III, a former officer of Torchlight Energy Resources, Inc. (“Husky Counterclaim”). The Husky Counterclaim asserts breach of contract against Torchlight Energy Resources, Inc. and its subsidiary Torchlight Energy, Inc. and asserts a claim for tortious interference with Husky’s contractual relationship with Torchlight and a claim for conspiracy to tortiously interfere with unspecified Husky business and contractual relationships against Torchlight Energy Resources, Inc. and its subsidiary Torchlight Energy, Inc., John Brda and Willard McAndrew III. We believe the Husky Counterclaim is without merit and intend to vigorously defend against it.

On May 22, 2017, the Court granted Gastar Exploration, Inc., J. Russell Porter, Michael A. Gerlich, and Jerry R. Schuyler’s (“Gastar Defendants”) motion for summary judgment dismissing all of Torchlight’s claims against the Gastar Defendants with prejudice. The only claim remaining related to the Gastar Defendants is a counterclaim against Torchlight by Gastar Exploration, Inc. for Torchlight’s alleged breach of a release that Gastar Exploration, Inc. claims occurred because Torchlight filed this lawsuit against the Gastar Defendants. Torchlight alleges in its lawsuit that this release is unenforceable against all the Defendants including but not limited to Gastar Defendants. On January 12, 2018, the Court heard but has not yet ruled on cross-motions for summary judgment by Gastar and Torchlight to resolve Gastar’s remaining claims against Torchlight. The case is currently set for trial on May 30, 2018.

### 7. STOCKHOLDERS’ EQUITY

#### Common Stock

During the years ended December 31, 2017 and 2016, the Company issued -0- and 3,750,000 shares of common stock, respectively, for cash of \$-0- and \$3,000,000.

During the years ended December 31, 2017 and 2016, the Company issued 507,897 and 768,832 shares of common stock with total fair values of \$579,754 and \$670,074, respectively, as compensation for services.

During the years ended December 31, 2017 and 2016, the Company issued 6,420,395 and 2,824,881 shares of common stock for lease interests with total fair values of \$6,812,362 and \$1,975,046, respectively.

During the year ended December 31, 2017 and 2016, the Company issued -0- and 10,257,439 shares of common stock, respectively, in conversions of preferred stock valued at \$-0- and \$13,399,992.

During the year ended December 31, 2017 the Company issued 1,007,890 shares of common stock, in conversions of notes payable valued \$1,007,890.

During the year ended December 31, 2017 and 2016, the Company issued 307,349 and 3,888,745 shares of common stock, respectively, resulting from warrant exercises for consideration totaling \$243,300 and \$2,543,749.

#### Preferred Stock

During the year ended December 31, 2016, the Company issued 10,000 shares of Series C preferred stock for \$1,000,000 in cash. The proceeds were deposited as a prepayment with the operator for development cost of the

Flying B #2 well in the Hazel Project. The preferred holders exercised their option in fourth quarter of 2016 to convert their preferred shares into an aggregate 33.33% working interest in the Flying "B" #2 whereupon they received credit for the prepayment to their working interest joint interest billing accounts.

During the year ended December 31, 2016 the Company paid dividends on preferred stock in cash of \$320,724. In addition, during the year 2016, 440,262 shares of common stock were issued for dividends on preferred stock.

There was no outstanding Preferred Stock as of December 31, 2017.

#### Warrants and Options

During the years ended December 31, 2017 and 2016, the Company issued/vested 1,808,026 and 6,437,267 warrants and options with total fair values of \$1,093,104 and \$2,205,231, respectively, as compensation for services.

During the years ended December 31, 2017, and 2016, the Company issued -0- and 137,500 warrants, respectively, in connection with financing transactions, with total values of \$-0- and \$80,750.

During the years ended December 31, 2017 and 2016, the Company issued -0- and 3,412,525 warrants and 6,420,395 and 2,824,881 shares of common stock, respectively, in connection with the acquisition of lease interests, respectively, with total value of \$6,812,362 and \$3,265,807.



## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

## 7. STOCKHOLDERS' EQUITY - continued

A summary of warrants outstanding as of December 31, 2017 by exercise price and year of expiration is presented below:

Exercise    Expiration Date in

| Price  | 2018      | 2019      | 2020      | 2021    | Total      |
|--------|-----------|-----------|-----------|---------|------------|
| \$0.50 | 400,000   | -         | -         | -       | 400,000    |
| \$0.70 | -         | -         | 420,000   | -       | 420,000    |
| \$0.77 | -         | 100,000   | -         | -       | 100,000    |
| \$1.00 | -         | 25,116    | -         | -       | 25,116     |
| \$1.03 | -         | -         | -         | 120,000 | 120,000    |
| \$1.08 | -         | 37,500    | -         | -       | 37,500     |
| \$1.40 | -         | -         | 1,121,736 | -       | 1,121,736  |
| \$1.64 | -         | -         | -         | 200,000 | 200,000    |
| \$1.73 | 100,000   | -         | -         | -       | 100,000    |
| \$1.80 | -         | -         | 1,250,000 | -       | 1,250,000  |
| \$2.00 | 1,906,249 | -         | -         | -       | 1,906,249  |
| \$2.03 | 2,000,000 | -         | -         | -       | 2,000,000  |
| \$2.09 | 2,800,000 | -         | -         | -       | 2,800,000  |
| \$2.23 | -         | -         | 832,512   | -       | 832,512    |
| \$2.29 | 120,000   | -         | -         | -       | 120,000    |
| \$2.50 | -         | 35,211    | -         | -       | 35,211     |
| \$2.82 | 38,174    | -         | -         | -       | 38,174     |
| \$3.50 | -         | 15,000    | -         | -       | 15,000     |
| \$4.50 | -         | 700,000   | -         | -       | 700,000    |
| \$6.00 | 523,123   | 22,580    | -         | -       | 545,703    |
| \$7.00 | -         | 700,000   | -         | -       | 700,000    |
|        | 7,887,546 | 1,635,407 | 3,624,248 | 320,000 | 13,467,201 |

A summary of stock options outstanding as of December 31, 2017 by exercise price and year of expiration is presented below:

Exercise    Expiration Date in

| Price | 2018 | 2019 | 2020 | 2021 | 2022 | Total |
|-------|------|------|------|------|------|-------|
|-------|------|------|------|------|------|-------|

|        |   |   |           |         |         |           |
|--------|---|---|-----------|---------|---------|-----------|
| \$0.97 | - | - | -         | 259,742 | -       | 259,742   |
| \$1.10 | - | - | -         | -       | 800,000 | 800,000   |
| \$1.57 | - | - | 5,997,163 | -       | -       | 5,997,163 |
| \$1.63 | - | - | -         | 58,026  | -       | 58,026    |
| \$1.79 | - | - | 300,000   | -       | -       | 300,000   |
|        | - | - | 6,297,163 | 317,768 | 800,000 | 7,414,931 |

At December 31, 2017, the Company had reserved 20,882,132 common shares for future exercise of warrants and options.



## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

## 7. STOCKHOLDERS' EQUITY - continued

Warrants and options granted were valued using the Black-Scholes Option Pricing Model. The assumptions used in calculating the fair value of the warrants issued were as follows:

2017

|                                       |                      |
|---------------------------------------|----------------------|
| Risk-free interest rate               | 1.47% - 2.06%        |
| Expected volatility of common stock   | 106% - 122%          |
| Dividend yield                        | 0.00%                |
| Discount due to lack of marketability | 20%                  |
| Expected life of option/warrant       | 2.75 years - 5 years |

2016

|                                       |                   |
|---------------------------------------|-------------------|
| Risk-free interest rate               | 0.78%-1.22%       |
| Expected volatility of common stock   | 101% - 189%       |
| Dividend yield                        | 0.00%             |
| Discount due to lack of marketability | 20-30%            |
| Expected life of warrant              | 3 years - 5 years |

## 8. INCOME TAXES

The Company recorded no income tax provision for 2017 and 2016 because of losses incurred. The Company has placed a full valuation allowance against net deferred tax assets because future realization of these assets is not assured.

The following is a reconciliation between the federal income tax benefit computed at statutory federal income tax rates and actual income tax provision for the years ended December 31, 2017 and 2016:

|                                              | Year ended        | Year ended        |
|----------------------------------------------|-------------------|-------------------|
|                                              | December 31, 2017 | December 31, 2016 |
| Federal income tax benefit at statutory rate | \$(312,769)       | \$(2,869,293)     |
| Permanent Differences                        | 1,640             | 3,000             |
| Other                                        | 719,197           | 4,096,946         |
| Change in valuation allowance                | (9,186,334)       | (1,230,653)       |
| Change in federal tax rate                   | 8,778,266         | -                 |
| Provision for income taxes                   | \$-               | \$-               |

The tax effects of temporary differences that gave rise to significant portions of deferred tax assets and liabilities at December 31, 2017 and December 31, 2016 are as follows:

December 31, 2017    December 31, 2016

## Deferred tax assets:

|                                                                |              |              |
|----------------------------------------------------------------|--------------|--------------|
| Net operating loss carryforward                                | \$11,116,332 | \$16,269,090 |
| Accruals                                                       | 9,450        | 15,300       |
| Reserves                                                       | 4,501,899    | 7,156,559    |
| Deferred tax liabilities:                                      |              |              |
| Intangible drilling and other costs for oil and gas properties | (1,447,405)  | (74,340)     |
| Net deferred tax assets and liabilities                        | 14,180,276   | 23,366,609   |
| Less valuation allowance                                       | (14,180,276) | (23,366,609) |
| Total deferred tax assets and liabilities                      | \$-          | \$-          |



## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

### 8. INCOME TAXES - continued

The Company had a net deferred tax asset related to federal net operating loss carryforwards of \$52,934,915 and \$51,028,330 at December 31, 2017 and December 31, 2016, respectively. The federal net operating loss carryforward will begin to expire in 2032. Realization of the deferred tax asset is dependent, in part, on generating sufficient taxable income prior to expiration of the loss carryforwards. The Company has placed a 100% valuation allowance against the net deferred tax asset because future realization of these assets is not assured.

On December 22, 2017, the U.S. government enacted comprehensive legislation titled the Tax Cuts and Jobs Act. Generally, effective for years 2018 and beyond, it makes broad and complex changes to the Internal Revenue Code, including, but not limited to, reducing the federal corporate income tax rate from 35% to 21%. As of December 31, 2017 we have made a reasonable estimate of the effects on our deferred tax assets and liabilities of the change in the corporate tax rate to be effective in 2018. The estimated amount is included our computation of net deferred tax assets and liabilities and the related valuation allowance.

### 9. PROMISSORY NOTES

The total outstanding balance of the 12% Series B Convertible Unsecured Promissory Notes at December 31, 2016 was \$3,569,500. On April 24, 2017 we used \$2,509,500 of the proceeds from the financing described below to redeem and repay a portion of the outstanding 12% Series B Convertible Unsecured Promissory Notes. Separately, \$1,000,000 of the principal amount of the Series B Notes plus accrued interest was converted into 1,007,890 shares of common stock valued at \$1,007,890 and \$60,000 was rolled into the new debt financing.

On April 10, 2017, we sold to investors in a private transaction two 12% unsecured promissory notes with a total of \$8,000,000 in principal amount. Interest only is due and payable on the notes each month at the rate of 12% per annum, with a balloon payment of the outstanding principal due and payable at maturity on April 10, 2020. The holders of the notes will also receive annual payments of common stock at the rate of 2.5% of principal amount outstanding, based on a volume-weighted average price. Both notes were sold at an original issue discount of 94.25% and accordingly, we received total proceeds of \$7,540,000 from the investors. Debt issuance costs were paid by issuance of 204,574 shares of common stock valued at \$279,754. We are using the proceeds for working capital and general corporate purposes, which includes, without limitation, drilling capital, lease acquisition capital and repayment of prior debt.

These 12% promissory notes allow for early redemption, provided that if we redeem before April 10, 2018, we must pay the holders all unpaid interest and common stock payments on the portion of the notes redeemed that would have been earned through April 10, 2018. The notes also contain certain covenants under which we have agreed that, except for financing arrangements with established commercial banking or financial institutions and other debts and liabilities incurred in the normal course of business, we will not issue any other notes or debt offerings which have a maturity date prior to the payment in full of the 12% notes, unless consented to by the holders.

The effective interest rate is 16.15%.

In connection with the transaction effective December 5, 2017 for the acquisition of the Warwink properties, the Company borrowed \$3.25 million from its Chairman, Greg McCabe on a three-year interest only promissory note bearing interest at 5% per annum.

### 10. ASSET RETIREMENT OBLIGATIONS

The following is a reconciliation of the asset retirement obligation liability for the period December 31, 2015 through December 31, 2017:

Asset retirement obligation – December 31, 2015 \$29,083

|                               |          |
|-------------------------------|----------|
| Accretion expense             | 41       |
| Removal of ARO for wells sold | (22,073) |

Asset retirement obligation – December 31, 2016 \$7,051

|                                |       |
|--------------------------------|-------|
| Estimated liabilities recorded | 2,007 |
| Accretion expense              | 216   |

Asset retirement obligation – December 31, 2017 \$9,274



## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

### 11. SUBSEQUENT EVENTS

On February 6, 2018, we sold to an investor in a private transaction a 12% unsecured promissory note with a principal amount of \$4,500,000. Interest only is due and payable on the note each month at the rate of 12% per annum, with a balloon payment of the outstanding principal due and payable at maturity on April 10, 2020. The holder of the note will also receive annual payments of common stock at the rate of 2.5% of principal amount outstanding, based on a volume-weighted average price. We sold the note at an original issue discount of 96.27% and accordingly, we received total proceeds of \$4,332,150 from the investor. We intend to use the proceeds for working capital and general corporate purposes, which includes, without limitation, drilling capital, lease acquisition capital and repayment of prior debt.

This 12% promissory note allows for early redemption, provided that if we redeem before February 6, 2019, we must pay the holder all unpaid interest and common stock payments on the portion of the note redeemed that would have been earned through February 6, 2019. The note also contains certain covenants under which we have agreed that, except for financing arrangements with established commercial banking or financial institutions and other debts and liabilities incurred in the normal course of business, we will not issue any other notes or debt offerings which have a maturity date prior to the payment in full of the 12% note, unless consented to by the holder.



TORCHLIGHT ENERGY RESOURCES, INC.  
SUPPLEMENTAL INFORMATION ON OIL AND GAS EXPLORATION  
AND PRODUCTION ACTIVITIES  
(Unaudited)

The unaudited supplemental information on oil and gas exploration and production activities has been presented in accordance with Financial Accounting Standards Board Accounting Standards Codification Topic 932, Extractive Activities—Oil and Gas and the SEC’s final rule, Modernization of Oil and Gas Reporting.

Investment in oil and gas properties during the years ended December 31, 2017 and 2016 is detailed as follows:

|                            | 2017         | 2016        |
|----------------------------|--------------|-------------|
| Property acquisition costs | \$7,227,362  | \$3,265,807 |
| Development costs          | \$8,034,962  | \$2,055,526 |
| Exploratory costs          | \$-          | \$-         |
| Totals                     | \$15,262,324 | \$5,321,333 |

Property acquisition cost relates to the Company’s acquisition of additional working interests in the Hazel Project in west Texas and the acquisition of the Warwink Project, also in west Texas. The development costs include work in the Orogrande and Hazel projects in west Texas. No development costs were incurred for Oklahoma properties in 2017.

Property acquisition costs presented above exclude interest capitalized into the full cost pool of \$1,010,868 in 2017 and \$215,938 in 2016.

#### Oil and Natural Gas Reserves

##### Reserve Estimates

SEC Case. The following tables sets forth, as of December 31, 2017, our estimated net proved oil and natural gas reserves, the estimated present value (discounted at an annual rate of 10%) of estimated future net revenues before future income taxes (PV-10) and after future income taxes (Standardized Measure) of our proved reserves and our estimated net probable oil and natural gas reserves, each prepared using standard geological and engineering methods generally accepted by the petroleum industry and in accordance with assumptions prescribed by the Securities and Exchange Commission (“SEC”). All of our reserves are located in the United States.

The PV-10 value is a widely used measure of value of oil and natural gas assets and represents a pre-tax present value of estimated cash flows discounted at ten percent. PV-10 is considered a non-GAAP financial measure as defined by the SEC. We believe that our PV-10 presentation is relevant and useful to our investors because it presents the estimated discounted future net cash flows attributable to our proved reserves before taking into account the related future income taxes, as such taxes may differ among various companies. We believe investors and creditors use PV-10 as a basis for comparison of the relative size and value of our proved reserves to the reserve estimates of other companies. PV-10 is not a measure of financial or operating performance under GAAP and neither it nor the Standardized Measure is intended to represent the current market value of our estimated oil and natural gas reserves. PV-10 should not be considered in isolation or as a substitute for the standardized measure of discounted future net cash flows as defined under GAAP.

The estimates of our proved reserves and the PV-10 set forth herein reflect estimated future gross revenue to be generated from the production of proved reserves, net of estimated production and future development costs, using prices and costs under existing economic conditions at December 31, 2017. For purposes of determining prices, we used the average of prices received for each month within the 12-month period ended December 31, 2017, adjusted for quality and location differences, which was \$48.53 per barrel of oil and \$2.58 per MCF of gas. This average historical price is not a prediction of future prices. The amounts shown do not give effect to non-property related expenses, such as corporate general administrative expenses and debt service, future income taxes or to depreciation, depletion and amortization.



December 31, 2017

December 31, 2017

Reserves

Future Net Revenue (M\$)

Present Value Discounted

| Category            | Oil (Bbls) | Gas (Mcf) | Total (BOE) | Total | at 10% |
|---------------------|------------|-----------|-------------|-------|--------|
| Proved Producing    | 2,300      | 43,800    | 9,600       | \$132 | \$96   |
| Proved Nonproducing | 0          | 0         | 0           | \$-   | \$-    |
| Total Proved        | 2,300      | 43,800    | 9,600       | \$132 | \$96   |

Standardized Measure of Future Net Cash Flows Related to  
Proved Oil and Gas Properties \$123

Probable Undeveloped 0 0 0 \$- \$-

December 31, 2016

December 31, 2016

Reserves

Future Net Revenue (M\$)

Present Value Discounted

| Category            | Oil (Bbls) | Gas (Mcf) | Total (BOE) | Total | at 10% |
|---------------------|------------|-----------|-------------|-------|--------|
| Proved Producing    | 1,400      | 23,300    | 5,284       | \$31  | \$29   |
| Proved Nonproducing | 46,800     | 467,600   | 124,733     | \$776 | \$301  |
| Total Proved        | 48,200     | 490,900   | 130,017     | \$807 | \$330  |

Standardized Measure of Future Net Cash Flows Related to  
Proved Oil and Gas Properties \$341

|                      |   |   |   |     |     |
|----------------------|---|---|---|-----|-----|
| Probable Undeveloped | 0 | 0 | 0 | \$- | \$- |
|----------------------|---|---|---|-----|-----|

The upward revisions of previous estimates from 2016 to 2017 of proved producing reserves of 900 Bbls and 20,500 MCF results primarily from 2017 reserve report calculations for the Company's properties driven by industry conditions and the change in the proportional quantities of oil and gas in production from the Judy well in Oklahoma from 2016 to 2017.

Reserve values as of December 31, 2017 are related to a single producing well in Oklahoma – the Judy well in the Prairie Grove AMI.

BOE equivalents are determined by combining barrels of oil with MCF of gas divided by six.



Standardized Measure of  
Oil & Gas Quantities -  
Volume Rollforward

Year Ended December 31,  
2017

The following table sets  
forth the Company's net  
proved reserves, including  
the changes therein, and  
proved

developed reserves:

|                                             | Crude Oil (Bbls) | Natural Gas (Mcf) | BOE       |
|---------------------------------------------|------------------|-------------------|-----------|
| TOTAL PROVED RESERVES:                      |                  |                   |           |
| Beginning of period                         | 48,200           | 490,900           | 130,017   |
| Revisions of previous estimates             | (35,509)         | (437,841)         | (108,483) |
| Extensions, discoveries and other additions | -                | -                 | -         |
| Divestiture of reserves                     | -                | -                 | -         |
| Acquisition of reserves                     | -                | -                 | -         |
| Production                                  | (10,391)         | (9,259)           | (11,934)  |
| End of period                               | 2,300            | 43,800            | 9,600     |
| PROVED DEVELOPED RESERVES                   |                  |                   |           |
| Proved developed producing                  | 2,300            | 43,800            | 9,600     |
| Proved nonproducing                         | -                | -                 | -         |
| Total                                       | 2,300            | 43,800            | 9,600     |

Standardized Measure of Oil & Gas Quantities

Year Ended December 31, 2017 & 2016

The standardized measure of discounted future net cash flows relating

to proved oil and natural gas reserves is as follows : 2017 2016

|                                                                                     |           |             |
|-------------------------------------------------------------------------------------|-----------|-------------|
| Future cash inflows                                                                 | \$240,370 | \$3,156,970 |
| Future production costs                                                             | (108,000) | (1,000,410) |
| Future development costs                                                            | -         | (1,350,000) |
| Future income tax expense                                                           | -         | -           |
| Future net cash flows                                                               | 132,370   | 806,560     |
| 10% annual discount for estimated timing of cash flows                              | (9,102)   | (465,644)   |
| Standardized measure of discounted future net cash flows related to proved reserves | \$123,268 | \$340,916   |

A summary of the changes in the standardized measure of discounted

future net cash flows applicable to proved oil and natural gas reserves

is as follows :

|                                                                                                        | 2017      | 2016        |
|--------------------------------------------------------------------------------------------------------|-----------|-------------|
| Balance, beginning of period                                                                           | \$340,916 | \$5,935,188 |
| Net change in sales and transfer prices and in production (lifting) costs related to future production | 207,241   | (482,569)   |
| Changes in estimated future development costs                                                          | 116,934   | (791,630)   |
| Net change due to revisions in quantity estimates                                                      | (129,565) | 482,272     |
| Accretion of discount                                                                                  | 28,604    | 80,393      |
| Other                                                                                                  | (43,372)  | 172,169     |
| Net change due to extensions and discoveries                                                           | -         | -           |
| Net change due to sales of minerals in place                                                           | -         | (191,470)   |
| Sales and transfers of oil and gas produced during the period                                          | (397,490) | (29,749)    |
| Previously estimated development costs incurred during the period                                      | -         | 58,575      |
| Net change in income taxes                                                                             | -         | (4,892,263) |
| Balance, end of period                                                                                 | \$123,268 | \$340,916   |



Due to the inherent uncertainties and the limited nature of reservoir data, both proved and probable reserves are subject to change as additional information becomes available. The estimates of reserves, future cash flows, and present value are based on various assumptions, including those prescribed by the SEC, and are inherently imprecise. Although we believe these estimates are reasonable, actual future production, cash flows, taxes, development expenditures, operating expenses, and quantities of recoverable oil and natural gas reserves may vary substantially from these estimates.

In estimating probable reserves, it should be noted that those reserve estimates inherently involve greater risk and uncertainty than estimates of proved reserves. While analysis of geoscience and engineering data provides reasonable certainty that proved reserves can be economically producible from known formations under existing conditions and within a reasonable time, probable reserves involve less certainty than reserves with a higher classification due to less data to support their ultimate recovery. Probable reserves have not been discounted for the additional risk associated with future recovery. Prospective investors should be aware that as the categories of reserves decrease with certainty, the risk of recovering reserves at the PV-10 calculation increases. The reserves and net present worth discounted at 10% relating to the different categories of proved and probable have not been adjusted for risk due to their uncertainty of recovery and thus are not comparable and should not be summed into total amounts.

#### Reserve Estimation Process, Controls and Technologies

The reserve estimates, including PV-10 estimates, set forth above were prepared by PeTech Enterprises, Inc. for the Company's Properties in Oklahoma. A copy of their full reports with regard to our reserves is attached as Exhibit 99.1 to this annual report on Form 10-K. These calculations were prepared using standard geological and engineering methods generally accepted by the petroleum industry and in accordance with SEC financial accounting and reporting standards.

#### Results of Operations for Oil and Gas Producing Activities

| For the Year Ended December 31, 2017                                                         | Total     | Texas     | Oklahoma   |
|----------------------------------------------------------------------------------------------|-----------|-----------|------------|
| Oil and Gas revenue                                                                          | \$570,499 | \$521,820 | \$48,679   |
| Production costs                                                                             | 173,187   | 155,897   | 17,290     |
| Depreciation, depletion, and amortization                                                    | 100,156   | 0         | 100,156    |
| Exploration expenses                                                                         | -         | -         | -          |
|                                                                                              | 273,343   | 155,897   | 117,446    |
| Income tax expense                                                                           | -         | -         | -          |
| Results of Operations (excluding corporate overhead, impairment expense, and interest costs) | \$297,156 | \$365,923 | \$(68,767) |

ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

Not Applicable.

ITEM 9A. CONTROLS AND PROCEDURES

Management's Evaluation of Disclosure Controls and Procedures

Our management, with the participation of our Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act) as of December 31, 2017. Based on this evaluation, our Chief Executive Officer and Chief Financial Officer have concluded that, as of December 31, 2017, our disclosure controls and procedures were effective, in that they ensure that information required to be disclosed by us in the reports that we file or submit under the Exchange Act is (1) recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and (2) accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure.



## ITEM 9A. CONTROLS AND PROCEDURES - continued

### Management's Annual Report on Internal Control Over Financial Reporting

Management acknowledges its responsibility for establishing and maintaining adequate internal control over financial reporting in accordance with Rule 13a-15(f) promulgated under the Exchange Act. The company's internal control over financial reporting includes those policies and procedures that (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Management has also evaluated the effectiveness of its internal control over financial reporting in accordance with generally accepted accounting principles within the guidelines of the Committee of Sponsoring Organizations of the Treadway Commission framework (2013). Based on the results of this evaluation, management has determined that the Company's internal control over financial reporting was effective as of December 31, 2017. The independent registered public accounting firm of Briggs & Veselka Co, as auditors of the Company's financial statements included in the Annual Report, has issued an attestation report on the Company's internal control over financial reporting.

### Changes in Internal Controls

There were no changes in our Company's internal control over financial reporting (as defined in Rule 13a-15(f) of the Securities Exchange Act of 1934) during the quarter ended December 31, 2017, that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

### Limitations on Effectiveness of Controls and Procedures

Our management, including our Chief Executive Officer and Chief Financial Officer, does not expect that disclosure controls or internal controls will prevent all error and all fraud. A control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. In addition, the design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within a company have been detected. These inherent limitations include the realities that judgments in decision-making can be faulty, and that breakdowns can occur because of simple error or mistake.

Additionally, controls can be circumvented by the individual acts of some persons, by collusion of two or more people or by management's override of the control. The design of any systems of controls is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions. Over time, control may become inadequate because of changes in conditions, or the degree of compliance with the policies or procedures may deteriorate. Because of these inherent limitations in a cost-effective control system, misstatements due to error or fraud may occur and not be detected. Individual persons may perform multiple tasks which normally would be allocated to separate persons and therefore extra diligence must be exercised during the period these tasks are combined.

## ITEM 9B. OTHER INFORMATION

Not applicable.



### PART III

#### ITEM 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE

Our executive officers and directors are as follows:

| Name               | Age | Position(s) and Office(s)                       |
|--------------------|-----|-------------------------------------------------|
| John A. Brda       | 53  | Chief Executive Officer, Secretary and Director |
| Roger N. Wurtele   | 71  | Chief Financial Officer                         |
| Greg McCabe, Sr.   | 56  | Director                                        |
| Alexandre Zyngier  | 48  | Director                                        |
| R. David Newton    | 63  | Director                                        |
| E. Scott Kimbrough | 67  | Director                                        |
| Michael Graves     | 50  | Director                                        |

Below is certain biographical information of our executive officers and directors:

John A. Brda – Mr. Brda has been our Chief Executive Officer since December 2014 and our Secretary and a member of the Board of Director since January 2012. He has been the Managing Member of Brda & Company, LLC since 2002, which provided consulting services to public companies—with a focus in the oil and gas sector—on investor relations, equity and debt financings, strategic business development and securities regulation matters, prior to him becoming President of the company.

We believe Mr. Brda is an excellent fit to our Board of Directors and management team based on his extensive experience in transaction negotiation and business development, particularly in the oil and gas sector as well as other non-related industries. He has consulted with many public companies in the last ten years, and we believe that his extensive network of industry professionals and finance firms will contribute to our success.

Roger N. Wurtele – Mr. Wurtele has served as our Chief Financial Officer since September 2013. He is a versatile, experienced finance executive that has served as Chief Financial Officer for several public and private companies. He has a broad range of experience in public accounting, corporate finance and executive management. Mr. Wurtele previously served as CFO of Xtreme Oil & Gas, Inc. from February 2010 to September 2013. From May 2013 to September 2013 he worked as a financial consultant for us. From November 2007 to January 2010, Mr. Wurtele served as CFO of Lang and Company LLC, a developer of commercial real estate projects. He graduated from the University of Nebraska and has been a Certified Public Accountant for 40 years.

Gregory McCabe – Mr. McCabe has been a member of our Board of Directors since July 2016 and was appointed Chairman of the Board in October 2016. He is an experienced geologist who brings over 32 years of oil and gas experience to our company. He is a principal of numerous oil and gas focused entities including McCabe Petroleum Corporation, Manix Royalty, Masterson Royalty Fund and GMc Exploration. He has been the President of McCabe Petroleum Corporation from 1986 to the present. Mr. McCabe has been involved in numerous oil and gas ventures throughout his career and has a vast experience in technical evaluation, operations and acquisitions and divestitures. Mr. McCabe is also our largest stockholder and provided entry for us into our two largest assets, the Hazel Project in the Midland Basin and the Orogrande Project in Hudspeth County, Texas.

We believe that Mr. McCabe's background in geology and his many years in the oil and gas industry compliments the Board of Directors.

E. Scott Kimbrough - Mr. Kimbrough has served on our Board of Directors since October 2016. He is the owner of multiple independent oil and gas related companies, which he has managed for more than 20 years, including serving as the President of Maverick Oil & Gas Corporation for the last 22 years. His diverse oil and gas background spans 39 years and includes roles ranging from field operations to senior corporate management. Mr. Kimbrough began his career with Arco Oil & Gas Company, followed by work with independents including Quintana Petroleum Corporation, Lasmo Energy, and Nearburg Producing Company. His focus has been in domestic U.S. fields including the Permian Basin in West Texas and Southeast New Mexico, on and offshore Gulf Coast, Midcontinent, Rocky Mountain area and onshore California. Mr. Kimbrough received a Bachelor of Science in Personnel Management (Business) from Louisiana Tech University and a Bachelor of Science in Mechanical Engineering from Texas A&M University. He is a Registered Petroleum Engineer in the State of Texas.

We believe Mr. Kimbrough's wide ranging experience in operating E&P (exploration and production) companies make him an excellent fit to the Board of Directors.



ITEM 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE - continued

R. David Newton - Mr. Newton has been a member of our Board of Directors since October 2016. He has more than 25 years of experience in management consulting from various positions he has held with U.S. based investment firms. Additionally, he has been active in farming, ranching and oil and gas exploration for over 30 years. Since 1994 he has owned and managed R. David Newton and Associates, a management consulting and investment firm, through which he has focused on funding venture capital, channel distribution, startups, second and third stage financings, and corporate turnarounds. He holds a Bachelor of Science degree from the University of Texas at Austin.

Mr. Newton brings a depth of relationships developed through decades of participation in corporate finance and operational skills obtained while focused on helping growth stage entities involved in oil and natural gas, aerospace, timber and various other industries, and accordingly can make a substantial contribution to the Board.

Alexandre Zyngier - Mr. Zyngier has served on our Board of Directors since June 2016. He has been the Managing Director of Batuta Advisors since founding it in August 2013. The firm pursues high return investment and advisory opportunities in the distressed and turnaround sectors. Mr. Zyngier has over 20 years of investment, strategy, and operating experience. He is currently a director of Atari SA, AudioEye Inc. and GT Advanced Technologies, Inc. Before starting Batuta Advisors, Mr. Zyngier was a portfolio manager at Alden Global Capital from February 2009 until August 2013, investing in public and private opportunities. He has also worked as a portfolio manager at Goldman Sachs & Co. and Deutsche Bank Co. Additionally, he was a strategy consultant at McKinsey & Company and a technical brand manager at Procter & Gamble. Mr. Zyngier holds an MBA in Finance and Accounting from the University of Chicago and a BS in Chemical Engineering from UNICAMP in Brazil.

We believe that Mr. Zyngier's investment experience and his experience in overseeing a broad range of companies will greatly benefit the Board of Directors.

Michael J. Graves – Mr. Graves has served on the Board of Directors since August 17, 2017. He is a Certified Public Accountant, and since 2005 he has been a managing shareholder of Fitch & Graves in Sioux City, Iowa, which provides accounting and tax, financial planning, consulting and investment services. Since 2008, he has also been a registered representative with Western Equity Group where he has worked in investment sales. He is also presently a shareholder in several businesses involved in residential construction and property rentals. Previously, he worked at Bill Markve & Associates, Gateway 2000 and Deloitte & Touche. He graduated Summa Cum Laude from the University of South Dakota with a B.S. in Accounting.

With Mr. Graves' extensive background in accounting and investment businesses, we believe his understanding of financial statements, business valuations, and general business performance are a valuable asset to the Board.

Section 16(a) Beneficial Ownership Reporting Compliance

Section 16(a) of the Securities Exchange Act of 1934 requires our directors and executive officers, and persons who own beneficially more than ten percent of our common stock, to file reports of ownership and changes of ownership with the Securities and Exchange Commission. Based solely upon a review of Forms 3, 4 and 5 furnished to us during the fiscal year ended December 31, 2017, we believe that the directors, executive officers, and greater than ten percent beneficial owners have complied with all applicable filing requirements during the fiscal year ended December 31, 2017, with the exception of (i) three Form 4's (including a Form 4/A) filed late by Gregory McCabe, and (ii) a Form 4 filed late by Alexandre Zyngier.

Code of Ethics

We have adopted a code of ethics that applies to our principal executive officer, principal financial officer, principal accounting officer or controller, or persons performing similar functions. The Code of Ethics is available at our website at [torchlightenergy.com](http://torchlightenergy.com). Further, we undertake to provide by mail to any person without charge, upon request, a copy of such code of ethics if we receive the request in writing by mail to: Torchlight Energy Resources, Inc., 5700 W. Plano Parkway, Suite 3600, Plano, Texas 75093.

#### Procedures for Stockholders to Recommend Nominees to the Board

There have been no material changes to the procedures by which stockholders may recommend nominees to our Board of Directors since we last provided disclosure regarding this process.

#### Audit Committee

We maintain a separately-designated standing audit committee. The Audit Committee currently consists of our three independent directors, Alexandre Zyngier, Michael Graves, and R. David Newton. Mr. Zyngier is the Chairman of the Audit Committee, and the Board of Directors has determined that he is an audit committee financial expert as defined in Item 5(d)(5) of Regulation S-K. The primary purpose of the Audit Committee is to oversee our accounting and financial reporting processes and audits of our financial statements on behalf of the Board of Directors. The Audit Committee meets privately with our management and with our independent registered public accounting firm and evaluates the responses by our management both to the facts presented and to the judgments made by our outside independent registered public accounting firm.



## ITEM 11. EXECUTIVE COMPENSATION

The following table provides summary information for the years 2017 and 2016 concerning cash and non-cash compensation paid or accrued to or on behalf of certain executive officers.

## Summary Executive Compensation Table

|                             | Year | Salary    | Bonus | Stock Awards | Option Awards | Non-Equity Incentive Plan          | Change in Pension Value | All Other Compensation | Total       |
|-----------------------------|------|-----------|-------|--------------|---------------|------------------------------------|-------------------------|------------------------|-------------|
|                             |      | (\$)      | (\$)  | (\$)         | (\$)          | (\$)                               | (\$)                    | (\$)                   | (\$)        |
|                             |      |           |       | (A)          | (A)           | Compensation and                   |                         |                        |             |
| Name and Principal Position |      |           |       | (1)          |               | Nonqualified Deferred Compensation |                         |                        |             |
|                             |      |           |       |              |               |                                    | (\$)                    |                        |             |
| John A. Brda                | 2017 | \$375,000 | -     | -            | \$-           | -                                  | -                       | -                      | \$375,000   |
| CEO/Secretary/Director      | 2016 | \$375,000 | -     | -            | \$712,500     | -                                  | -                       | -                      | \$1,087,500 |
| Roger Wurtele               | 2017 | \$225,000 | -     | -            | \$-           | -                                  | -                       | -                      | \$225,000   |
| CFO                         | 2016 | \$225,000 | -     | -            | \$356,250     | -                                  | -                       | -                      | \$581,250   |

(A) Stock/Option Value as applicable is determined using the Black Scholes Method.

On June 11, 2015, we granted new stock option awards to our executive officers, as follows: 3,000,000 stock options to John Brda, President and Chief Executive Officer and 1,500,000 stock options to Roger Wurtele, Chief Financial Officer. The options were granted under our 2015 Stock Option Plan which plan was approved by (1) stockholders on September 9, 2015. The options are subject to a two-year vesting schedule with one-half vesting September 9, 2015, one-fourth vesting after one year of the grant date, and the remaining one-fourth vesting after the second year, provided however that the options will be subject to earlier vesting under certain events set forth in the 2015 Stock Option Plan, including without limitation a change in control.

## Setting Executive Compensation

We fix executive base compensation at a level we believe enables us to hire and retain individuals in a competitive environment and to reward satisfactory individual performance and a satisfactory level of contribution to our overall

business goals. We also take into account the compensation that is paid by companies that we believe to be our competitors and by other companies with which we believe we generally compete for executives.

In establishing compensation packages for executive officers, numerous factors are considered, including the particular executive's experience, expertise, and performance, our company's overall performance, and compensation packages available in the marketplace for similar positions. In arriving at amounts for each component of compensation, our Compensation Committee strives to strike an appropriate balance between base compensation and incentive compensation. The Compensation Committee also endeavors to properly allocate between cash and non-cash compensation (including without limitation stock and stock option awards) and between annual and long-term compensation.

#### Employment Agreements

On June 16, 2015, we entered into new five-year employment agreements with each of John Brda, our President and Chief Executive Officer and Roger Wurtele, our Chief Financial Officer. Under the new agreements, which replace and supersede their prior employment agreements, each individual's salary was increased by 25%, so that the salaries of Messrs. Brda and Wurtele were \$375,000, and \$225,000, respectively, provided these salary increases will accrue unpaid until such time as management believes there is adequate cash for such increases. Also under the new agreements, each individual was eligible for a bonus, at the Compensation Committee's discretion, of up to two times his salary and was eligible for any additional stock options, as deemed appropriate by the Compensation Committee. Each agreement also provided that if we (or our successor) terminate the employee upon the occurrence of a change in control, the employee will be paid in one lump sum his salary and any bonus or other amounts due through the end of the term of the agreement. Each employment agreement also has a covenant not to compete.



ITEM 11. EXECUTIVE COMPENSATION - continued

### Outstanding Equity Awards at Fiscal Year End

The following table details all outstanding equity awards held by our named executive officers at December 31, 2017:

|               | Option Awards |         |               |                        |                       |            |
|---------------|---------------|---------|---------------|------------------------|-----------------------|------------|
|               | Number of     |         | Number of     | Equity Incentive       |                       |            |
|               | Securities    |         | Securities    | Plan Awards: Number of |                       |            |
|               | Underlying    |         | Underlying    | Securities             |                       |            |
|               | Unexercised   |         | Unexercised   | Underlying             | Option                |            |
|               | Options       |         | Options       | Unexercised            | Exercise    Option    |            |
|               | (#)           |         | (#)           | Unearned Options       | Price      Expiration |            |
| Name          | Exercisable   |         | Unexercisable | (#)                    | (\$)                  | Date       |
|               |               |         |               |                        |                       |            |
| John A. Brda  | 245,000       |         | -             | -                      | \$2.00                | 9/4/2018   |
|               | 3,000,000     | (1)     |               | -                      | \$1.57                | 6/11/2020  |
| Roger Wurtele | 300,000       | (2) (3) | -             | -                      | \$2.09                | 10/10/2018 |
|               | 1,500,000     | (1)     | -             | -                      | \$1.57                | 6/11/2020  |

The options were awarded on June 11, 2015. The options were granted under our 2015 Stock Option Plan which plan was approved by stockholders on September 9, 2015. The options are subject to a two-year vesting schedule (1) with one-half vesting on September 9, 2015, one-fourth vesting after one year of the grant date, and the remaining one-fourth vesting after the second year, provided however that the options will be subject to earlier vesting under certain events set forth in the 2015 Stock Option Plan, including without limitation a change in control.

- (2) Mr. Wurtele gifted these options to Birch Glen Investments Ltd. Mr. Wurtele and his wife together hold a 98% interest in the general partner of Birch Glen Investments Ltd.
- (3) These options were awarded to Mr. Wurtele in October 2013. 100,000 options vested in October 2013 and the remaining 200,000 options vested on January 2, 2014.

### Compensation of Directors

We have no standard arrangement pursuant to which directors are compensated for any services they provide or for committee participation or special assignments. We anticipate, however, implementing more standardized director compensation arrangements in the near future.

### Summary Director Compensation Table

Compensation to directors during the year ended December 31, 2017 was as follows:

| Name                | Fees Earned       |                   | Option Awards         | Nonqualified                                |                                     |                             | Total     |
|---------------------|-------------------|-------------------|-----------------------|---------------------------------------------|-------------------------------------|-----------------------------|-----------|
|                     | Paid in Cash (\$) | Stock Awards (\$) | Option Awards (\$)(A) | Non-Equity Incentive Plan Compensation (\$) | Deferred Compensation Earnings (\$) | All Other Compensation (\$) |           |
| Alexandre Zyngier - |                   | \$112,500 (1)     | \$110,000 (2) -       |                                             | -                                   | -                           | \$185,000 |
| R. David Newton -   |                   | -                 | \$110,000 (2) -       |                                             | -                                   | -                           | \$110,000 |
| E. Scott Kimbrough  | -                 | -                 | \$110,000 (2) -       |                                             | -                                   | -                           | \$110,000 |
| Michael Graves      | -                 | -                 | \$110,000 (2) -       |                                             | -                                   | -                           | \$110,000 |

(A) Stock Value as applicable is determined using the Black Scholes Method.



ITEM 11. EXECUTIVE COMPENSATION - continued

In October 2016, our Board of Directors formed a special committee called the “Litigation Committee,” appointed Mr. Zyngier to that committee, and approved compensating Mr. Zyngier for his role with the Litigation Committee by paying him up to \$150,000 over four quarters, with the first quarterly payment of \$37,500 being made on October 11, 2016 and \$37,500 being payable at the beginning of each three months thereafter that certain litigation is not settled or otherwise resolved, up to a maximum amount of \$150,000. Each payment was to either be paid in cash or common stock at our election. For a stock payment, the amount of shares of common stock issued would be based on the closing price of our common stock on the day of the payment. On December 8, 2016, stockholders approved giving the Company authority to make these payments in stock. Immediately after the December 8, 2016 meeting of stockholders, the Board of Directors held a meeting, at which Mr. Zyngier and the Board discussed placing vesting restrictions on all the above shares described in this footnote, and accordingly such shares were not immediately issued. Subsequently in January 2017, the Board and Mr. Zyngier agreed on what the vesting restrictions would be and we issued him the 136,986 shares in connection with his directorship and 47,504 shares in lieu of the cash payment of \$37,500 that was payable to Mr. Zyngier on October 11, 2016 in connection with his role on the Litigation Committee. Additionally on April 26, 2017, 28,626 shares were issued for the \$37,500 payment due 1/11/17 and 23,885 shares were issued for the payment due 4/11/17. On 7/11/17, 25,000 shares were issued for the final payment. As of the date of this report, none of these shares have vested.

(2)

On August 17, 2017, this director was granted 200,000 stock options under the 2015 Stock Option Plan as director compensation. 100,000 of the stock options vested immediately, and the remaining 100,000 stock options will vest on August 17, 2018.

Compensation Policies and Practices as they Relate to Risk Management

We attempt to make our compensation programs discretionary, balanced and focused on the long term. We believe goals and objectives of our compensation programs reflect a balanced mix of quantitative and qualitative performance measures to avoid excessive weight on a single performance measure. Our approach to compensation practices and policies applicable to employees and consultants is consistent with that followed for its executives. Based on these factors, we believe that our compensation policies and practices do not create risks that are reasonably likely to have a material adverse effect on us.

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT

The following table sets forth information, as of March 15, 2018, concerning, except as indicated by the footnotes below, (i) each person whom we know beneficially owns more than 5% of our common stock, (ii) each of our directors, (iii) each of our named executive officers, and (iv) all of our directors and executive officers as a group. The table includes these persons’ beneficial ownership of common stock. Unless otherwise noted below, the address of each beneficial owner listed in the table is c/o Torchlight Energy Resources, Inc., 5700 W. Plano Parkway, Suite 3600, Plano, Texas 75093. We have determined beneficial ownership in accordance with the rules of the SEC. Except as indicated by the footnotes below, we believe, based on the information furnished to us, that the persons and entities named in the table below have sole voting and investment power with respect to all shares of common stock that they beneficially own, subject to applicable community property laws. Applicable percentage ownership is based on 63,378,033 shares of common stock outstanding at March 15, 2018 (which amount excludes the 262,001 restricted shares of common stock issued to our director Alexandre Zyngier). In computing the number of shares of common stock beneficially owned by a person and the percentage ownership of that person, we deemed outstanding shares of common stock subject to stock options or warrants held by that person that are currently exercisable or exercisable within 60 days of March 15, 2018 and shares of common stock issuable upon conversion of other securities held by

that person that are currently convertible or convertible within 60 days of March 15, 2018. We did not deem these shares outstanding, however, for the purpose of computing the percentage ownership of any other person. Unless otherwise noted, stock options and warrants referenced in the footnotes below are currently fully vested and exercisable. Beneficial ownership representing less than 1% is denoted with an asterisk (\*).



## ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT - continued

## Shares Beneficially Owned

| Common Stock                                                |            |            |
|-------------------------------------------------------------|------------|------------|
| Name of beneficial owner                                    | Shares     | % of Class |
| John A. Brda<br>President, CEO, Secretary and Director      | 5,513,322  | (1) 8.28   |
| Gregory McCabe<br>Director (Chairman of the Board)          | 13,648,390 | (2) 21.51  |
| Roger N. Wurtele<br>Chief Financial Officer                 | 1,810,000  | (3) 2.78   |
| E. Scott Kimbrough<br>Director                              | 258,884    | (4) *      |
| R. David Newton<br>Director                                 | 258,884    | (5) *      |
| Alexandre Zyngier<br>Director                               | 100,000    | *          |
| Michael J. Graves<br>Director                               | 125,000    | (6) *      |
| All directors and executive officers as a group (7 persons) | 21,814,480 | 32.10      |
| Robert Kenneth Dulin (7)                                    | 4,351,381  | (7) 6.68   |
| Willard G. McAndrew III (8)                                 | 3,993,046  | (8) 5.94   |

- (1) Includes 2,268,322 shares of common stock held by the John A. Brda Trust (the "Trust"). Mr. Brda is the settlor of the Trust and reserves the right to revoke the Trust without the consent of another person. Further, he is the trustee of the Trust and exercises investment control over the securities held by the Trust. Also includes stock options that are exercisable into 3,245,000 shares of common stock, held individually by Mr. Brda.

- Includes (a) 10,264,335 shares of common stock held individually by Mr. McCabe; (b) securities held by G Mc Exploration, LLC ("GME"), including (i) 797,099 shares of common stock and (ii) 86,956 shares issuable upon exercise of warrants; and (c) 2,500,000 shares of common stock beneficially owned by McCabe Petroleum Corporation ("MPC"). Mr. McCabe may be deemed to hold beneficial ownership of securities held by GME as a result of his ownership of 50% of the outstanding membership interests of GME. Mr. McCabe may be deemed to hold beneficial ownership of securities held by MPC as a result of his ownership of 100% of the outstanding shares of capital stock of MPC.

- Includes 10,000 shares of common stock and stock options that are exercisable into 1,500,000 shares of common stock held individually by Mr. Wurtele. Also includes stock options held by Birch Glen Investments Ltd. that are exercisable into 300,000 shares of common stock. Mr. Wurtele and his wife together hold a 98% interest in the general partner of Birch Glen Investments Ltd., and Mr. Wurtele shares voting and investment authority over the
- (3) shares held by Birch Glen Investments Ltd. Additionally, the general partner and 1% owner of WMDM Family, Ltd. (see footnote "(7)" below) is a limited liability company which is owned by a trust of which Mr. Wurtele is the trustee. Securities held by WMDM Family, Ltd. are not included, however, because Mr. Wurtele is not deemed to have voting or investment authority over the shares held by WMDM Family, Ltd. Mr. Wurtele disclaims beneficial ownership of shares held by WMDM Family, Ltd.
- (4) Includes stock options that are exercisable into 258,884 shares of common stock held individually by Mr. Kimbrough.
- (5) Includes stock options that are exercisable into 258,884 shares of common stock held individually by Mr. Newton.
- (6) Includes stock options that are exercisable into 100,000 shares of common stock held individually by Mr. Graves.



ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT - continued

Includes (a) securities held individually by Robert Kenneth Dulin, including (i) 27,000 shares of common stock and (ii) warrants that are exercisable into 150,000 shares of common stock; (b) 243,360 shares of common stock held in trust for the benefit of immediate family members of Mr. Dulin; (c) securities held by Sawtooth Properties, LLLP (“Sawtooth”), including (i) 892,258 shares of common stock and (ii) warrants that are exercisable into 234,745 shares of common stock; (d) securities held by Black Hills Properties, LLLP (“Black Hills”), including (i) 612,099 shares of common stock, and (ii) warrants that are exercisable into 189,956 shares of common stock; (e) securities held by Pine River Ranch, LLC (“Pine River”), including (i) 801,939 shares of common stock and (ii) (7) warrants that are exercisable into 450,024 shares of common stock; and (f) securities held by Pandora Energy, LP (“Pandora”), including warrants that are exercisable into 750,000 shares of common stock. Mr. Dulin is trustee/custodian of each of the trusts and/or accounts referenced in “(b)” above and has voting and investment authority over the shares held by them. Mr. Dulin is the Managing Partner of Sawtooth Properties, LLLP, the Managing Partner of Black Hills, the Managing Member of Pine River, and the General Partner of Pandora, and he has voting and investment authority over the shares held by each entity. Mr. Dulin’s address is 8449 Greenwood Drive, Niwot, Colorado, 80503. The information herein is based in part on information provided to us by Mr. Dulin, and accordingly, we are unable to verify the accuracy this information.

Includes 95,883 shares of common stock and stock options that are exercisable into 1,497,163 shares of common stock held individually by Mr. McAndrew. Also includes securities held by WMDM Family, Ltd., including warrants that are exercisable into 900,000 shares of common stock and stock options that are exercisable into (8) 1,500,000 shares of common stock. The general partner and 1% owner of WMDM Family, Ltd. is a limited liability company of which Mr. McAndrew is the manager. He has voting and investment authority over the shares held by WMDM Family, Ltd. Mr. McAndrew’s address is 6608 Indian Trail, Plano TX 75024. The information herein is based in part on information provided to us by Mr. McAndrew, and accordingly, we are unable to verify the accuracy this information.

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

On February 15, 2016, we entered into a consulting service agreement with Green Hill Minerals, LLC. As compensation for the consulting services provided under the agreement, we agreed to issue Green Hill Minerals 115,000 shares of common stock at signing, 115,000 shares of common stock 90 days from signing, 115,000 shares of common stock 180 days from signing and 115,000 shares of common stock 270 days from signing. Also under the agreement, we issued Green Hill Minerals 1,700,000 four-year warrants to purchase shares of common stock at an exercise price of \$0.70 per share, vesting as follows: 425,000 warrants at signing, 425,000 warrants 90 days from signing, 425,000 warrants 180 days from signing and 425,000 warrants 270 days from signing.

On March 31, 2016, Mr. McCabe made a short term, non-interest bearing loan to us of \$500,000. We repaid the loan in full on April 29, 2016.

Effective April 4, 2016, our subsidiary, Torchlight Energy Inc., acquired from McCabe Petroleum Corporation (“MPC”) a 66.66% working interest in approximately 12,000 acres in the Midland Basin in exchange for 1,500,000 warrants to purchase our common stock at an exercise price of \$1.00 for five years, and a back-in after payout of a 25% working interest to MPC. Gregory McCabe is the sole owner of MPC.

On January 30, 2017, we and our wholly-owned subsidiary, Torchlight Acquisition Corporation, a Texas corporation (“TAC”), entered into and closed an Agreement and Plan of Reorganization and Plan of Merger with Line Drive Energy, LLC, a Texas limited liability company (“Line Drive”), under which agreements TAC merged with and into Line Drive and the separate existence of TAC ceased, with Line Drive being the surviving organization and becoming our

wholly-owned subsidiary. Line Drive, which was wholly-owned by Gregory McCabe, owned certain assets and securities, including approximately 40.66% of 12,000 gross acres in the Hazel Project and 521,739 warrants to purchase our common stock (which warrants had been assigned by Mr. McCabe to Line Drive). Under the merger transaction, our shares of common stock of TAC converted into a membership interest of Line Drive, the membership interest in Line Drive held by Mr. McCabe immediately prior to the transaction ceased to exist, and we issued Mr. McCabe 3,301,739 restricted shares of common stock as consideration therefor. Immediately after closing, the 521,739 warrants held by Line Drive were cancelled, which warrants had an exercise price of \$1.40 per share and an expiration date of June 9, 2020. A Certificate of Merger for the merger transaction was filed with the Secretary of State of Texas on January 31, 2017.

Also on January 30, 2017, our wholly-owned subsidiary, Torchlight Energy, Inc., a Nevada corporation (“TEI”), entered into and closed a Purchase and Sale Agreement with Wolfbone Investments, LLC, a Texas limited liability company (“Wolfbone”) which is wholly-owned by Gregory McCabe. Under the agreement, TEI acquired certain of Wolfbone’s Hazel Project assets, including its interest in the Flying B Ranch #1 well and the 40 acre unit surrounding the well, for consideration of \$415,000, and additionally, Wolfbone caused to be cancelled a total of 2,780,000 warrants to purchase our common stock, including 1,500,000 warrants held by McCabe Petroleum Corporation, an entity owned by Mr. McCabe, and 1,280,000 warrants held by Green Hill Minerals, an entity owned by Mr. McCabe’s son, which warrant cancellations were effected through certain Warrant Cancellation Agreements. The 1,500,000 warrants held by McCabe Petroleum Corporation had an exercise price of \$1.00 per share and an expiration date of April 4, 2021. The warrants held by Green Hill Minerals included 100,000 warrants with an exercise price of \$1.73 and an expiration date of September 30, 2018 and 1,180,000 warrants with an exercise price of \$0.70 and an expiration date of February 15, 2020.



ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS - continued

On November 15, 2017, we and our wholly-owned subsidiary, Hudspeth Oil Corporation, a Texas corporation (“HOC”), entered into an Assignment of Farmout Agreement with Founders Oil & Gas, LLC (“Founders”) and Wolfbone Investments, LLC (“Wolfbone”), along with Pandora Energy, LP as a party to the agreement for limited purposes. Wolfbone is owned by our Chairman, Gregory McCabe. Under the agreement, Founders will assign to HOC and Wolfbone all its right, title and interest in the remaining leases under the original Farmout Agreement that Founders entered into with us on September 23, 2015; provided, however, that Founders will retain an undivided 9.5% of 8/8ths working interest and 9.5% of 75% of 8/8ths net revenue interest to the remaining leases, which retained interest will be carried by HOC and Wolfbone through the next \$40,500,000 in total costs. Accordingly, HOC and Wolfbone will each gain a 20.25% working interest in the remaining leases, bringing HOC’s total working interest to 67.75%. On behalf of HOC and Wolfbone, Founders (through its operating affiliate) will take such action necessary to spud the University Founders A 25 Well on or before December 1, 2017. After spudding of the well, Founders’ operating affiliate will remain operator of that well under the direction of us and Gregory McCabe.

On December 1, 2017, the transactions contemplated by the Agreement and Plan of Reorganization that we and our newly formed wholly-owned subsidiary, Torchlight Wolfbone Properties, Inc., a Texas corporation (“TWP”), entered into with McCabe Petroleum Corporation, a Texas corporation (“MPC”), and Warwink Properties, LLC, a Texas limited liability company (“Warwink Properties”) closed. Under the agreement, which was entered into on November 14, 2017, TWP merged with and into Warwink Properties and the separate existence of TWP ceased, with Warwink Properties becoming the surviving organization and our wholly-owned subsidiary. Warwink Properties was wholly owned by MPC which is wholly owned by Gregory McCabe, our Chairman. Warwink Properties owns certain assets, including a 10.71875% working interest in 640 acres in Winkler County, Texas. At closing of the merger transaction, our shares of common stock of TWP converted into a membership interest of Warwink Properties, the membership interest in Warwink Properties held by MPC ceased to exist, and we issued MPC 2,500,000 restricted shares of common stock as consideration. Also on December 1, 2017, MPC closed its transaction with MECO IV, LLC (“MECO”) for the purchase and sale of certain assets as contemplated by the Purchase and Sale Agreement dated November 9, 2017 (the “MECO PSA”), to which we are not a party. Under the MECO PSA, Warwink Properties received a carry from MECO (through the tanks) of up to \$1,475,000 in the next well drilled on the Winkler County leases. A Certificate of Merger for the merger transaction was filed with the Secretary of State of Texas on December 5, 2017.

Also on December 1, 2017, the transactions contemplated by the Purchase Agreement that our wholly-owned subsidiary, Torchlight Energy, Inc., a Nevada corporation (“TEI”), entered into with MPC closed. Under the Purchase Agreement, which was entered into on November 14, 2017, TEI acquired beneficial ownership of certain of MPC’s assets, including acreage and wellbores located in Ward County, Texas (the “Ward County Assets”). As consideration under the Purchase Agreement, at closing TEI issued to MPC an unsecured promissory note in the principal amount of \$3,250,000, payable in monthly installments of interest only beginning on January 1, 2018, at the rate of 5% per annum, with the entire principal amount together with all accrued interest due and payable on December 31, 2020. In connection with TEI’s acquisition of beneficial ownership in the Ward County Assets, MPC sold those same assets, on behalf of TEI, to MECO at closing of the MECO PSA, and accordingly, TEI received \$3,250,000 in cash for its beneficial interest in the Ward County Assets. Additionally, at closing of the MECO PSA, MPC paid TEI a performance fee of \$2,781,500 in cash as compensation for TEI’s marketing and selling the Winkler County assets of MPC and the Ward County Assets as a package to MECO.

Director Independence

We currently have four independent directors on our Board, Alexandre Zyngier, E. Scott Kimbrough, Michael Graves, and R. David Newton. The definition of “independent” used herein is based on the independence standards of The NASDAQ Stock Market LLC. The Board performed a review to determine the independence of these Directors and

made a subjective determination as to each of these directors that no transactions, relationships, or arrangements exist that, in the opinion of the Board, would interfere with the exercise of independent judgment in carrying out the responsibilities of a director of Torchlight Energy Resources, Inc. In making these determinations, the Board reviewed information provided by these directors with regard to each Director's business and personal activities as they may relate to us and our management.



## ITEM 14. PRINCIPAL ACCOUNTANT FEES AND SERVICES

The following table sets forth the fees paid or accrued by us for the audit and other services provided by our former auditor, Calvetti Ferguson, during the years ended December 31, 2017 and 2016 and Briggs & Veselka Co. who were engaged in 2017 for our year end December 31, 2017 audit.

|                       | 2017      | 2016      |
|-----------------------|-----------|-----------|
| Audit Fees(1)         | \$196,666 | \$73,968  |
| Audit Related Fees(2) | -         | 26,280    |
| Tax Fees(3)           | 65,888    | 22,035    |
| All Other Fees        | -         | 450       |
| Total Fees            | \$262,554 | \$122,733 |

(1) Audit Fees: This category represents the aggregate fees billed for professional services rendered by the principal independent accountant for the audit of our annual financial statements and review of financial statements included in our Form 10-K and services that are normally provided by the accountant in connection with statutory and regulatory filings or engagements for the fiscal years.

(2) Audit Related Fees: This category consists of the aggregate fees billed for assurance and related services by our independent consultant that are reasonably related to the performance of the audit or review of our financial statements and are not reported under "Audit Fees."

(3) Tax Fees: This category consists of the aggregate fees billed for professional services rendered by the principal independent consultant for tax compliance, tax advice, and tax planning.



PART IV

ITEM 15. EXHIBITS

| Exhibit No.  | Description                                                                                                                                                                                                         |
|--------------|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <u>2.1</u>   | <u>Share Exchange Agreement dated November 23, 2010. (Incorporated by reference from Form 8-K filed with the SEC on November 24, 2010.) *</u>                                                                       |
| <u>3.1</u>   | <u>Articles of Incorporation. (Incorporated by reference from Form S-1 filed with the SEC on May 2, 2008.) *</u>                                                                                                    |
| <u>3.2</u>   | <u>Certificate of Amendment to Articles of Incorporation dated December 10, 2014. (Incorporated by reference from Form 10-Q filed with the SEC on May 15, 2015.) *</u>                                              |
| <u>3.3</u>   | <u>Certificate of Amendment to Articles of Incorporation dated September 15, 2015. (Incorporated by reference from Form 10-Q filed with the SEC on November 12, 2015.) *</u>                                        |
| <u>3.4</u>   | <u>Amended and Restated Bylaws (Incorporated by reference from Form 8-K filed with the SEC on October 26, 2016.) *</u>                                                                                              |
| <u>10.1</u>  | <u>12% Series B Unsecured Convertible Promissory Note (form of) (Incorporated by reference from Form 10-Q filed with the SEC on August 14, 2015.) *</u>                                                             |
| <u>10.2</u>  | <u>Securities Purchase Agreement (for Series A Convertible Preferred Stock) (Incorporated by reference from Form 10-Q filed with the SEC on August 14, 2015.) *</u>                                                 |
| <u>10.3</u>  | <u>Employment Agreement (with John A. Brda) (Incorporated by reference from Form 8-K filed with the SEC on June 16, 2015.) *</u>                                                                                    |
| <u>10.4</u>  | <u>Employment Agreement (with Roger Wurtele) (Incorporated by reference from Form 8-K filed with the SEC on June 16, 2015.) *</u>                                                                                   |
| <u>10.5</u>  | <u>Loan documentation and warrants with Eunis L. Shockey (Incorporated by reference from Form 10-Q filed with the SEC on August 14, 2015.) *</u>                                                                    |
| <u>10.6</u>  | <u>Farmout Agreement between Hudspeth Oil Corporation, Founders Oil &amp; Gas, LLC and certain other parties (Incorporated by reference from Form 8-K filed with the SEC on September 29, 2015) *</u>               |
| <u>10.7</u>  | <u>Securities Purchase Agreement and Amendment to Securities Purchase Agreement (for Series B Convertible Preferred Stock) (Incorporated by reference from Form 10-Q filed with the SEC on November 12, 2015) *</u> |
| <u>10.8</u>  | <u>Purchase and Sale Agreement with Husky Ventures, Inc. (Incorporated by reference from Form 8-K filed with the SEC on November 12, 2015) *</u>                                                                    |
| <u>10.10</u> | <u>Purchase Agreement with McCabe Petroleum Corporation for acquisition of "Hazel Project" (Incorporated by reference from Form 10-Q filed with the SEC on August 15, 2016) *</u>                                   |

- 10.11 Resignation and Settlement Agreement with Willard G. McAndrew (Incorporated by reference from Form 10-Q filed with the SEC on November 10, 2016) \*
- 10.12 Agreement and Plan of Reorganization and Plan of Merger with Line Drive Energy, LLC (Incorporated by reference from Form 10-K filed with the SEC on March 31, 2017) \*
- 10.13 Purchase and Sale Agreement with Wolfbone Investments, LLC (Incorporated by reference from Form 10-K filed with the SEC on March 31, 2017) \*
- 10.14 12% 2020 Senior Unsecured Promissory Note (form of) (Incorporated by reference from Form 10-Q filed with the SEC on May 12, 2017) \*
- 10.15 Agreement and Plan of Reorganization and Plan of Merger with McCabe Petroleum Corporation and Warwink Properties, LLC



ITEM 15. EXHIBITS - continued

10.16 Purchase Agreement with Torchlight Energy, Inc. and McCabe Petroleum Corporation

10.17 Promissory Note for \$3,250,000 by Torchlight Energy, Inc. to McCabe Petroleum Corporation

10.18 Assignment of Farmout Agreement between Hudspeth Oil Corporation, Founders Oil & Gas, LLC and Wolfbone Investments, LLC

10.19 12% 2020 Senior Unsecured Promissory Note for \$4,500,000 with David A. Straz, Jr Revocable Trust of 1986

14.1 Code of Ethics (Incorporated by reference from Form S-1 filed with the SEC on May 2, 2008.) \*

16.01 Letter from Calvetti Ferguson to the Securities and Exchange Commission (Incorporated by reference from Form 8-K filed with the SEC on December 19, 2016) \*

21.1 Subsidiaries

23.1 Consent of Briggs & Veselka Co.

23.2 Consent of PeTech Enterprises, Inc.

31.1 Certification of principal executive officer required by Rule 13a – 14(1) or Rule 15d – 14(a) of the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

31.2 Certification of principal financial officer required by Rule 13a – 14(1) or Rule 15d – 14(a) of the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

32.1 Certification of principal executive officer and principal financial officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 and Section 1350 of 18 U.S.C. 63.

99.1 Report of PeTech Enterprises, Inc.

101.INS XBRL Instance Document

101.SCH XBRL Taxonomy Extension Schema

101.CAL XBRL Taxonomy Extension Calculation Linkbase

101.DEF XBRL Taxonomy Extension Definitions Linkbase

101.LAB XBRL Taxonomy Extension Label Linkbase

101.PRE XBRL Taxonomy Extension Presentation Linkbase

\* Incorporated by reference from our previous filings with the SEC



## SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

Torchlight Energy Resources, Inc.

/s/ John A. Brda  
By: John A. Brda  
Chief Executive Officer

Date: March 16, 2018

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated:

| Signature                                    | Title                                                      | Date           |
|----------------------------------------------|------------------------------------------------------------|----------------|
| /s/ John A. Brda<br>John A. Brda             | Director, Chief Executive Officer, President and Secretary | March 16, 2018 |
| /s/ Gregory McCabe<br>Gregory McCabe         | Director (Chairman of the Board)                           | March 16, 2018 |
| /s/ Roger N. Wurtele<br>Roger N. Wurtele     | Chief Financial Officer and Principal Accounting Officer   | March 16, 2018 |
| /s/ E. Scott Kimbrough<br>E. Scott Kimbrough | Director                                                   | March 16, 2018 |
| /s/ R. David Newton<br>R. David Newton       | Director                                                   | March 16, 2018 |
| /s/ Alexandre Zyngier<br>Alexandre Zyngier   | Director                                                   | March 16, 2018 |
| /s/ Michael J. Graves<br>Michael J. Graves   | Director                                                   | March 16, 2018 |

