

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

(Mark One)

Quarterly report under Section 13 or 15(d) of the Securities Exchange Act of 1934
For the Quarter Ended September 30, 2020

Transition report under Section 13 or 15(d) of the Securities Exchange Act of 1934
For the transition period from _____ to _____.

Commission file number: 001-36247

TORCHLIGHT ENERGY RESOURCES, INC.

(Name of registrant in its charter)

Nevada

(State or Other Jurisdiction of Incorporation or Organization)

74-3237581

(I.R.S. Employer Identification No.)

5700 West Plano Pkwy, 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 Act:

<u>Title of each class</u>	<u>Trading Symbol(s)</u>	<u>Name of each exchange on which registered</u>
Common Stock, \$0.001 par value	TRCH	The Nasdaq Stock Market LLC

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 every Interactive Data File required to be submitted 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 such files). Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or an emerging growth company. Large accelerated filer Accelerated Filer Non-accelerated filer 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

As of November 9, 2020, there were 99,327,673 shares of the registrant's common stock outstanding (the only class of voting common stock).

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NOTE ABOUT FORWARD-LOOKING STATEMENTS

This Quarterly Report on Form 10-Q 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, Item 2 “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,” “will 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 report and in our Annual Report on Form 10-K for the year ended December 31, 2019 and in particular, the risks discussed in our Form 10-K under the caption “Risk Factors” in Item 1A therein, 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 our ability to extend or restructure existing debt, to obtain additional capital in the future to repay outstanding debt and fund planned expansion, the demand for oil and natural gas which demand could be materially affected by the economic impacts of COVID-19 and possible increases in supply from Russia and OPEC, the proposed business combination transaction with Metamaterial, Inc., general economic factors, competition in the industry, our ability to regain and maintain compliance with the minimum bid price requirement of the Nasdaq Stock Market 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.

PART I FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

TORCHLIGHT ENERGY RESOURCES, INC.
CONSOLIDATED BALANCE SHEETS (Unaudited)

	September 30, 2020	December 31, 2019
ASSETS		
Current assets:		
Cash	\$ 258,803	\$ 89,730
Restricted cash	500,000	-
Accounts receivable	268,458	199,462
Production revenue receivable	73,464	100,546
Subscription receivable	-	250,000
Prepayments - development costs	750,000	-
Prepaid expenses	153,062	96,006
Total current assets	2,003,787	735,744
Oil and gas properties, net	33,463,330	40,182,043
Convertible note receivable	501,096	-
Office equipment, net	4,905	6,348
TOTAL ASSETS	\$ 35,973,118	\$ 40,924,135
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	\$ 819,458	\$ 1,444,002
12% 2021 Secured promissory notes, net of \$132,192 and \$-0- of discount and financing costs, respectively	12,367,808	-
6% 2021 Secured convertible promissory note due to related party	1,500,000	-
12% 2020 Unsecured promissory notes, net of \$-0- and \$127,170 of discount and financing costs, respectively	-	8,437,127
8% 2021 Convertible promissory notes payable, net of \$733,257 of discount and BCF	1,226,743	-
10% 2020 Convertible promissory notes payable	540,000	540,000
14% 2020 Convertible promissory notes payable	-	2,000,000
PPP note payable	77,477	-
Accrued payroll	1,131,176	996,176
Related party payables	45,000	45,000
Due to working interest owners	54,320	54,320
Accrued interest payable	501,171	445,861
Total current liabilities	18,263,153	13,962,486
12% 2021 Unsecured promissory notes, net of \$-0- and \$59,297 of discount and financing costs, respectively	-	3,940,703
8% 2021 Convertible promissory notes payable, net of \$1,186,029 of discount and BCF	-	773,971
14% 2021 Convertible promissory notes payable, net of \$26,915 of financing costs	1,973,085	-
Convertible notes payable and accrued interest	-	7,157,260
Asset retirement obligations	23,745	23,319
Total liabilities	20,259,983	25,857,739
Commitments and contingencies		
Stockholders' equity:		
Preferred stock, par value \$0.001, 10,000,000 shares authorized; -0- issued and outstanding September 30, 2020 and December 31, 2019	-	-
Common stock, par value \$0.001; 150,000,000 shares authorized; 99,432,298 issued and outstanding at September 30, 2020; 76,222,042 issued and outstanding at December 31, 2019	99,438	76,225
Additional paid-in capital	122,645,462	114,143,872
Accumulated deficit	(107,031,765)	(99,153,701)
Total stockholders' equity	15,713,135	15,066,396
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	\$ 35,973,118	\$ 40,924,135

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

TORCHLIGHT ENERGY RESOURCES, INC.
CONSOLIDATED STATEMENTS OF OPERATIONS (Unaudited)

	Three Months Ended September 30, 2020	Three Months Ended September 30, 2019	Nine Months Ended September 30, 2020	Nine Months Ended September 30, 2019
Oil and gas sales	\$ 61,722	\$ 71,142	\$ 191,819	\$ 619,054
Cost of revenues	<u>(23,644)</u>	<u>(117,104)</u>	<u>(171,664)</u>	<u>(358,424)</u>
Gross profit	<u>38,078</u>	<u>(45,962)</u>	<u>20,155</u>	<u>260,630</u>
Operating expenses:				
General and administrative	590,369	849,425	2,244,804	2,557,343
Depreciation, depletion and amortization	77,118	27,355	802,316	355,050
Loss on extinguishment of debt	-	-	1,829,651	-
Impairment loss	-	-	2,108,301	474,357
Total operating expenses	<u>667,487</u>	<u>876,780</u>	<u>6,985,072</u>	<u>3,386,750</u>
Other income (expense)				
Interest expense and accretion of note discounts	(256,636)	(328,895)	(914,243)	(694,077)
Interest income	1,096	-	1,096	52
Total (expense), net	<u>(255,540)</u>	<u>(328,895)</u>	<u>(913,147)</u>	<u>(694,025)</u>
Loss before income taxes	(884,949)	(1,251,637)	(7,878,064)	(3,820,145)
Provision for income taxes	-	-	-	-
Net loss	<u>\$ (884,949)</u>	<u>\$ (1,251,637)</u>	<u>\$ (7,878,064)</u>	<u>\$ (3,820,145)</u>
Loss per common share:				
Basic and Diluted	<u>\$ (0.01)</u>	<u>\$ (0.02)</u>	<u>\$ (0.09)</u>	<u>\$ (0.05)</u>
Weighted average number of common shares outstanding:				
Basic and Diluted	<u>98,242,340</u>	<u>73,930,596</u>	<u>87,926,086</u>	<u>72,350,083</u>

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

TORCHLIGHT ENERGY RESOURCES, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited)

	Nine Months Ended September 30, 2020	Nine Months Ended September 30, 2019
Cash Flows From Operating Activities		
Net loss	\$ (7,878,064)	\$ (3,820,145)
Adjustments to reconcile net loss to net cash from operations:		
Stock based compensation	395,150	854,720
Stock issued for interest payments on notes payable	-	497,817
Accrued interest payable in stock	60,801	163,168
Amortization of debt issuance costs	230,755	214,939
Accretion of note discounts	82,605	274,217
Amortization of beneficial conversion on convertible notes	452,772	-
Depreciation, depletion and amortization	802,316	355,050
Loss on extinguishment of debt	1,829,651	-
Impairment loss	2,108,301	474,357
Change in:		
Accounts receivable	(68,996)	(56,456)
Production revenue receivable	27,082	247,123
Prepayments - development costs	-	144,641
Prepaid expenses	(57,056)	(106,265)
Accounts payable and accrued expenses	226,820	89,119
Accrued interest payable	483,554	489,127
Net cash from operating activities	<u>(1,304,309)</u>	<u>(178,588)</u>
Cash Flows From Investing Activities		
Investment in oil and gas properties	(5,570,495)	(6,606,279)
Purchase of property, plant, and equipment	-	(6,564)
Net cash from investing activities	<u>(5,570,495)</u>	<u>(6,612,843)</u>
Cash Flows From Financing Activities		
Issuance of common stock, net of offering costs	6,466,400	2,516,880
Proceeds from stock subscription receivable	250,000	-
Proceeds from notes payable	1,077,477	4,010,000
Payment for extension of debt maturity	(250,000)	-
Proceeds from exercise of warrants into common stock	-	184,843
Net cash from financing activities	<u>7,543,877</u>	<u>6,711,723</u>
Net increase (decrease) in cash and restricted cash	669,073	(79,708)
Cash and restricted cash - beginning of period	89,730	840,163
Cash and restricted cash - end of period	<u>\$ 758,803</u>	<u>\$ 760,455</u>
Supplemental disclosure of cash flow information:		
Cash paid for interest	\$ 1,344,469	\$ 1,131,819
Cash paid for state franchise tax	\$ 100	\$ 4,442
Supplemental disclosure of non-cash investing and financing activities:		
Debt converted by transfer of working interest	\$ 7,330,849	\$ -
Common stock issued for prepayment of development costs	\$ 750,000	\$ -
Common stock issued for payment in kind on notes payable	\$ 314,107	\$ 314,107
Common stock issued for note principal and interest conversion	\$ 65,646	\$ 50,000
Common stock issued for note extension	\$ 16,000	\$ -
Increase (decrease) in accounts payable for property development costs	\$ (531,864)	\$ 225,536
Beneficial conversion feature on convertible notes	\$ -	\$ 1,145,546
Debt discount from fair value of warrants with convertible notes	\$ -	\$ 240,455
Note receivable from third party	\$ 500,000	\$ -
Account payable relieved in transfer of oil and gas properties	\$ 7,000	\$ -
Common stock issued for lease interests	\$ -	\$ 125,000

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

TORCHLIGHT ENERGY RESOURCES, INC.
CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY (Unaudited)

	Common stock shares	Common stock amount	Additional paid-in capital	Accumulated deficit	Total
Balance, December 31, 2019	<u>76,222,042</u>	<u>\$ 76,225</u>	<u>\$ 114,143,872</u>	<u>\$ (99,153,701)</u>	<u>\$ 15,066,396</u>
Issuance of common stock for services	125,000	125	86,125	-	86,250
Issuance of common stock to a vendor for delay in payment	40,000	40	25,960	-	26,000
Issuance of common stock for cash, less underwriting/offering costs	3,885,715	3,886	2,353,232	-	2,357,118
Warrants issued in conversion of notes payable	-	-	382,500	-	382,500
Warrants issued for services	-	-	98,900	-	98,900
Stock options issued for services	-	-	19,500	-	19,500
Net loss	-	-	-	(3,693,863)	(3,693,863)
Balance, March 31, 2020	<u>80,272,757</u>	<u>\$ 80,276</u>	<u>\$ 117,110,089</u>	<u>\$ (102,847,564)</u>	<u>\$ 14,342,801</u>
Issuance of common stock for services	142,857	143	59,857	-	60,000
Issuance of common stock for cash, less underwriting/offering costs	11,344,737	11,345	2,767,856	-	2,779,201
Warrants issued in connection with common stock offerings	-	-	891,112	-	891,112
Issuance of common stock for promissory note extension	40,000	40	15,960	-	16,000
Common stock issued in payment of accounts payable	357,143	357	134,643	-	135,000
Issuance of common stock for payment in kind on notes payable	680,376	680	313,427	-	314,107
Issuance of common stock for prepayment of development costs	1,630,434	1,630	748,370	-	750,000
Stock options issued for services	-	-	19,500	-	19,500
Net loss	-	-	-	(3,299,252)	(3,299,252)
Balance, June 30, 2020	<u>94,468,304</u>	<u>\$ 94,471</u>	<u>\$ 122,060,814</u>	<u>\$ (106,146,816)</u>	<u>\$ 16,008,469</u>
Issuance of common stock for services	50,000	50	15,450	-	15,500
Issuance of common stock for cash, less underwriting/offering costs	1,557,173	1,557	437,412	-	438,969
Common stock issued in warrant exercise	3,157,895	3,158	(3,158)	-	-
Common stock issued in note principal and interest conversion	198,926	202	65,444	-	65,646
Warrants issued for services	-	-	50,000	-	50,000
Stock options issued for services	-	-	19,500	-	19,500
Net loss	-	-	-	(884,949)	(884,949)
Balance, September 30, 2020	<u>99,432,298</u>	<u>\$ 99,438</u>	<u>\$ 122,645,462</u>	<u>\$ (107,031,765)</u>	<u>\$ 15,713,135</u>

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

TORCHLIGHT ENERGY RESOURCES, INC.
CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY (Unaudited) (Continued)

	Common stock shares	Common stock amount	Additional paid-in capital	Accumulated deficit	Total
Balance, December 31, 2018	70,112,376	\$ 70,116	\$ 107,266,965	\$ (89,314,305)	\$ 18,022,776
Issuance of common stock for services	92,593	92	99,908	-	100,000
Issuance of common stock for cash	1,592,600	1,593	1,272,487	-	1,274,080
Issuance of common stock for interest	13,546	13	14,615	-	14,628
Issuance of common stock for warrant exercise	100,000	100	76,900	-	77,000
Warrants issued for services	-	-	186,000	-	186,000
Stock options issued for services	-	-	111,250	-	111,250
Net loss	-	-	-	(1,677,874)	(1,677,874)
Balance, March 31, 2019	<u>71,911,115</u>	<u>\$ 71,914</u>	<u>\$ 109,028,125</u>	<u>\$ (90,992,179)</u>	<u>\$ 18,107,860</u>
Issuance of common stock for services	100,000	\$ 100	\$ 148,900	-	\$ 149,000
Issuance of common stock for cash	695,000	\$ 695	\$ 555,305	-	\$ 556,000
Issuance of common stock for oil and gas lease extension	100,000	\$ 100	\$ 124,900	-	\$ 125,000
Issuance of common stock for interest	46,796	\$ 48	\$ 50,492	-	\$ 50,540
Issuance of common stock for note payment in kind	202,316	\$ 202	\$ 313,906	-	\$ 314,108
Issuance of common stock for option/warrant exercise	68,690	\$ 68	\$ 107,775	-	\$ 107,843
Warrants issued for services	-	-	\$ 87,000	-	\$ 87,000
Stock options issued for services	-	-	\$ 25,000	-	\$ 25,000
Net loss	-	-	-	(890,634)	\$ (890,634)
Balance, June 30, 2019	<u>73,123,917</u>	<u>\$ 73,127</u>	<u>\$ 110,441,403</u>	<u>\$ (91,882,813)</u>	<u>\$ 18,631,717</u>
Issuance of common stock for services	120,000	120	116,280	-	116,400
Issuance of common stock for cash	858,500	858	685,942	-	686,800
Issuance of common stock for interest	107,503	108	118,438	-	118,546
Warrants issued for services	-	-	67,570	-	67,570
Beneficial conversion feature on convertible notes	-	-	1,145,546	-	1,145,546
Debt discount from fair value of warrants issued with convertible notes	-	-	240,455	-	240,455
Issuance of common stock for convertible note conversion	45,455	45	49,955	-	50,000
Stock options issued for services	-	-	12,500	-	12,500
Net loss	-	-	-	(1,251,637)	(1,251,637)
Balance, September 30, 2019	<u>74,255,375</u>	<u>\$ 74,258</u>	<u>\$ 112,878,089</u>	<u>\$ (93,134,450)</u>	<u>\$ 19,817,897</u>

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

TORCHLIGHT ENERGY RESOURCES, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

1. NATURE OF BUSINESS

Torchlight Energy Resources, Inc. 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.

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, Hudspeth Oil Corporation, Torchlight Hazel LLC, and Warwink Properties LLC.

2. GOING CONCERN

At September 30, 2020, the Company had not yet achieved profitable operations. We had a net loss of \$7,878,064 for the nine months ended September 30, 2020 and had accumulated losses of \$107,031,765 since our inception. We expect to incur further losses in the development of our business. The Company had a working capital deficit as of September 30, 2020 of \$16,259,366. 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, institutional, or public 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.

These interim financial statements are unaudited and have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission (“SEC”) regarding interim financial reporting. Certain disclosures have been condensed or omitted from these financial statements. Accordingly, they do not include all the information and notes required by accounting principles generally accepted in the United States of America (“GAAP”) for complete consolidated financial statements, and should be read in conjunction with the audited consolidated financial statements and notes thereto included in our Annual Report on Form 10-K for the year ended December 31, 2019.

In the opinion of management, the accompanying unaudited financial condensed consolidated financial statements include all adjustments, consisting of normal recurring adjustments, necessary to fairly present the financial position as of, and the results of operations for, all periods presented. In preparing the accompanying financial statements, management has made certain estimates and assumptions that affect reported amounts in the condensed financial statements and disclosures of contingencies. Actual results may differ from those estimates. The results for interim periods are not necessarily indicative of annual results. Certain reclassifications have been made to the prior period’s consolidated financial statements and related footnotes to conform them to the current period presentation.

TORCHLIGHT ENERGY RESOURCES, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

3. SIGNIFICANT ACCOUNTING POLICIES - continued

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, convertible note receivable, 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. The recorded value of the Company’s convertible note receivable reflects the amount which management believes approximates fair value.

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. Restricted cash consists of funds held in legal escrow at September 30, 2020. (See Note 9)

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 September 30, 2020 and December 31, 2019, no valuation allowance was considered necessary.

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.

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.

3. SIGNIFICANT ACCOUNTING POLICIES - *continued*

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 nine months ended September 30, 2020 and 2019, the Company capitalized \$1,773,658 and \$2,084,026, 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 realizable 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 Company recorded an impairment expense of \$2,108,301 and \$474,357 for the nine months ended September 30, 2020 and 2019, respectively, to recognize the adjustment required by the ceiling test.

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.

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.

TORCHLIGHT ENERGY RESOURCES, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

3. SIGNIFICANT ACCOUNTING POLICIES - continued

Estimated interest and penalties related to potential underpayment on any unrecognized tax benefits are classified as a component of tax expense in the statements 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.

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.

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

Revenue recognition – The Company’s revenue is typically generated from contracts to sell natural gas, crude oil or NGLs produced from interests in oil and gas properties owned by the Company. Contracts for the sale of natural gas and crude oil are evidenced by (1) base contracts for the sale and purchase of natural gas or crude oil, which document the general terms and conditions for the sale, and (2) transaction confirmations, which document the terms of each specific sale. The transaction confirmations specify a delivery point which represents the point at which control of the product is transferred to the customer. These contracts frequently meet the definition of a derivative under ASC 815, and are accounted for as derivatives unless the Company elects to treat them as normal sales as permitted under that guidance. The Company elects to treat contracts to sell oil and gas production as normal sales, which are then accounted for as contracts with customers. The Company has determined that these contracts represent multiple performance obligations which are satisfied when control of the commodity transfers to the customer, typically through the delivery of the specified commodity to a designated delivery point.

Revenues from oil and gas sales are detailed as follows:

	Three Months Ended <u>September 30, 2020</u>	Three Months Ended <u>September 30, 2019</u>	Nine Months Ended <u>September 30, 2020</u>	Nine Months Ended <u>September 30, 2019</u>
Revenues				
Oil sales	\$ 59,858	\$ 71,064	\$ 186,968	\$ 596,247
Gas sales	1,864	78	4,851	22,807
Total	<u>\$ 61,722</u>	<u>\$ 71,142</u>	<u>\$ 191,819</u>	<u>\$ 619,054</u>

Revenue is measured based on consideration specified in the contract with the customer, and excludes any amounts collected on behalf of third parties. The Company recognizes revenue in the amount that reflects the consideration it expects to be entitled to in exchange for transferring control of those goods to the customer. Amounts allocated in the Company’s price contracts are based on the standalone selling price of those products in the context of long-term contracts. Payment is generally received one or two months after the sale has occurred.

TORCHLIGHT ENERGY RESOURCES, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

3. SIGNIFICANT ACCOUNTING POLICIES - continued

Gain or loss on derivative instruments is outside the scope of ASC 606 and is not considered revenue from contracts with customers subject to ASC 606. The Company may in the future use financial or physical contracts accounted for as derivatives as economic hedges to manage price risk associated with normal sales, or in limited cases may use them for contracts the Company intends to physically settle but do not meet all of the criteria to be treated as normal sales.

Producer Gas Imbalances. The Company applies the sales method of accounting for natural gas revenue. Under this method, revenues are recognized based on the actual volume of natural gas sold to purchasers.

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 11,027,390 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. The Company accrued no liability as of September 30, 2020 and December 31, 2019.

Recent adopted accounting pronouncements – 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 was effective for the Company in the first quarter of 2019. The Company adopted the change which did not have a material impact on its consolidated financial statements.

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 November 9, 2020, 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 September 30, 2020 and December 31, 2019:

	<u>September 30, 2020</u>	<u>December 31, 2019</u>
Evaluated costs subject to amortization	\$ 16,092,416	\$ 13,243,541
Unevaluated costs	33,009,327	39,667,740
Total capitalized costs	49,101,743	52,911,281
Less accumulated depreciation, depletion and amortization	(15,638,413)	(12,729,238)
Total oil and gas properties	<u>\$ 33,463,330</u>	<u>\$ 40,182,043</u>

Unevaluated costs as of September 30, 2020 include cumulative costs on developing projects including the Orogrande, Hazel, and Winkler projects in West Texas.

The Company periodically adjusts for the separation of evaluated versus unevaluated costs within its full cost pool to recognize the value impairment related to the expiration of, or changes in market value, of unevaluated leases. The impact of reclassifications as they become necessary is to increase the basis for calculation of future period's depletion, depreciation and amortization which effectively recognizes the impairment on the consolidated statement of operations over future periods. Reclassified costs also become evaluated costs for purposes of ceiling tests and which may cause recognition of increased impairment expense in future periods. The cumulative unevaluated costs which have been reclassified within our full cost pool totals \$5,881,635 as of September 30, 2020.

4. OIL & 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.

Current Projects

We are an energy company engaged in the acquisition, exploration, exploitation and/or development of oil and natural gas properties in the United States. We are primarily focused on the acquisition of early stage projects, the development and delineation of these projects, and then the monetization of those assets once these activities are completed.

Since 2010, our primary focus has been the development of interests in oil and gas projects we hold in the Permian Basin in West Texas. We also hold minor interests in certain other oil and gas projects in Central Oklahoma that we are in the process of divesting.

As of September 30, 2020, we 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 Winkler Project in Winkler County, Texas and the wells 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 Gregory McCabe, our Chairman. Mr. McCabe was the sole owner of both Hudspeth and MPC. Under the terms and conditions of the Purchase Agreement, we purchased 100% of the capital stock of Hudspeth which held certain oil and gas assets, including a 100% working interest in approximately 172,000 predominately contiguous acres in the Orogrande Basin in West Texas. 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 among Hudspeth, MPC and Mr. McCabe. Mr. McCabe also holds a 4.5% overriding royalty interest in the Orogrande acreage, which he obtained prior to, and was not a part of the August 2014 transaction. As of September 30, 2020, leases covering approximately 134,000 acres remain in effect.

We believe all drilling obligations through September 30, 2020 have been met.

On September 23, 2015, Hudspeth entered into a Farmout Agreement with Pandora Energy, LP (“Pandora”), Founders Oil & Gas, LLC (“Founders”), and for the limited purposes set forth therein, MPC and Mr. McCabe, for the entire Orogrande Project in Hudspeth County, Texas. The Farmout Agreement provided that Hudspeth and Pandora (collectively referred to as “Farmor”) would assign to Founders an undivided 50% of the leasehold interest and a 37.5% net revenue interest in the oil and gas leases and mineral interests in the Orogrande Project, which interests, except for any interests retained by Founders, would be reassigned to Farmor by Founders if Founders did not spend a minimum of \$45.0 million on actual drilling operations on the Orogrande Project by September 23, 2017. Under a joint operating agreement also entered into on September 23, 2015, Founders was designated as operator of the leases.

Effective March 27, 2017 the property became subject to a DDU Agreement which allows for all 192 existing leases covering approximately 134,000 net acres leased from University Lands to be combined into one drilling and development unit for development purposes. The term of the DDU Agreement expires on December 31, 2023, and the time to drill on the drilling and development unit continues through December 2023. The DDU Agreement also grants the right to extend the DDU Agreement through December 2028 if compliance with the DDU Agreement is met and the extension fee associated with the additional time is paid.

Our drilling obligations include four wells in year 2020 and five wells per year in years 2021, 2022 and 2023. We have received a waiver of the requirement to develop four wells in 2020. The drilling obligations are minimum yearly requirements and may be exceeded if acceleration is desired.

During 2017, we assumed operational control from Founders Oil and Gas Operating LLC on the Orogrande Project. We were joined by Wolfbone Investments, LLC, (“Wolfbone”), a company owned by Mr. McCabe. We, along with Hudspeth, Wolfbone and, for the limited purposes set forth therein, Pandora, entered into an Assignment of Farmout Agreement with Founders, (the “Assignment of Farmout Agreement”), pursuant to which we and Wolfbone will share the remaining commitments under the Farmout Agreement. All original provisions of our carried interest were to remain in place including reimbursement to us on each wellbore. Founders was to remain a 9.5% working interest owner in the Orogrande Project for the \$9.5 million it had spent as of the date of the Assignment of Farmout Agreement, and such interests were to be carried until \$40.5 million is spent by Wolfbone and us, with each contributing 50% of such capital spend, under the existing agreement.

TORCHLIGHT ENERGY RESOURCES, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

4. OIL & GAS PROPERTIES - continued

Our working interest in the Orogrande Project thereby increased by 20.25% to a total of 67.75% and Wolfbone then owned 20.25%.

On July 25, 2018, we and Hudspeth entered into a Settlement & Purchase Agreement (the "Settlement Agreement") with Founders (and Founders Oil & Gas Operating, LLC), Wolfbone and MPC, which agreement provides for Founders assigning all of its working interest in the oil and gas leases of the Orogrande Project to Hudspeth and Wolfbone equally. Future well capital spending obligations remained the same 50% contribution from Hudspeth and 50% from Wolfbone until such time as the \$40.5 million to be spent on the project. The Company estimates that there is still approximately \$9.0 million remaining to be spent on the project until such time as the capital expenditures revert back to the percentages of the working interest owners.

After the assignment by Founders, Hudspeth's working interest increased to 72.5%.

The Company has drilled eight test wells in the Orogrande in order to stay in compliance with University Lands D&D Unit Agreement, as well as, to test for potential shallow pay zones and deeper pay zones that may be present on structural plays. Development of the wells continued into the nine months ended September 30, 2020 to further capture and document the scientific base in support of demonstrating the production potential of the property. The Company is currently marketing the project for an outright sale or farm in partner. This marketing process has been long and arduous as the overall market is quite soft. Due to the size and scope of the project, we are dealing with very large companies that have multitudes of people reviewing our material, which in itself is extensive. During the marketing process, the Company and Wolfbone will endeavor to complete the University Maverick A24 #1 as a potential producer in the Atoka formation. Should a farm out partner or sale not occur, the Company and Wolfbone will continue to drill additional wells in the play in order to fulfill the obligations under the DDU Agreement

Rich Masterson, our consulting geologist, is credited with originating the Orogrande Project in Hudspeth County in the Orogrande Basin. With Mr. Masterson's assistance and based on all the science we have gathered to date, we have identified multiple unconventional and conventional target pay zones with depths between 3,000' and 8,000' with primary pay, described as the Penn formation, located at depths of 5,300 to 5,900'. Based on our geologic analysis to date, this basin has stacked pay with zones including the Wolfcamp, Penn, Barnett, Woodford, Atoka and more. These potential zones are prospective for oil and gas with a GOR of 1100 expected based on our gathered scientific information and analysis from independent third parties.

On March 9, 2020, holders of notes payable by the Company entered into a Conversion Agreement under which the noteholders elected to convert principal of \$6,000,000 and approximately \$1,331,000 of accrued interest on the notes, in accordance with their terms, into an aggregate 6% working interest (of all such holders) in the Orogrande Project.

The Orogrande Project ownership as of September 30, 2020 is detailed as follows:

	Revenue Interest	Working Interest
University Lands - Mineral Owner	20.000%	n/a
ORRI - Magdalena Royalties, LLC, an entity controlled by Gregory McCabe, Chairman	4.500%	n/a
ORRI - Unrelated Party	0.500%	n/a
Hudspeth Oil Corporation, a subsidiary of Torchlight Energy Resources Inc.	49.875%	66.500%
Wolfbone Investments LLC, an entity controlled by Gregory McCabe, Chairman	18.750%	25.000%
Conversion by Note Holders in March, 2020	4.500%	6.000%
Unrelated Party	1.875%	2.500%
	<u>100.000%</u>	<u>100.000%</u>

TORCHLIGHT ENERGY RESOURCES, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

4. OIL & GAS PROPERTIES - continued

Hazel Project in the Midland Basin in West Texas

Effective April 4, 2016, TEI acquired from MPC a 66.66% working interest in approximately 12,000 acres in the Midland Basin. A back-in after payout of a 25% working interest was retained by MPC and another unrelated working interest owner.

In October 2016, the holders of all of our then-outstanding shares of Series C Preferred Stock (which were issued in July 2016) elected to convert into a total 33.33% working interest in our Hazel Project, reducing our ownership from 66.66% to a 33.33% working interest.

The Company has drilled six test wells on the Hazel Project to capture and document the scientific base in support of demonstrating the production potential of the property.

Acquisition of Additional Interests in Hazel Project

On January 30, 2017, we entered into and closed an Agreement and Plan of Reorganization and a Plan of Merger with an entity which was wholly-owned by Mr. McCabe, which resulted in the acquisition of approximately 40.66% working interest in the 12,000 gross acres, 9,600 net acres, in the Hazel Project.

Also on January 30, 2017, TEI entered into and closed a Purchase and Sale Agreement with Wolfbone. 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.

Upon the closing of the transactions, our working interest in the Hazel Project increased by 40.66% to a total ownership of 74%.

Effective June 1, 2017, we acquired an additional 6% working interest from unrelated working interest owners increasing our working interest in the Hazel project to 80%, and an overall net revenue interest of 74-75%.

Mr. Masterson, who assisted with development in our Orogrande project, is also credited with originating the Hazel Project in the Midland Basin.

We were required to drill one well every six months to hold the entire 12,000 acre block for eighteen months until to November 22, 2018, and thereafter two wells every six months. During 2019 and the nine months ended September 30, 2020 modifications were completed to mineral owner leases as described below.

Lease Modifications

In May 2019 we entered into agreements with two of the three mineral owners on the northern section of the leases to keep the entire acreage block as one lease with a one year extension. We issued each of them 50,000 shares of our common stock as consideration for this extension. As of September 30, 2020 we have structured the extension agreement retroactively with the third mineral owner for cash consideration. Due to this extension, our obligation for 2019 reduced to one obligation well. We finished that obligation well targeting a shallow zone that showed oil potential. For the remainder of 2020 the Company must drill one well in June and two wells by the December 31, 2020. Development of the June well was initiated during June, 2020. The December obligation was met under the terms of the Option Agreement. See below.

In April 2018, we announced that we have commenced a process that could result in the monetization of the Hazel Project. We believed the development activity at the Hazel Project, coupled with nearby activities of other oil and gas operators, suggested that this project has achieved a level of value worth monetizing. We anticipate that the liquidity that would be provided from selling the Hazel Project would be used to retire debt with any remainder redeployed into the Orogrande Project.

Option Agreement with Masterson Hazel Partners, LP

On August 13, 2020, our subsidiaries Torchlight Energy, Inc. and Torchlight Hazel, LLC (collectively, "Torchlight") entered into an option agreement (the "Option Agreement") with Masterson Hazel Partners, LP ("MHP") and McCabe Petroleum Corporation. Under the agreement, MHP is obligated to drill and complete, or cause to be drilled and completed, at its sole cost and expense, a new lateral well (the "Well") on our Hazel Project, sufficient to satisfy Torchlight's continuous development obligations on the southern half of the prospect no later than September 30, 2020. MHP paid to Torchlight \$1,000 as an option fee at the time of execution of the Option Agreement. If MHP fails to meet the September 30, 2020 deadline, then the options granted pursuant to the Option Agreement will automatically terminate, and Torchlight will retain the \$1,000 option fee as its sole remedy. MHP is entitled to receive, as its sole recourse for the recoupment of drilling costs, the revenue from production of the Well attributable to Torchlight's interest until such time as it has recovered its reasonable costs and expenses for drilling, completing, and operating the well.

In exchange for MHP satisfying the above drilling obligations, Torchlight granted to MHP the exclusive right and option to perform operations, at MHP's sole cost and expense, on the Hazel Project sufficient to satisfy Torchlight's continuous development obligations on the northern half of the prospect. In the event that MHP exercises this drilling option and satisfies the continuous development obligations on the northern half of the prospect, then MHP will have the option to purchase the entire Hazel Project by March 31, 2021, under the terms of the form of Purchase and Sale Agreement included as an exhibit to the Option Agreement, at an aggregate purchase price of \$12,690,704 for approximately 9,762.08 net mineral acres, and not less than 74% net revenue interest (approximately \$1,300 per net mineral acre).

MHP must exercise the above options no later than December 1, 2020, subject to extension to March 11, 2021 if MHP drills the Well on the southern half of the prospect, provides notice no later than December 1, 2020 of its intent to conduct operations on the northern half of the prospect and on or before December 15, 2020, conducts operations sufficient to satisfy the drilling obligations regarding the second well on the northern half of the prospect.

In the event MHP exercises its option to purchase the entire Hazel Project, McCabe Petroleum Corporation, which is owned by our chairman Gregory McCabe, has agreed to reduce its reversionary interest in the Hazel Project from 20% to not more than 12.5%.

TORCHLIGHT ENERGY RESOURCES, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

4. OIL & GAS PROPERTIES - *continued*

On September 18, 2020, the parties entered into a First Amendment to Option Agreement, under which, the date MHP must exercise its options under the Option Agreement was extended. MHP must now exercise the options no later than February 3, 2021, subject to extension to the earlier of May 31, 2021 or the maturity date of the promissory notes held by the David A. Straz, Jr. Foundation and David A. Straz, Jr. Irrevocable Trust DTD 11/11/1986, if MHP drills the well on the southern half of the prospect, provides notice no later than February 3, 2021 of its intent to conduct operations on the northern half of the prospect and on or before February 17, 2021, conducts operations sufficient to satisfy the drilling obligations regarding the second well on the northern half of the prospect.

Winkler Project, Winkler County, Texas

On December 1, 2017, an Agreement and Plan of Reorganization was entered into with MPC and Warwink Properties, LLC (“Warwink Properties”) to acquire certain assets, including a 10.71875% working interest in approximately 640 acres in Winkler County, Texas. Also on December 1, 2017, MPC closed its transaction with MECO IV, LLC (“MECO”), for the purchase and sale of certain assets. Warwink Properties received a carry from MECO (through the tanks) of up to \$1,179,076 in the next well drilled on the Winkler County leases.

Also on December 1, 2017, the transactions contemplated by the Purchase Agreement that TEI entered into with MPC closed. Under the Purchase Agreement TEI acquired beneficial ownership of certain of MPC’s assets, including acreage and wellbores located in Ward County, Texas (the “Ward County Assets”).

Addition to the Winkler Project

As of May 7, 2018 our Winkler project in the Delaware Basin had begun the drilling phase of the first Winkler Project well, the UL 21 War-Wink 47 #2H. Additional acreage was leased by our operating partner under the Area of Mutual Interest Agreement (AMI) and we exercised its right to participate for its 12.5% in the additional 1,080 gross acres. Our carried interest in the first well was applied to this new well and allowed MECO to drill and produce potential revenues sooner than originally planned. The primary leasehold is a 320-acre block and allows for 5,000-foot lateral wells to be drilled. The first well was completed and began production in October, 2018 and is producing currently.

The operator has informed us that there will be no planned additional wells in the acreage in 2020. All acreage is presently held by production.

During the nine months ended September 30, 2020, the Company transferred a group of marginal unproductive wells (acquired as part of the original Winkler transaction) to the Operator of the properties in exchange for a \$7,000 credit against the outstanding account payable due to the Operator. No gain or loss was recognized on the transaction.

In December 2018, the Company began to take measures on its own to market the Winkler Project in an effort to focus on the Orogrande. This process is ongoing.

Hunton Play, Central Oklahoma

Presently, we are producing from one well in the Viking Area of Mutual Interest and one well in Prairie Grove.

Assessment for Assets Held for Sale Classification

With respect to marketing oil and natural gas properties, the Company has evaluated the properties being marketed to determine whether any should be reclassified as held-for-sale at September 30, 2020. The held-for-sale criteria include: management commits to a plan to sell; the asset is available for immediate sale; an active program to locate a buyer exists; the sale of the asset is probable and expected to be completed within one year; the asset is being actively marketed for sale; and it is unlikely that significant changes to the plan will be made. If each of these criteria is met, the property would be reclassified as held-for-sale on the Company’s consolidated balance sheets and measured at the lower of their carrying amount or estimated fair value less costs to sell. Fair values are estimated using accepted valuation techniques, such as a discounted cash flow model, valuations performed by third parties, earnings multiples, or indicative bids, when available. Management considers historical experience and all available information at the time the estimates are made; however, the fair value that is ultimately realized upon the sale of the assets to be divested may differ from the estimated fair values reflected in the consolidated financial statements. If each of these criteria is met, DD&A expense would not be recorded on assets to be divested once they are classified as held for sale. Based on management’s assessment, certain criteria have not been met and no assets are classified as held for sale as of September 30, 2020.

5. RELATED PARTY PAYABLES

As of September 30, 2020 and December 31, 2019, related party payables was \$5,000, and accrued payroll was \$1,131,176 and \$996,176, respectively, consisting of accrued and unpaid compensation due to our executive officers.

On September 18, 2020, McCabe Petroleum Corporation, an entity owned by Greg McCabe, Torchlight’s Chairman, provided a bridge loan to Torchlight for \$1,500,000. See the description below under the subsection “Secured Convertible Promissory Note Issued in Third Quarter, 2020” in Note 9, which description is incorporated herein by reference. The Company evaluated the note for beneficial conversion feature (“BCF”) and derivative accounting criteria and concluded that there was no BCF or derivative accounting treatment applicable.

6. COMMITMENTS AND CONTINGENCIES

Leases

The Company is a subtenant on a month to month basis for the occupancy of its office premises.

TORCHLIGHT ENERGY RESOURCES, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

6. COMMITMENTS AND CONTINGENCIES - continued

Legal Matters

On January 31, 2020, Torchlight Energy Resources, Inc. and its wholly owned subsidiaries Torchlight Energy, Inc. and Torchlight Energy Operating, LLC were served with a lawsuit brought by Goldstone Holding Company, LLC (*Goldstone Holding Company, LLC v. Torchlight Energy, Inc., et al.*, in the 160th Judicial District Court of Dallas County, Texas). On February 24, 2020, Torchlight Energy Resources, Inc., Torchlight Energy, Inc., and Torchlight Energy Operating, LLC timely filed their answer, affirmative defenses, and requests for disclosure. The suit, which seeks monetary relief over \$1 million, makes unspecified allegations of misrepresentations involving a November 2015 participation agreement and a 2016 amendment to the participation agreement. The Company has denied the allegations and has asserted several affirmative defenses including but not limited to, that the suit is barred by the applicable statute of limitations, that the claims have been released, and that the claims are barred because of contractual disclaimers between sophisticated parties.

On April 30, 2020, our wholly owned subsidiary, Hudspeth Oil Corporation, filed suit against Datalog LWT, Inc. d/b/a Cordax Evaluation Technologies. The suit seeks the recovery of approximately \$1.4 million in costs incurred as a result of a tool failure during drilling activities on the University Founders A25 #2 well that is located in the Orogrande Field. Working interest owner Wolfbone Investments, LLC, a company owned by our Chairman Gregory McCabe, is a co-plaintiff in that action. After the suit was filed, Cordax filed a mineral lien in the amount of \$104,500.01 against the Orogrande Field and has sued the operator and counterclaimed against Hudspeth for breach of contract, seeking the same amount as the lien. We are contesting the lien in good faith. The suit, *Hudspeth Oil Corporation and Wolfbone Investments, LLC v. Datalog LWT, Inc. d/b/a Cordax Evaluation Technologies*, was filed in the 189th Judicial District Court of Harris County, Texas.

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 September 30, 2020 and December 31, 2019, 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.

7. STOCKHOLDERS' EQUITY

Common Stock

On January 10, 2020, the Company sold 600,000 shares of common stock for cash at \$0.60 per share for total proceeds of \$360,000 in a private placement.

On January 16, 2020, the Company announced the closing of its underwritten public offering of 3,285,715 shares of its common stock at a public offering price of \$0.70 per share, for total proceeds of \$1,997,118 after deducting underwriting discounts and other offering expenses payable by the Company.

In May 2020, the Company issued 680,376 shares of common stock in satisfaction of the payment in kind valued at \$14,107 due on April 10, 2020 under the terms of the promissory notes held by the Straz Foundation and the Straz Trust (see Note 9 below).

In May 2020, we issued 1,630,434 restricted shares of common stock to an investor for the purchase price of \$750,000. The investor, Maverick Oil & Gas Corporation, is the operator for our Orogrande Project. Our subsidiary Hudspeth Oil Corporation owed the investor in excess of \$750,000 on unpaid balances and cost overruns on work performed on the Orogrande Project, which amount is due and payable now. The investor agreed to a future credit of \$750,000 in the balance of accounts receivable owed to it by Hudspeth Oil as consideration for the purchase of the common stock. Under the terms of the sale, we provided registration rights to the investor.

On May 20, 2020, the Company announced the closing of its underwritten public offering of 3,450,000 shares of its common stock at a public offering price of \$0.34 per share, for total proceeds of \$886,622 after deducting underwriting discounts and other offering expenses payable by the Company. In connection with the offering the Company issued 172,500 warrants valued at \$36,225 using the Black Scholes method.

TORCHLIGHT ENERGY RESOURCES, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

7. STOCKHOLDERS' EQUITY - *continued*

On June 16, 2020, the Company announced the closing of its registered direct offering of 7,894,737 shares of its common stock at a public offering price of \$0.38 per share, for total proceeds of \$2,783,691 after deducting underwriting discounts and other offering expenses payable by the Company. In connection with the offering the Company issued 3,157,895 warrants. The warrants were exercised on July 9, 2020 under the cashless provisions in the agreement resulting in the Company issuing 3,157,895 shares of common stock for which no cash was received. Of the total proceeds received from the offering, \$854,887 was allocated to the warrants using the pro rata percentage of the number of warrants to the total shares ultimately issued under the offering terms.

During the nine months ended September 30, 2020, the Company issued 317,857 shares of common stock with a fair value of \$61,750 as compensation for services.

During the nine months ended September 30, 2020, the Company issued 40,000 shares of common stock to a vendor with a fair value of \$6,000 for delay in payment on outstanding account payable.

During the nine months ended September 30, 2020, the Company issued 198,926 shares of common stock to a note holder with a fair value of \$5,646 in conversion of principal and accrued interest on a note payable.

During the nine months ended September 30, 2020, the Company issued 40,000 shares of common stock to note holders as compensation for extension of the maturity date of the notes. The fair value of the shares was \$16,000.

During the nine months ended September 30, 2020, the Company issued 257,143 shares of common stock to a vendor with a fair value of \$90,000 in payment of an outstanding account payable.

During the nine months ended September 30, 2020, the Company issued 100,000 shares of common stock to the former CEO of the Company with a fair value of \$5,000 in payment of an accrued liability from prior years.

On July 20, 2020, the Company entered into a Sales Agreement to conduct an "at-the-market" equity offering program pursuant to which the Company may issue and sell, from time to time at its sole discretion, shares of its common stock having an aggregate offering price of up to \$7,000,000. The Sales Agent is entitled to an aggregate fixed commission of 3.0% of the gross proceeds from shares sold. Gross proceeds from sales of 1,557,173 shares under the Sales Agreement through September 30, 2020 totaled \$511,966. Commissions on the sales totaled \$72,997, resulting in net proceeds of \$438,969 during the period.

Warrants and Options

During the nine months ended September 30, 2020, the Company issued 715,000 warrants with total fair value of \$48,900 as compensation for services and recorded expense of \$58,500 related to options issued in prior periods.

During the nine months ended September 30, 2020, the Company issued 750,000 warrants valued at \$82,500 in connection with the conversion of convertible notes payable into working interest in the Company's Orogrande Project.

During the nine months ended September 30, 2020, the Company issued 600,000 warrants in connection with the sale of 600,000 shares of common stock valued at \$360,000 in a private placement.

During the nine months ended September 30, 2020, the Company issued 172,500 warrants valued at \$36,225 in connection with the offering of common stock on May 20, 2020 as referred to above.

In connection with the registered direct offering closed June 16, 2020, as referenced above, the Company issued 3,157,895 warrants. The warrants were exercised on July 9, 2020 under the cashless provisions in the agreement resulting in the Company issuing 3,157,895 shares of common stock for which no cash was received. Of the total proceeds received from the offering \$854,887 was allocated to the warrants using the pro rata percentage of the number of warrants to the total shares ultimately issued under the offering terms.

TORCHLIGHT ENERGY RESOURCES, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

7. STOCKHOLDERS' EQUITY - continued

A summary of warrants outstanding as of September 30, 2020 by exercise price and year of expiration is presented below:

Exercise Price	Expiration Date in					Total
	2021	2022	2023	2024	2025	
\$ 0.425	-	-	-	-	172,500	172,500
\$ 0.500	-	-	500,000	-	-	500,000
\$ 0.70	-	-	-	-	965,000	965,000
\$ 0.80	-	-	-	-	2,266,667	2,266,667
\$ 1.03	120,000	-	-	-	-	120,000
\$ 1.14	-	-	600,000	-	-	600,000
\$ 1.21	-	-	120,000	-	-	120,000
\$ 1.35	-	365,455	-	-	-	365,455
\$ 1.63	-	-	-	100,000	-	100,000
\$ 1.64	200,000	-	-	-	-	200,000
\$ 2.00	200,000	-	-	-	-	200,000
	<u>520,000</u>	<u>365,455</u>	<u>1,220,000</u>	<u>100,000</u>	<u>3,404,167</u>	<u>5,609,622</u>

On June 11, 2020, 4,500,000 stock options previously granted to officers of the Company in 2015 expired.

On July 15, 2020, we entered into new one-year employment agreements with John Brda, our President and Chief Executive Officer, and Roger Wurtele, our Chief Financial Officer. As part of their employment compensation, the Compensation Committee granted Mr. Brda an option to purchase a total of up to 2,250,000 shares of common stock, including up to 375,000 shares at an exercise price of \$0.50 per share and up to 1,875,000 shares at an exercise price of \$1.00 per share, and granted Mr. Wurtele an option to purchase a total of up to 750,000 shares of common stock, including up to 375,000 shares at an exercise price of \$0.50 per share and up to 375,000 shares at an exercise price of \$1.00 per share. The options were granted under our Amended and Restated 2015 Stock Option Plan. The options of both executives will vest upon either (a) the closing of a change of control occurring prior to July 15, 2021, or (b) the Company entering into a letter of intent with a third party prior to July 15, 2021 that contemplates a change of control, and the change of control transaction closes with that third party (or an affiliate(s) of that third party) at a date not later than July 15, 2022; subject, however, to acceleration and earlier vesting of all of the options in the event of (i) the termination of employment by the employee for "good reason" under his employment agreement or (ii) a determination of the Compensation Committee, at its discretion. In the event of the death or disability of the employee prior to vesting or if the Company terminates the employee's employment for reasons other than for "cause" under the employment agreement prior to vesting, the option will still vest upon the occurrence of the events described under clauses (a) or (b) above. The options, to the extent such options have not been exercised, will terminate and become null and void on July 15, 2025, if and only if the options vest as described above, or on July 15, 2021, if the options do not vest as described above, subject to the occurrence of the events contemplated under clause (b) above whereby the options would not terminate until July 15, 2022. At such time that the options vest, the Black Scholes valuation of the options will be recorded as an expense.

A summary of stock options outstanding as of September 30, 2020 by exercise price and year of expiration is presented below:

Exercise Price	Expiration Date in					Total
	2021	2022	2023	2024	2025	
\$ 0.50	-	-	-	-	750,000	750,000
\$ 1.00	-	-	-	-	2,250,000	2,250,000
\$ 0.85	-	-	-	600,000	-	600,000
\$ 0.97	259,742	-	-	-	-	259,742
\$ 1.10	-	800,000	-	-	-	800,000
\$ 1.19	-	-	700,000	-	-	700,000
\$ 1.57	-	-	-	-	-	-
\$ 1.63	-	58,026	-	-	-	58,026
	<u>259,742</u>	<u>858,026</u>	<u>700,000</u>	<u>600,000</u>	<u>3,000,000</u>	<u>5,417,768</u>

At September 30, 2020, the Company had reserved 11,027,390 common shares for future exercise of warrants and options.

TORCHLIGHT ENERGY RESOURCES, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

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 and options issued were as follows:

2020

Risk-free interest rate	0.13% - 1.21%
Expected volatility of common stock	90% - 205%
Dividend yield	0.00%
Discount due to lack of marketability	20%
Expected life of option/warrant	Three Years to Five Years

2019

Risk-free interest rate	1.77% - 2.46%
Expected volatility of common stock	80% - 107%
Dividend yield	0.00%
Discount due to lack of marketability	20%
Expected life of option/warrant	Three Years to Five Years

8. INCOME TAXES

The Company recorded no income tax provision at September 30, 2020 and December 31, 2019 because of losses incurred.

The Company estimates its annual effective income tax rate in recording its quarterly provision for income taxes in the various jurisdictions in which it operates. Statutory tax rate changes and other significant or unusual items are recognized as discrete items in the quarter in which they occur. The Company recorded no income tax expense for the nine months ended September 30, 2020 because the Company expects to incur a tax loss in the current year. Similarly, no income tax expense was recognized for the nine months ended September 30, 2019.

The Company had a net deferred tax asset related to federal net operating loss carryforwards of \$7,280,671 and \$66,984,025 at September 30, 2020 and December 31, 2019, respectively. The federal net operating loss carryforward will begin to expire in 2034. 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.

9. PROMISSORY NOTES

Promissory Notes Issued in 2017

On April 10, 2017, we sold two 12% unsecured promissory notes with a total of \$8,000,000 in principal amount to David A. Straz, Jr. Foundation (the "Straz Foundation") and the David A. Straz, Jr. Irrevocable Trust DTD 11/11/1986 (the "Straz Trust") in a private transaction. 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. We used 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. 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.

TORCHLIGHT ENERGY RESOURCES, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

9. PROMISSORY NOTES - *continued*

The effective interest rate is 16.15%.

On April 24, 2017, we used \$2,509,500 of the proceeds from this financing 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 and \$64,297 was rolled into the new debt financing.

On February 20, 2020, the Company extended the maturity on \$4 million of the 12% unsecured promissory notes previously due in April, 2020. The maturity date of the subject promissory note has been extended for one year, from April 10, 2020 to April 10, 2021.

As part of the terms of this extension agreement, the Company paid the noteholder a fee of \$80,000 on February 20, 2020. The promissory note was originally issued in April 2017, and provides for monthly payments of interest only at the rate of 12% per annum, with a balloon payment of the outstanding principal due and payable at maturity.

Promissory Notes Issued in 2018

On February 6, 2018, we sold to the Straz Trust in a private transaction a 12% unsecured promissory note with a principal amount of \$5,500,000. Interest only was 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 used 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.

The effective interest rate is 15.88%.

Extension of Promissory Notes

On April 24, 2020, the Company entered into a Note Amendment Agreement with each of the Straz Foundation, as a lender, the Straz Trust, as a lender and collateral agent, and The Northern Trust Company and Christopher M. Straz, as co-trustees of the Straz Trust. Under the Note Amendment Agreement, the parties agreed to amend and restate the two promissory notes issued to the Straz Trust on April 10, 2017 and February 6, 2018 that have total principal outstanding of \$8,500,000, along with the promissory note issued to the Straz Foundation on April 10, 2017 which had an outstanding principal amount of \$4,000,000. Under the Note Amendment Agreement, the maturity dates of the two promissory notes held by the Straz Trust and the Note held by the Foundation were extended to April 10, 2021. We had previously extended the maturity date of the promissory note held by the Straz Foundation to April 10, 2021.

Under the Note Amendment Agreements, we and our subsidiaries provided a first priority lien on certain collateral in favor of the collateral agent for the benefit of the lenders. The collateral includes all assets and property held by Hudspeth Oil Corporation and Torchlight Hazel, LLC, which includes without limitation our working interest in certain oil and gas leases in Hudspeth County, Texas, known as the "Orogrande Project" and our working interest in certain oil and gas leases in the Midland Basin in West Texas, known as the "Hazel Project." Further, these subsidiaries, along with Torchlight Energy, Inc., provided guaranty with respect to payment of the three promissory notes. The Note Amendment Agreements also provide that (a) upon any disposition of less than 100% of Borrower's right, title and interest in and to the Orogrande Project or the Hazel Project, we must prepay an amount equal to 75% of the proceeds thereof (up to the outstanding amount due under the notes), unless such disposition results in us owning less than a 45% working interest (on an 8/8ths basis) in the Orogrande Project or the Hazel Project, in which case the prepayment amount is to be equal to 100% of such proceeds (up to the outstanding amount due under the notes); and (b) upon any disposition of 100% of our right, title and interest in and to the Orogrande Project or the Hazel Project, we must prepay an amount equal to 100% of the proceeds thereof (up to the outstanding amount due under the notes).

Additionally, the promissory notes, as amended, now provide conversion rights whereby the lenders will have the right, at each such lender's option, to convert any portion of principal and interest into shares of common stock of Torchlight Energy Resources, Inc. at a conversion price of \$1.50 per share.

TORCHLIGHT ENERGY RESOURCES, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

9. PROMISSORY NOTES - *continued*

The Note Amendment Agreements (as further amended) provided that no later than May 25, 2020, we were obligated to pay: (a) to the lenders all past due interest that has accrued on the existing promissory notes, and (b) to the Straz Trust a fee of \$170,000, which payments were made. Further, the agreements have certain negative covenants regarding related party transactions, dividends, stock repurchases, grants of liens on other assets, and payment of accrued executive compensation. There are also typical affirmative covenants regarding legal compliance and payment of taxes. The agreements also provide certain notice and disclosure requirements, including notice of material events, such as defaults under other obligations and litigation. The \$170,000 extension fee was paid on May 22 and the interest payments were made on June 17, 2020 within the terms of a forbearance agreement which provided an extension of the due date of the interest payments.

All other terms and conditions of the three original promissory notes remain substantially unchanged, including without limitation, monthly payments of interest only at the rate of 12% per annum, with a balloon payment of the outstanding principal due and payable at maturity, and annual payments of common stock at the rate of 2.5% of the principal amount outstanding, based on a volume-weighted average price.

In May 2020 and April 2019, respectively, the holders of the notes described above received 680,376 and 202,316 shares of common stock as a payment in kind representing the annual payments of common stock due at the rate of 2.5% of principal amount outstanding as of April 10 based on a volume-weighted average price calculation.

The 12% promissory note transactions through September 30, 2020 are summarized as follows:

12% 2020 Unsecured promissory note balance - December 31, 2019	\$ 12,377,830
Note principal converted to common stock on July 14, 2020	(64,297)
Accretion of discount and amortization of debt issuance costs	304,275
Debt extension fee paid	(250,000)
12% 2021 Secured promissory note balance - September 30, 2020	<u>\$ 12,367,808</u>

Convertible Notes Issued in October, 2018

On October 17, 2018, we sold to certain investors in a private transaction 16% Series C Unsecured Convertible Promissory Notes with a total principal amount of \$,000,000. Interest and principal were due and payable on the notes in one balloon payment at maturity on April 17, 2020. The notes were convertible, at the election of the holders, into an aggregate 6% working interest in certain oil and gas leases in Hudspeth County, Texas, known as our "Orogrande Project." After an analysis of the transaction and a review of applicable accounting pronouncements, management concluded that the notes issued on October 17, 2018 which contain a conversion right for holders to convert into a working interest in the Orogrande Project of the Company, meet a specific scope exception to the provisions requiring derivative accounting.

TORCHLIGHT ENERGY RESOURCES, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

9. PROMISSORY NOTES - *continued*

On March 9, 2020, each of the noteholders entered into a Conversion Agreement with us and our subsidiary Hudspeth Oil Corporation (“Hudspeth”), under which the noteholders elected to convert the notes, in accordance with their terms, into an aggregate 6% working interest (of all such holders) in certain oil and gas leases in Hudspeth County, Texas, known as our “Orogrande Project.” Principal of \$6,000,000 and approximately \$1,331,000 of accrued interest were converted at March 9, 2020.

The Conversion Agreements also provided additional consideration to the noteholders including a limited carry, a top-off obligation of us and Hudspeth, and warrants to purchase a total of 750,000 restricted shares of our common stock, which warrants will have a term of five years and an exercise price of \$0.70 per share. The limited carry provides that for the remainder of the 2020 calendar year, Hudspeth will pay all costs and expenses attributable to the assigned working interests, except where prohibited by law or regulation. The top-off obligation provides that, subject to the terms and conditions of the Conversion Agreements, if (a) we sell our entire working interest in the Orogrande Project, (b) as part of such sale, the holder’s entire working interests are sold, and (c) the gross proceeds received by all the holders in such transaction are equal to less than \$9,000,000; then we must pay the holders an amount equal to \$9,000,000, (i) less gross proceeds the holders received in the transaction, (ii) less the amount of the carry the holders received under the Conversion Agreements, and (iii) less any gross proceeds the holders received in any farmouts occurring prior to the transaction.

The transaction was treated as an extinguishment of debt. The fair value of the working interest transferred in the conversion of the debt was \$8,778,000 and the value of warrants issued to the holders was \$382,500. The Company recognized a loss on extinguishment of debt in the amount of \$1,829,651 during the nine months ended September 30, 2020.

Convertible Notes Issued in First Quarter 2019

On February 11, 2019 the Company raised a total of \$2,000,000 from investors through the sale of two 14% Series D Unsecured Convertible Promissory Notes. Principal was payable in a lump sum at maturity on May 11, 2020 with payments of interest payable monthly at the rate of 14% per annum. Holders of the notes have the right to convert principal and interest at any time into common stock at a conversion price of \$1.08 per share. The Company has the right to redeem the notes at any time, provided that the redemption amount must include all interest that would have been earned through maturity. The Company evaluated the notes for beneficial conversion features and derivative accounting criteria and concluded that derivative accounting treatment is not applicable.

On April 21, 2020, Torchlight Energy Resources, Inc. entered into agreements to amend the two 14% Series D Unsecured Convertible Promissory Notes that were originally issued on February 11, 2019. Under the amendment agreements, (a) the maturity dates were extended from May 11, 2020 to November 11, 2021, (b) the conversion price under which the noteholders may convert into our common stock was changed from \$1.08 to \$0.43, and (c) the noteholders were provided the right, at each noteholder’s election, to convert their notes into either (i) a working interest in the Orogrande Project at the rate of one acre per \$1,100 of principal and unpaid interest converted, or (ii) a working interest in the Hazel Project at the rate of one acre per \$1,300 of principal and unpaid interest converted; provided, that the noteholders’ right to convert into either such working interest is subject to approval of the collateral agent of the Note Amendment Agreement with the Straz parties.

Under the note amendments, the noteholders agreed to forebear demand or collection on all interest payments due and payable under the Note, including any past due interest payments, for 20 days after the execution of the Note Amendment Agreement. Further, we agreed to (a) issue each holder 20,000 restricted shares of common stock immediately and (b) pay each holder a fee of \$10,000, at the same time as the payment of past due interest is paid. The past due interest and fee was paid.

These two promissory notes will continue to provide for monthly payments of interest only at the rate of 14% per annum, with a balloon payment of the outstanding principal due and payable at maturity.

TORCHLIGHT ENERGY RESOURCES, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

9. PROMISSORY NOTES - *continued*

Convertible Notes Issued in Third Quarter 2019

In July 2019, the Company issued 8% Unsecured Convertible Promissory notes in the amount of \$2,010,000 together with warrants to purchase our common stock. Principal and 8% interest are due at maturity on May 21, 2021. The principal and accrued interest on the notes are convertible into shares of common stock at \$1.10 per common share at any time after the original issue date. Along with the notes, the three year warrants equal to 20% of the number of shares of common stock issuable upon the conversion of the notes were issued to note holders. The warrants are exercisable at \$1.35 per share.

Warrants issued along with the notes meet the requirements of the scope exemptions in ASC 815-10-15-74 and are thus classified as equity upon issuance. The Company determined the fair value of the warrants using the Black Scholes pricing formula and is recognized as a discount on the carrying amount of the notes and is credited to additional paid in capital. The fair value of the warrants at the issuance date was determined to be \$240,455.

A beneficial conversion feature (“BCF”) of a convertible note is normally characterized as the convertible portion feature that provides a rate of conversion that is below market value or “in the money” when issued. The BCF related to the issuance of the notes was recorded at the issuance date. The BCF was measured using the intrinsic value method and is shown as a discount to the carrying amount of the convertible note and is credited to additional paid in capital. The intrinsic value of the BCF at the issuance date of the notes was determined to be \$1,145,546.

The allocated fair values of the BCF and the warrants was recorded as a debt discount from the face amount of the notes and such discount is being accreted over the expected term of the notes and is charged to interest expense. The Company recognized interest expense of \$452,772 from the amortization of debt discount from notes for the nine months ended September 30, 2020.

The Company evaluated the July 2019 notes for derivative accounting criteria and concluded that derivative accounting treatment was not applicable.

Convertible Notes Issued in Fourth Quarter 2019

Effective October 31, 2019, the Company issued 10% Unsecured Convertible Promissory notes in the amount of \$40,000. Principal and interest are due at maturity on December 3, 2020. The principal and accrued interest on the notes are convertible into shares of common stock at \$0.75 per common share at any time after the original issue date. The notes are convertible, at the election of the holders, into an aggregate 0.367% working interest in our Orogrande Project.

The Company evaluated the October 2019 notes for BCF and derivative accounting criteria and concluded that there was no BCF or derivative accounting treatment applicable.

Paycheck Protection Program Loan

In response to the COVID-19 pandemic, the U.S. Small Business Administration (the “SBA”) made available low-interest rate loans to qualified small businesses, including under its Paycheck Protection Program (the “PPP”). On April 10, 2020, in order to supplement its cash balance, the Company submitted an application for a loan (“SBA loan”) in the amount of \$77,477. On May 1, 2020, Company’s SBA loan application was approved and the Company received the loan proceeds. The SBA loan has an interest rate of 0.98% and matures in April 2022.

Section 1106 of the CARES Act provides for forgiveness of up to the full principal amount of qualifying loans guaranteed under the PPP. The PPP and loan forgiveness are intended to provide economic relief to small businesses, such as the Company, that are adversely impacted under the COVID-19 Emergency Declaration issued by President Trump on March 13, 2020. The Company will apply for loan forgiveness.

Secured Convertible Promissory Note Issued in Third Quarter, 2020

On September 18, 2020, McCabe Petroleum Corporation, a company owned by our chairman Gregory McCabe (“MPC”), loaned us \$1,500,000, evidenced by a 6% Secured Convertible Promissory Note (the “MPC Note”). The note bears interest at the rate of 6% per annum and provides for payment of the principal amount along with all accrued and unpaid interest in one lump sum payment on its maturity date of May 10, 2021. In connection with the proposed business combination transaction with Metamaterial Inc. (“Metamaterial”), the note provides the following requirements on the use of proceeds of the loan as follows: (i) we will lend \$500,000 to Metamaterial pursuant to an 8% Unsecured Convertible Promissory Note (the “Metamaterial Note”); (ii) we will retain and use \$500,000 for general corporate purposes, including without limitation, expenses incurred by us in connection with the proposed business combination transaction; and (iii) we will deposit \$500,000 into an escrow account, to be held in escrow. If we and Metamaterial enter into a definitive agreement by the later of November 30, 2020 or such later date that is agreed to by us and Metamaterial in writing, the \$500,000 from this escrow account will be released to us, and we will lend this amount to Metamaterial pursuant to another convertible promissory note (the “Second Metamaterial Note”). If we do not enter into a definitive agreement by the later of November 30, 2020 or such later date that is agreed to in writing, the \$500,000 from this escrow account will be released back to MPC and deducted from the principal amount outstanding under the MPC Note.

The MPC Note is secured by our pledge of the Metamaterial Note and the Second Metamaterial Note (if issued). If we and Metamaterial do not enter into a definitive agreement by the later of November 30, 2020 or such later date that is agreed to in writing, then promptly after that date, we will assign to MPC the Metamaterial Note in full repayment and discharge of \$500,000 (plus accrued and unpaid interest on the Metamaterial Note) of the principal amount of the MPC Note, and the remaining \$500,000 (less accrued and unpaid interest on the Metamaterial Note) of the principal amount, plus all unpaid interest accrued under the MPC Note, will remain subject to the MPC Note. If a definitive agreement is entered into by the later of November 30, 2020 or such later date that is agreed to in writing, but the proposed business combination transaction is terminated prior to closing or otherwise does not close by the maturity date of the MPC Note, then we will assign to MPC both the Metamaterial Note and Second Metamaterial Note in full repayment and discharge of \$1,000,000 (plus accrued and unpaid interest on the Metamaterial Note and Second Metamaterial Note) of the principal amount of the MPC Note, and the remaining \$500,000 (less accrued and unpaid interest on the Metamaterial Note and Second Metamaterial Note) of the principal amount, plus all unpaid interest accrued under the MPC Note, will remain subject to the MPC Note.

TORCHLIGHT ENERGY RESOURCES, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

9. PROMISSORY NOTES - continued

The MPC Note also provides that if (i) we and Metamaterial do not enter into a definitive agreement by the later of November 30, 2020 or such later date that is agreed to in writing, or (ii) we and Metamaterial enter into a definitive agreement but the proposed transaction is terminated prior to closing or otherwise does not close by the maturity date of the MPC Note, then at such time and until the maturity date, MPC will have the right, at its option, to convert up to \$500,000 of the remaining principal amount of the MPC Note, plus all unpaid interest accrued under the MPC Note, into shares of our common stock at a conversion price of \$0.375 per share. Additionally, if the proposed transaction with Metamaterial closes, all principal and interest under the MPC Note will automatically convert into shares of our common stock at \$0.375 per share. The Company evaluated the notes for a beneficial conversion feature (“BCF”) and derivative accounting criteria and concluded that there was no BCF or derivative accounting treatment applicable.

Loan to Metamaterial Inc.

On September 20, 2020, we loaned Metamaterial \$500,000, evidenced by an 8% Unsecured Convertible Promissory Note (the “Metamaterial Note”). The note bears interest at the rate of 8% per annum and provides for payment of the principal amount along with all accrued and unpaid interest in one lump sum payment on its maturity date of September 20, 2022. Metamaterial has the right to redeem after 120 days. The note is convertible at the price of \$0.35 (CAD) per share at the option of the holder if the definitive agreement for the proposed transaction between us and Metamaterial is not entered into by November 2, 2020 (unless extended in writing by the parties) or the definitive agreement is entered but is terminated or expires without closing. The date was extended to November 30, 2020 on November 2, 2020. The Company evaluated the notes for a beneficial conversion feature (“BCF”) and derivative accounting criteria and concluded that there was no BCF or derivative accounting treatment applicable.

10. ASSET RETIREMENT OBLIGATIONS

The following is a reconciliation of the asset retirement obligations liability through September 30, 2020:

Asset retirement obligations – December 31, 2019	\$	23,319
Accretion expense		142
Estimated liabilities recorded		-
Asset retirement obligations – March 31, 2020	\$	23,461
Accretion expense		142
Estimated liabilities recorded		-
Asset retirement obligations – June 30, 2020	\$	23,603
Accretion expense		142
Estimated liabilities recorded		-
Asset retirement obligations – September 30, 2020	\$	23,745

11. SUBSEQUENT EVENTS

Hazel Project Option Agreement

In accordance with the terms of the Option Agreement (see Note 4), Masterson Hazel Partners, LP exercised its option on August 17, 2020 to drill the well that was required to meet the Company’s drilling obligation on the southern half of the prospect. The development of that well is in progress at date of this filing.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Overview

We are an energy company engaged in the acquisition, exploration, exploitation and/or development of oil and natural gas properties in the United States. We are primarily focused on the acquisition of early stage projects, the development and delineation of these projects, and then the monetization of those assets once these activities are completed.

Since 2010, our primary focus has been the development of interests in oil and gas projects we hold in the Permian Basin in West Texas, including the Orogrande Project in Hudspeth County, Texas, the Hazel Project in the Midland Basin and the project in Winkler County, Texas in the Delaware Basin. We also hold interests in certain other oil and gas projects that we are in the process of divesting, including the Hunton wells project as part of a partnership with Husky Ventures, Inc., or Husky, in Central Oklahoma.

We employ a private equity model within a public platform, with the goal to (i) enter into a play at favorable valuations, (ii) "prove up" and delineate the play through committed capital and exhaustive geologic and engineering review, and (iii) monetize our position through an exit to public and private independents that can continue full-scale development. Rich Masterson, our consulting geologist, has originated several of our current plays, as discussed below, based on his tenure as a geologist since 1974. He is credited with originating the Wolfbone shale play in the Southern Delaware Basin of West Texas and has prepared prospects totaling over 150,000 acres that have been leased, drilled and are currently being developed by Devon Energy Corp., Occidental Petroleum Corporation, Noble Energy, and Samson Oil & Gas Ltd., among others.

In April 2018, we announced that we have commenced a process that could result in the monetization of the Hazel Project. Pursuant to our corporate strategy, in our opinion the development activity at the Hazel Project, coupled with nearby activities of other oil and gas operators, is indicative of this project having achieved a level of value that suggests monetization. We believed that the liquidity that would be provided from selling the Hazel Project would be used for debt retirement with any remainder being redeployed into the Orogrande Project. The Hazel Project is currently subject to an Option Agreement, as described above under Note 4.

We are also currently marketing the Orogrande Project for an outright sale or farm in partner and are taking measures on our own to market the Winkler Project. These efforts are continuing.

On September 21, 2020, we announced that we entered into a non-binding letter of intent with Metamaterial Inc. for a proposed business combination transaction. See subsection titled "Recent Developments" below.

We operate our business through five wholly-owned subsidiaries, Torchlight Energy, Inc., a Nevada corporation, 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. We currently have four full-time employees and we employ consultants for various tasks as needed.

Our principal executive offices are located at 5700 W. Plano Parkway, Suite 3600, Plano, Texas 75093. The telephone number of our principal executive offices is (214) 432-8002.

The following discussion of our financial condition and results of operations should be read in conjunction with our unaudited financial statements included herewith and our audited financial statements for the year ended December 31, 2019. 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 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS- *continued*

Historical Results for the nine months ended September 30, 2020 and 2019:

Revenues and Cost of Revenues

For the nine months ended September 30, 2020, we had production revenue of \$191,819 compared to \$619,054 for the nine months ended September 30, 2019. Refer to the table of production and revenue included below for quarterly changes in revenue. Our cost of revenue, consisting of lease operating expenses and production taxes, was \$171,664 and \$358,424 for the nine months ended September 30, 2020 and 2019, respectively.

Property	Quarter	Oil Production {BBLs}	Gas Production {MCF}	Oil Revenue	Gas Revenue	Total Revenue
Oklahoma	Q1 - 2020	181	468	\$ 583	\$ 1,000	\$ 1,583
Hazel (TX)	Q1 - 2020	0	0	\$ -	\$ -	\$ -
MECO (TX)	Q1 - 2020	1,863	1,559	\$ 81,530	\$ 1,507	\$ 83,037
Total Q1-2020		2,044	2,027	\$ 82,113	\$ 2,507	\$ 84,620
Oklahoma	Q2 - 2020	28	448	\$ 774	\$ 156	\$ 930
Hazel (TX)	Q2 - 2020	0	0	\$ -	\$ -	\$ -
MECO (TX)	Q2 - 2020	1,389	747	\$ 44,223	\$ 324	\$ 44,547
Total Q2-2020		1,417	1,195	\$ 44,997	\$ 480	\$ 45,477
Oklahoma	Q3 - 2020	69	1,096	\$ 2,084	\$ 494	\$ 2,578
Hazel (TX)	Q3 - 2020	0	0	\$ -	\$ -	\$ -
MECO (TX)	Q3 - 2020	1,480	680	\$ 57,774	\$ 1,370	\$ 59,144
Total Q3-2020		1,549	1,776	\$ 59,858	\$ 1,864	\$ 61,722
2020 Year To Date		5,010	4,998	\$ 186,968	\$ 4,851	\$ 191,819
Oklahoma	Q1 - 2019	56	1,072	\$ 2,567	\$ 2,333	\$ 4,900
Hazel (TX)	Q1 - 2019	2,864	0	\$ 131,901	\$ -	\$ 131,901
MECO (TX)	Q1 - 2019	3,525	2,565	\$ 167,677	\$ 6,359	\$ 174,036
Total Q1-2019		6,445	3,637	\$ 302,145	\$ 8,692	\$ 310,837
Oklahoma	Q2 - 2019	43	1,770	\$ 2,477	\$ 2,450	\$ 4,927
Hazel (TX)	Q2 - 2019	1,123	0	\$ 64,302	\$ -	\$ 64,302
Meco (TX)	Q2 - 2019	2,585	2,623	\$ 156,259	\$ 11,587	\$ 167,846
Total Q2-2019		3,751	4,393	\$ 223,038	\$ 14,037	\$ 237,075
Oklahoma	Q3 - 2019	0	0	\$ -	\$ -	\$ -
Hazel (TX)	Q3 - 2019	0	0	\$ -	\$ -	\$ -
Meco (TX)	Q3 - 2019	1,320	4,522	\$ 71,064	\$ 78	\$ 71,142
Total Q3-2019		1,320	4,522	\$ 71,064	\$ 78	\$ 71,142
Oklahoma	Q4 - 2019	166	3,766	\$ 8,873	\$ 1,895	\$ 10,768
Hazel (TX)	Q4 - 2019	0	0	\$ -	\$ -	\$ -
Meco (TX)	Q4 - 2019	2,102	5,890	\$ 110,894	\$ 5,547	\$ 116,441
Total Q4-2019		2,268	9,656	\$ 119,767	\$ 7,442	\$ 127,209
2019 Year To Date		13,784	22,208	\$ 716,014	\$ 30,249	\$ 746,263

During the nine months ended September 30, 2020, oil production decreased due to down time associated with equipment repair and typical decline in production from the MECO property.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS- continued

We recorded depreciation, depletion, and amortization expense of \$802,316 for the nine months ended September 30, 2020 compared to \$355,050 for the nine months ended September 30, 2019.

General and Administrative Expenses

Our general and administrative expenses for the nine months ended September 30, 2020 and 2019 were \$2,244,804 and \$2,557,343, respectively, a decrease of \$312,539. 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 fees, and other general corporate expenses. The change in general and administrative expenses for the nine months ended September 30, 2020 compared to 2019 is detailed as follows:

Increase(decrease) in non cash stock and warrant compensation	\$ (475,072)
Increase(decrease) in consulting expense	(64,561)
Increase(decrease) in professional fees	(82,178)
Increase(decrease) in investor relations	131,231
Increase(decrease) in travel expense	(7,787)
Increase(decrease) in salaries and compensation	34,875
Increase(decrease) in legal fees	69,793
Increase(decrease) in insurance	72,082
Increase(decrease) in rent	(14,622)
Increase(decrease) in accounting and audit fees	13,803
Increase(decrease) in general corporate expenses	9,897
Total Decrease in General and Administrative Expenses	\$ (312,539)

Historical Results for the three months ended September 30, 2020 and 2019:Revenues and Cost of Revenues

For the three months ended September 30, 2020, we had production revenue of \$61,722 compared to \$71,142 for the three months ended September 30, 2019. Refer to the table of production and revenue presented above for quarterly changes in revenue. Our cost of revenue, consisting of lease operating expenses and production taxes, was \$23,644 and \$117,104 for the three months ended September 30, 2020 and 2019, respectively.

We recorded depreciation, depletion, and amortization expense of \$77,118 for the three months ended September 30, 2020 compared to \$27,355 for the three months ended September 30, 2019.

General and Administrative Expenses

Our general and administrative expenses for the three months ended September 30, 2020 and 2019 were \$590,369 and \$849,425 respectively, a decrease of \$259,056. 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 change in general and administrative expenses for the three months ended September 30, 2020 compared to 2019 is detailed as follows:

Increase(decrease) in non cash stock and warrant compensation	\$ (112,342)
Increase(decrease) in consulting expense	(125,000)
Increase(decrease) in professional fees	(73,069)
Increase(decrease) in investor relations	(7,624)
Increase(decrease) in travel expense	(4,420)
Increase(decrease) in salaries and compensation	58,295
Increase(decrease) in legal fees	33,471
Increase(decrease) in insurance	14,233
Increase(decrease) in rent	(4,918)
Increase(decrease) in accounting and audit fees	(22,823)
Increase(decrease) in general corporate expenses	(14,859)
Total Decrease in General and Administrative Expenses	\$ (259,056)

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS- *continued*

Liquidity and Capital Resources

At September 30, 2020, we had working capital deficit of \$16,259,366 and total assets of \$35,973,118. Stockholders' equity was \$15,713,135. The negative working capital is principally due to accumulated accounts payable balances at September 30, 2020 and notes payable which are payable within one year.

Cash flows from operating activities for the nine months ended September 30, 2020 was \$(1,304,309) compared to \$(178,588) for the nine months ended September 30, 2019, a decrease of \$1,125,721. Cash flows from operating activities for the nine months ended September 30, 2020 can be primarily attributed to net loss from operations of \$7,878,064, stock based compensation of \$395,150, a loss on extinguishment of debt \$1,829,651, a \$2,108,301 impairment loss, and other noncash expense adjustments. Cash flows from operating activities for the nine months ended September 30, 2019 can be primarily attributed to net loss from operations of \$3,820,145 and \$854,720, in stock compensation expense, an impairment expense of \$474,357 and changes in other noncash expense adjustments. Reference the Consolidated Statements of Cash Flows for additional detail of the components that comprise the net use of cash in operations. We expect to continue to use cash flow in operating activities until such time as we achieve sufficient commercial oil and gas production to cover all of our cash costs.

Cash flows from investing activities for the nine months ended September 30, 2020 was \$(5,570,495) compared to \$(6,612,843) for the nine months ended September 30, 2019. Cash flows from investing activities principally consists of investment in oil and gas properties in Texas.

Cash flows from financing activities for the nine months ended September 30, 2020 was \$7,543,877 as compared to \$6,711,723 for the nine months ended September 30, 2019. Cash flows from financing activities consists of proceeds from issuance of our common stock, proceeds from a subscription receivable, and additional borrowings under notes payable. We expect to continue to have cash flow provided by financing activities as we seek new rounds of financing and continue to develop our oil and gas investments.

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 industry conditions and our history and current record of net losses. 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.

Commitments and Contingencies-

Operating Leases

Effective June 1, 2019 the Company entered into an agreement with a company that had been subleasing a portion of its office space to become the primary obligor on the lease and to assume full responsibility for lease payments after lease expiration on November 30, 2019. The Company has continued after November 30, 2019 as a subtenant on a month-to-month basis.

Environmental matters

We are subject to contingencies as a result of environmental laws and regulations. Present and future environmental laws and regulations applicable to our operations could require substantial capital expenditures or could adversely affect our operations in other ways that cannot be predicted at this time. As of September 30, 2020 and December 31, 2019, no amounts have been recorded because no specific liability has been identified that is reasonably probable of requiring us to fund any future material amounts.

Recent Developments

On September 21, 2020, we announced that we entered into a non-binding letter of intent with Metamaterial Inc., an Ontario business corporation headquartered in Nova Scotia, Canada ("Metamaterial"), for a proposed business combination transaction. On November 2, 2020, the letter of intent was extended. See our current reports on Form 8-K filed on September 23, 2020 and November 2, 2020 for a description of the proposed parameters of the transaction.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Not Applicable

ITEM 4. CONTROLS AND PROCEDURES

Disclosure Controls and Procedures

Under the supervision and with the participation of our management, including our Chief Executive Officer (principal executive officer) and Chief Financial Officer (principal financial officer), we evaluated the effectiveness of the design and operation of our disclosure controls and procedures, as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act, as of September 30, 2020. Based on this evaluation, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were effective to ensure that the information required to be disclosed by us in the reports we submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the applicable rules and forms and that such information was accumulated and communicated to our Chief Executive Officer and Chief Financial Officer, in a manner that allowed for timely decisions regarding disclosure.

Changes in Internal Control over Financial Reporting

There were no changes during the quarter ended September 30, 2020 that materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

On January 31, 2020, Torchlight Energy Resources, Inc. and its wholly owned subsidiaries Torchlight Energy, Inc. and Torchlight Energy Operating, LLC were served with a lawsuit brought by Goldstone Holding Company, LLC (*Goldstone Holding Company, LLC v. Torchlight Energy, Inc., et al.*, in the 160th Judicial District Court of Dallas County, Texas). On February 24, 2020, Torchlight Energy Resources, Inc., Torchlight Energy, Inc., and Torchlight Energy Operating, LLC timely filed their answer, affirmative defenses, and requests for disclosure. The suit, which seeks monetary relief over \$1 million, makes unspecified allegations of misrepresentations involving a November 2015 participation agreement and a 2016 amendment to the participation agreement. We have denied the allegations and have asserted several affirmative defenses including but not limited to, that the suit is barred by the applicable statute of limitations, that the claims have been released, and that the claims are barred because of contractual disclaimers between sophisticated parties.

On April 30, 2020, our wholly owned subsidiary, Hudspeth Oil Corporation, filed suit against Datalog LWT, Inc. d/b/a Cordax Evaluation Technologies. The suit seeks the recovery of approximately \$1.4 million in costs incurred as a result of a tool failure during drilling activities on the University Founders A25 #2 well that is located in the Orogrande Field. Working interest owner Wolfbone Investments, LLC, a company owned by our Chairman Gregory McCabe, is a co-plaintiff in that action. After suit was filed, Cordax filed a mineral lien in the amount of \$104,500.01 against the Orogrande Field and has sued the operator and counterclaimed against Hudspeth for breach of contract, seeking the same amount as the lien. We are contesting the lien in good faith. The suit, *Hudspeth Oil Corporation and Wolfbone Investments, LLC v. Datalog LWT, Inc. d/b/a Cordax Evaluation Technologies*, was filed in the 189th Judicial District Court of Harris County, Texas.

ITEM 1A. RISK FACTORS

There were no material changes to the risk factors disclosed in our Annual Report on Form 10-K for the fiscal year ended December 31, 2019, except for such risks and uncertainties associated with the COVID-19 pandemic, as disclosed below. The risks described in the Annual Report on Form 10-K and in this Form 10-Q are not the only risks we face. Additional risks and uncertainties not currently known to us, or that we deem to be immaterial, also may have a material adverse impact on our business, financial condition or results of operations.

An occurrence of an uncontrollable event such as the COVID-19 pandemic is likely to negatively affect, and has to date negatively affected, our operations.

The occurrence of an uncontrollable event such as the COVID-19 pandemic is likely to, and has already, negatively affected our operations. A pandemic typically results in social distancing, travel bans and quarantine, and the effects of, and response to, the COVID-19 pandemic has limited access to our facilities, properties, management, support staff and professional advisors. These, in turn, have not only negatively impacted our operations and financial condition, but our overall ability to react timely to mitigate the impact of this event. Further, the COVID-19 pandemic has resulted in declines in the demand for, and the price of, oil and gas, and it is unclear how long this decline will last. The full effect on our business and operation is currently unknown. In the event that the effects of COVID-19 continue in the future and/or the economy continues to deteriorate, we may be forced to curtail our operations and may be unable to pay our debt obligations as they come due.

ITEM 1A. RISK FACTORS - continued

The coronavirus/COVID-19 pandemic has had a negative effect on oil and gas prices, and depending on the severity and longevity of the pandemic, it may result in a major economic recession which will continue to depress oil and gas prices and cause our business and results of operations to suffer.

The inability and/or unwillingness of individuals to congregate in large groups, travel and/or visit retail businesses or travel outside of their homes will, and has to date, had a negative effect on the demand for, and the current prices of, oil and gas. Additionally, the demand for oil and gas is based partially on global economic conditions. If the COVID-19 pandemic results in a global economic recession, there will be a continued negative effect on the demand for oil and gas and this will have a negative effect on our operating results. All of the above may be exacerbated in the future as the COVID-19 outbreak and the governmental responses thereto continue. Concerns about global economic growth have had a significant adverse impact on global financial markets and commodity prices. If the economic climate in the United States or abroad continues to deteriorate, demand for petroleum products could further diminish, which will impact the price at which we can sell our oil and gas, impact the value of our working interests and other oil and gas assets, affect the ability of our vendors, suppliers and customers to continue operations, affect our operations and ultimately adversely impact our results of operations, liquidity and financial condition.

The proposed business combination transaction with Metamaterial may not be completed on the terms or timeline currently contemplated, or at all, and we will incur significant expenses in connection with the steps we will take to pursue the business combination transaction.

The consummation of the proposed business combination transaction with Metamaterial is subject to numerous conditions, including (i) entry into a definitive arrangement agreement, which is subject to our and Metamaterial's satisfactory completion of due diligence and the negotiation of the final terms and conditions of the business combination transaction, (ii) the absence of certain legal impediments to the consummation of the proposed business combination transaction, (iii) the approval of the business combination transaction by our stockholders and Metamaterial's stockholders, and (iv) the satisfaction of certain customary and deal-specific conditions to closing that will be contemplated under the final arrangement agreement. We cannot assure you that the proposed business combination will be consummated on the terms or timeline currently contemplated, or at all.

Further, we have expended, and will continue to expend, significant management time and resources and have incurred, and will continue to incur, significant expenses due to legal, advisory and financial services fees related to the proposed business combination transaction. These expenses must be paid regardless of whether the proposed business combination is consummated. Our management's focus on the proposed business combination could reduce their ability to adequately manage our operations, and the financial expenses associated with the proposed business combination transaction may harm our cash position, both of which may negatively impact our business.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

In July 2020, we issued 198,926 shares of common stock to a noteholder in the conversion of \$65,646 in principal and accrued interest on his promissory note.

In August 2020, we issued 50,000 restricted shares of common stock to a consultant as consideration for services.

In August 2020, we issued warrants to purchase a total of 500,000 shares of common stock at an exercise price of \$0.50 per share to certain consultants as consideration for services. The warrants are exercisable for a term of three years.

All of the above sales of securities 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. EXHIBITS

Exhibit No.	Description
2.1	Share Exchange Agreement dated November 23, 2010. (Incorporated by reference from Form 8-K filed with the SEC on November 24, 2010.) *
3.1	Articles of Incorporation. (Incorporated by reference from Form 10-K filed with the SEC on March 18, 2019.) *
3.2	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.) *
3.3	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.) *
3.4	Certificate of Amendment to Articles of Incorporation dated August 18, 2017 (Incorporated by reference from Form 10-Q filed with the SEC on August 9, 2018.) *
3.5	Amended and Restated Bylaws (Incorporated by reference from Form 8-K filed with the SEC on October 26, 2016.) *
10.1	Farmout Agreement between Hudspeth Oil Corporation, Founders Oil & Gas, LLC and certain other parties (Incorporated by reference from Form 8-K filed with the SEC on September 29, 2015) *
10.2	Purchase and Sale Agreement with Husky Ventures, Inc. (Incorporated by reference from Form 8-K filed with the SEC on November 12, 2015) *
10.3	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) *
10.4	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) *
10.5	Purchase and Sale Agreement with Wolfbone Investments, LLC (Incorporated by reference from Form 10-K filed with the SEC on March 31, 2017) *
10.6	Agreement and Plan of Reorganization and Plan of Merger with McCabe Petroleum Corporation and Warwink Properties, LLC (Incorporated by reference from Form 10-K filed with the SEC on March 16, 2018) *
10.7	Purchase Agreement with Torchlight Energy, Inc. and McCabe Petroleum Corporation (Incorporated by reference from Form 10-K filed with the SEC on March 16, 2018) *
10.8	Promissory Note for \$3,250,000 by Torchlight Energy, Inc. to McCabe Petroleum Corporation (Incorporated by reference from Form 10-K filed with the SEC on March 16, 2018) *
10.9	Assignment of Farmout Agreement between Hudspeth Oil Corporation, Founders Oil & Gas, LLC and Wolfbone Investments, LLC (Incorporated by reference from Form 10-K filed with the SEC on March 16, 2018) *
10.10	Underwriting Agreement, dated April 19, 2018, between Torchlight Energy Resources, Inc. and Roth Capital Partners, LLC (Incorporated by reference from Form 8-K filed with the SEC on April 19, 2018) *
10.11	Purchase & Settlement Agreement, dated July 24, 2018, between Torchlight Energy Resources, Inc., Hudspeth Oil Corporation, Founders Oil & Gas, LLC, Founders Oil & Gas Operating, LLC, Wolfbone Investments, LLC and McCabe Petroleum Corporation (Incorporated by reference from Form 10-Q filed with the SEC on August 9, 2018) *

- [10.12](#) [16% Series C Unsecured Convertible Promissory Note \(form of\) dated October 17, 2018 \(Incorporated by reference from Form 8-K filed with the SEC on October 18, 2018\)*](#)
- [10.13](#) [Underwriting Agreement, dated January 14, 2020, between Torchlight Energy Resources, Inc. and Aegis Capital Corp. \(Incorporated by reference from Form 8-K filed with the SEC on January 14, 2020\) *](#)
- [10.14](#) [Conversion Agreement \(form of\) dated March 9, 2020 between Torchlight Energy Resources, Inc., Hudspeth Oil Corporation and the previous holders of 16% Series C Unsecured Convertible Promissory Notes \(Incorporated by reference from Form 10-K filed with the SEC on March 16, 2020\) *](#)
- [10.15](#) [Underwriting Agreement, dated May 18, 2020, between Torchlight Energy Resources, Inc. and ThinkEquity, a division of Fordham Financial Management, Inc. \(Incorporated by reference from Form 8-K filed with the SEC on May 18, 2020\) *](#)
- [10.16](#) [Foundation Note Amendment Agreement dated April 24, 2020 with the David A. Straz, Jr Foundation \(Incorporated by reference from Form 10-Q filed with the SEC on June 5, 2020\)](#)
- [10.17](#) [Amendment to Foundation Note Amendment Agreement dated May 12, 2020 with David A. Straz, Jr. Foundation \(Incorporated by reference from Form 10-Q filed with the SEC on June 5, 2020\)](#)
- [10.18](#) [Trust Note Amendment Agreement dated April 24, 2020 with The David A. Straz, Jr. Irrevocable Trust DTD 11/11/1986 \(Incorporated by reference from Form 10-Q filed with the SEC on June 5, 2020\)](#)
- [10.19](#) [Amendment to Trust Note Amendment Agreement dated May 12, 2020 with the David A. Straz Jr. Irrevocable Trust DTD 11/11/1986 \(Incorporated by reference from Form 10-Q filed with the SEC on June 5, 2020\)](#)
- [10.20](#) [Amended and Restated Note dated April 24, 2020 in the amount of \\$4,000,000 with The David A. Straz, Jr. Irrevocable Trust DTD 11/11/1986 \(Incorporated by reference from Form 10-Q filed with the SEC on June 5, 2020\)](#)
- [10.21](#) [Amended and Restated Note dated April 24, 2020 in the amount of \\$4,500,000 with THE David A. Straz, Jr. Irrevocable Trust DTD 11/11/1986 \(Incorporated by reference from Form 10-Q filed with the SEC on June 5, 2020\)](#)
- [10.22](#) [Amended and Restated Note dated April 24, 2020 in the amount of \\$4,000,000 with David A. Straz, Jr. Foundation \(Incorporated by reference from Form 10-Q filed with the SEC on June 5, 2020\)](#)
- [10.23](#) [Form of Securities Purchase Agreement, dated June 12, 2020, between Torchlight Energy Resources, Inc. and the investor \(Incorporated by reference from Form 8-K filed with the SEC on June 12, 2020\) *](#)
- [10.24](#) [Employment Agreement with John A. Brda dated July 15, 2020 \(Incorporated by reference from Form 8-K filed with the SEC on July 16, 2020\) *](#)
- [10.25](#) [Employment Agreement with Roger Wurtele dated July 15, 2020 \(Incorporated by reference from Form 8-K filed with the SEC on July 16, 2020\) *](#)
- [10.26](#) [Stock Option Agreement with John A. Brda dated July 15, 2020 \(Incorporated by reference from Form 8-K filed with the SEC on July 16, 2020\) *](#)
- [10.27](#) [Stock Option Agreement with Roger Wurtele dated July 15, 2020 \(Incorporated by reference from Form 8-K filed with the SEC on July 16, 2020\) *](#)
- [10.28](#) [Sales Agreement, dated July 20, 2020, between Torchlight Energy Resources, Inc. and Roth Capital Partners, LLC \(Incorporated by reference from Form 8-K filed with the SEC on July 20, 2020\) *](#)
- [10.29](#) [Option Agreement with Masterson Hazel Partners, LP and McCabe Petroleum Corporation dated August 13, 2020](#)
- [10.30](#) [First Amendment to Option Agreement with Masterson Hazel Partners, LP and McCabe Petroleum Corporation dated September 18, 2020](#)
- [10.31](#) [6% Secured Convertible Promissory Note for \\$1,500,000 to McCabe Petroleum Corporation dated September 18, 2020 \(and Amendment to Promissory Note\)](#)
- [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.](#)

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

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

SIGNATURES

Pursuant to the requirements 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.

Date: November 9, 2020

/s/ John A. Brda

By: John A. Brda
Chief Executive Officer

Date: November 9, 2020

/s/ Roger Wurtele

By: Roger Wurtele
Chief Financial Officer and Principal Accounting Officer

OPTION AGREEMENT

This option agreement (the “*Option Agreement*”), is made on August 13, 2020 (the “*Effective Date*”), by TORCHLIGHT ENERGY, INC., a Texas corporation, and TORCHLIGHT HAZEL, LLC, a Texas limited liability company, whose mailing address is 5700 W. Plano Pkwy #3600, Plano, TX 75093 and email address is john@torchlightenergy.com (collectively “*Torchlight*”), MASTERSON HAZEL PARTNERS, LP, a Texas limited partnership whose mailing address is P.O. Box 1189, Midland, TX 79702 and email address is ced@mastersonps.com (“*Masterson*”), and McCabe Petroleum Corporation, a Texas Corporation, whose mailing address is 500 W. Texas Ave. Ste. 890, Midland, TX 79701 and email address is gregmccabe@aol.com (“*MPC*”) collectively the “*Parties*”.

I – Drilling Obligation & Grant of Options

Masterson shall drill and complete, or cause to be drilled and completed, at its sole cost and expense (subject to Sections V and VII), a new lateral well on Torchlight’s Hazel Prospect¹ (the “*Well*”) sufficient to satisfy Torchlight’s continuous development obligations on the southern half of the Hazel Prospect² (“*Southern Drilling Obligations*”). Masterson shall satisfy the Southern Drilling Obligations no later than September 30, 2020. Provided, however, that Masterson shall be entitled to receive, as its sole recourse for the recoupment of Drilling Costs, the revenue from production of the Well attributable to Torchlight’s interest (“*Production Revenue*”) until such time as it has recovered its reasonable costs and expenses for drilling, completing, and operating the Well (“*Drilling Costs*”).

In exchange for Masterson satisfying the Southern Drilling Obligations, Torchlight grants to Masterson the exclusive right and option to perform operations, at Masterson’s sole cost and expense, on the Hazel Prospect sufficient to satisfy Torchlight’s continuous development obligations on the northern half of the Hazel Prospect (“*Northern Drilling Obligations*”),³ as defined below (the “*Drilling Option*”). Masterson will also pay to Torchlight \$1,000.00 at the time this Option Agreement is executed and delivered as further consideration of the Options (“*Option Fee*”). In spite of anything to the contrary, if Masterson fails to satisfy the Southern Drilling Obligations by September 30, 2020, then the Options will automatically terminate, and Torchlight may retain the Option Fee as its sole remedy.

In the event that Masterson exercises such Drilling Option and satisfies the Northern Drilling Obligations, then Masterson shall have the option to purchase the Hazel Prospect under the terms of the Purchase and Sale Agreement which is attached as Exhibit “B” (the “*Purchase Option*”). The Drilling Option and Purchase Option may be collectively referred to herein as the “*Options*”.

¹ “Hazel Prospect” means Torchlight and its subsidiaries’ interests in the Hazel Prospect leases and the lands described in Exhibit “A” and the Assets as described in the Purchase Sale Agreement attached as Exhibit “B”.

² The south half of the Hazel Prospect being those 5,131.44 net mineral acres in Sections 70, 71, 72, 73, 74, 75, 41, 86, 87 and 88 as described further in Exhibit “A” and the Assets as described in the Purchase Sale Agreement attached as Exhibit “B”.

³ The north half of the Hazel Prospect being those 4,630.64 net mineral acres in Sections 89, 90, 91, 102, 103, 104, 105, 106 and 107 as described further in Exhibit “A”.

II - Option Period

The time during which Masterson may exercise the Options shall be from the Effective Date through and including December 1, 2020, unless extended under the terms of this Option Agreement (the "***Option Period***"). The Option Period may be extended to March 31, 2021 if Masterson: (1) has satisfied its obligations regarding the Well; (2) no later than December 1, 2020, delivers notice of intent to conduct operations sufficient to satisfy the Northern Drilling Obligations; and (3) on before December 15, 2020 conducts operations sufficient to satisfy the Northern Drilling Obligations.

III - Purchase Price of Hazel Prospect

The full purchase price of the Hazel Prospect is \$12,690,704.00 for approximately 9,762.08 net mineral acres (the "***Purchase Price***"), and not less than a 74% net revenue interest (the "***NRI***"), which is payable as provided in this Option Agreement and the "***Purchase Sale Agreement***", which is to be executed by the parties in the form of the document attached as Exhibit "B", if Masterson elects to exercise the Purchase Option. The price per net mineral acre shall be \$1,300.00.

As provided in the Purchase Sale Agreement, in the event Masterson establishes that Torchlight or its subsidiaries own more or less net mineral acreage or NRI than set forth above, the Purchase Price shall accordingly be proportionately increased or reduced by the price per net mineral acre.

Torchlight shall maintain and protect the leasehold interest until execution of the Purchase Sale Agreement or give Masterson thirty (30) days prior written notice of Torchlight's intent not to maintain and protect said leasehold interest.

IV - MPC Reversionary Interest

In order to induce Masterson to enter into this Option Agreement, on the strict condition of Masterson closing the transaction pursuant to the Purchase Sale Agreement, then MPC (an entity wholly owned by Greg McCabe) agrees to reduce its reversionary interest burdening Torchlight's proportionate interest in the Hazel Prospect (as described in that certain "***Participation Agreement***" dated May 1, 2016) from 20% to not more than 12.5%.

V - The Well

The Well shall be a lateral well drilled by, or caused to be drilled by, Masterson utilizing a stimulation method at a location and length approved, in writing and prior to commencement, by Greg McCabe or Rich Masterson. Masterson, its affiliates and agents shall have the right to use any and all necessary Torchlight facilities, including, but not limited to, Torchlight or its affiliates' tank battery. At all times Masterson shall conduct itself and the operations in a manner consistent with a reasonably prudent operator.

If, during the drilling of the Well, Masterson shall encounter granite or any other practically impenetrable substance or encounter mechanical difficulties or if the hole is lost for any reason not reasonably within control of Masterson, Masterson shall have and is hereby granted the right to abandon said well; and Masterson may commence the actual drilling and completion, at Masterson's sole costs and expense (subject to Section VII), of a substitute well to serve as the Well. If a substitute well is commenced, it will be drilled at a location and using a stimulation method and depth as approved by Greg McCabe or Rich Masterson. For the avoidance of doubt, the substitute well shall be deemed to be the Well for all purposes of this Option Agreement.

Torchlight shall instruct the payor of any proceeds of production to deliver all income attributable to Torchlight's interest that is generated from the Well directly to Masterson until Masterson's Drilling Costs have been recouped in full. In the event Torchlight receives any proceeds that should have been delivered to Masterson, Torchlight shall immediately notify Masterson and send the misdelivered proceeds to Masterson.

VI - Purchase Sale Agreement

Within ten (10) days of a timely election of Masterson's exercise of the Purchase Option pursuant to Section IV, Torchlight and Masterson shall execute the Purchase Sale Agreement for the Hazel Prospect attached as Exhibit "B".

The Parties covenant that at any time after the Effective Date of this Option Agreement, they will execute such additional instruments and take such actions as may be reasonably be requested by the party(ies) to confirm or perfect or otherwise to carry out the intent and purposes of this Option Agreement.

VII - Failure to Exercise Option

If Masterson does not exercise the Drilling Option in accordance with its terms and within the Option Period, the Purchase Option and the rights of Masterson will automatically and immediately terminate.

Pursuant to the terms of Section V, if Masterson fails to exercise the Purchase Option, Masterson shall retain any and all income from the Well until Masterson recoups all Drilling Costs, as Masterson's sole recourse in recouping its Drilling Costs.

VIII - Notices

All notices provided for in this Option Agreement will be deemed to have been given if and when deposited in the United States mail by registered or certified mail, properly stamped and addressed to the party for whom intended, at the party's address listed above, or when delivered personally in writing to the party, or via electronic mail to the addresses provided in the Option Agreement.

IX - Binding Effect and Miscellaneous Provisions

This Option Agreement and corresponding Purchase Sale Agreement are subject to any and all leases, assignments, or other public filings affecting the Assets, the Participation Agreement, that certain Farmout Agreement executed by and between Oxy USA, Inc. and Imperial Exploration, LLC on March 21, 2016, and that certain Joint Operating Agreement executed by, between, and among Torchlight Energy Operating, LLC, Torchlight Energy, Inc., and Imperial Exploration, LLC on May 1, 2016 ("**JOA**").

This Option Agreement is not transferable nor assignable unless agreed to by the Parties in writing and will be binding on and inure to the benefit of the Parties to them and to their respective heirs, personal representatives, successors, and assigns. Any assignment made in violation of this requirement is void.

Except as otherwise expressly provided herein, no waiver with respect to this Option Agreement shall be enforceable unless in writing and signed by the party against whom enforcement is sought. Except as otherwise expressly provided herein, no failure to exercise, delay in exercising, or single or partial exercise of any right, power or remedy by any party, and no course of dealing between or among any of the Parties, shall constitute a waiver of, or shall preclude any other or further exercise of, any right, power or remedy.

This Option Agreement may be executed in counterparts, each of which shall be deemed an original and both considered one and the same Option Agreement and shall become effective when counterparts have been signed by each party and delivered to the other party, it being understood that both parties need not sign the same counterpart. In the event that any signature is delivered by e-mail delivery of a ".pdf" format data file, such signature shall create a valid and binding obligation of the party executing (or on whose behalf such signature is executed) with the same force and effect as if such ".pdf" signature page were an original thereof. This Option Agreement shall only be binding on the Parties and their respective successors and assigns when executed by both of the Parties.

In connection with the negotiation and drafting of this Option Agreement, the Parties represent and warrant to each other that they have had the opportunity to be advised by attorneys of their own choice and, therefore, the normal rule of construction to the effect that any ambiguities are to be resolved against the drafting Party shall not be employed in the interpretation of this Option Agreement or any amendments hereto.

If any provision of this Option Agreement is held to be illegal, invalid, or unenforceable under present or future law, such provision shall be fully severable and this Option Agreement shall be construed and enforced as if such illegal, invalid, or unenforceable provision had never comprised a part hereof, and the remaining provisions hereof shall remain in full force and effect and shall not be affected by the illegal, invalid, or unenforceable provision or by its severance herefrom. Furthermore, in lieu of such illegal, invalid, or unenforceable provision, there shall be added automatically, as part of this Option Agreement, a provision as similar in terms and substance to such illegal, invalid, or unenforceable provision as may be possible and legal, valid, and enforceable.

OPTION AGREEMENT

- Page 4 -

The Parties agree that as between the Parties hereto the terms in this Option Agreement shall prevail should there be any conflict with any other agreement, including, but not limited to, the Purchase Sale Agreement.

Capitalized terms used but not defined herein shall have the respective meanings given to them in the Purchase Sale Agreement.

This Option Agreement shall be governed by and construed in accordance with the domestic laws of the State of Texas without giving effect to any choice or conflict of law provision or rule that would cause the application of the laws of any jurisdiction other than the State of Texas. The Parties agree that venue is proper in Midland County, Texas and if venue is not mandatory shall be filed in a court of competent jurisdiction in Midland County, Texas.

This Option Agreement shall not confer any rights or remedies upon any person other than the Parties and their respective successors and assigns.

Each of the Parties agrees to execute, acknowledge, and deliver to the other party such further instruments, and take such other actions, as may be reasonably requested in order to more effectively assure to said other party all of the respective rights, titles, interests, and privileges intended to be assigned or inuring to the benefit of such party in consummation of the transactions contemplated hereby.

The Parties agree that this Option Agreement is intended to be a fully-integrated document, and all prior agreements or understanding regarding the subject matter are superseded by this Option Agreement.

A Party prevailing in any legal action arising from this Option Agreement shall be entitled to recover its reasonable and necessary attorney fees and costs from the non-prevailing Party(ies).

[Signature pages follow.]

FIRST AMENDMENT TO OPTION AGREEMENT

This First Amendment (this "**First Amendment**") to the Option Agreement (as defined below), is made and entered into on September 15, 2020, to be effective on August 13, 2020 (the "**Effective Date**"), by **TORCHLIGHT ENERGY, INC.**, a Texas corporation, and **TORCHLIGHT HAZEL, LLC**, a Texas limited liability company, whose mailing address is 5700 W. Plano Pkwy #3600, Plano, TX 75093 and email address is john@torchlightenergy.com (collectively "**Torchlight**"), **MASTERSON HAZEL PARTNERS, LP**, a Texas limited partnership whose mailing address is P.O. Box 1189, Midland, TX 79702 and email address is ced@mastersonps.com ("**Masterson**"), and McCabe Petroleum Corporation, a Texas Corporation, whose mailing address is 500 W. Texas Ave. Ste. 890, Midland, TX 79701 and email address is gregmccabe@aol.com ("**MPC**") collectively the "**Parties**".

RECITALS:

- A. The Parties entered into that certain Option Agreement, dated August 13, 2020.
- B. The undersigned, which constitute all of the Parties to the Option Agreement, desire to amend the Option Agreement.

AGREEMENT:

NOW, THEREFORE, in consideration of the mutual agreements herein contained and for other good and valuable consideration, the receipt and sufficiency of which is hereby acknowledged, the undersigned hereby agree to amend the Option Agreement as follows, effective as of the Effective Date:

1. Masterson will pay to Torchlight \$1,000.00 at the time this First Amendment is executed and delivered as further consideration of the Options.
2. Section II of the Option Agreement is hereby deleted in its entirety and replaced with the following:

II - Option Period

The time during which Masterson may exercise the Options shall be from the Effective Date through and including February 3, 2021, unless extended under the terms of this Option Agreement (the "**Option Period**"). The Option Period may be extended to the earlier of (1) May 31, 2021 or (2) the Final Maturity Date (as defined below) of the notes set forth in Exhibit A attached hereto (the "**Notes**"), if Masterson: (a) has satisfied its obligations regarding the Well; (b) no later than February 3, 2021, delivers notice of intent to conduct operations sufficient to satisfy the Northern Drilling Obligations; and (c) on before February 17, 2021 conducts operations sufficient to satisfy the Northern Drilling Obligations. The "**Final Maturity Date**" shall be defined as the date upon which the first of the Notes becomes due and payable.

3. Except as amended by this First Amendment, the Option Agreement shall remain in full force and effect, and each of the undersigned hereby restates and reaffirms all of the terms and provisions of the Option Agreement.

4. This First Amendment may be executed in any number of counterparts (including by facsimile or other reliable electronic means), each of which shall be considered an original.

[Signature pages follow.]

MASTERSON HAZEL PARTNERS, LP

X: /s/ Clifton DuBose, Jr.
Clifton Edwin DuBose, Jr., CEO of Masterson
Hazel Management, LLC, its General Partner

STATE OF TEXAS

§

COUNTY OF MIDLAND

§

BEFORE ME, the undersigned authority, on this day personally appeared Clifton Edwin DuBose, Jr., who being duly sworn, upon oath, says that he is authorized to execute this agreement; and he acknowledged to me that he executed the same for the purposes and considerations therein expressed, and in the capacity stated herein. SUBSCRIBED AND SWORN TO before me by the said CEO on this the 18th day of September 2020, to certify which witness my hand and seal of office.

/s/ Amy Taylor
Notary Public
In and For Said County and State

MCCABE PETROLEUM CORPORATION

X: /s/ Greg McCabe
Name: Greg McCabe
Title: President

STATE OF TEXAS

§

COUNTY OF MIDLAND

§

BEFORE ME, the undersigned authority, on this day personally appeared Greg McCabe, who being duly sworn, upon oath, says that he is authorized to execute this agreement; and he acknowledged to me that he executed the same for the purposes and considerations therein expressed, and in the capacity stated herein. SUBSCRIBED AND SWORN TO before me by the said President on this the 18th day of September 2020, to certify which witness my hand and seal of office.

/s/ Amy Taylor
Notary Public
In and For Said County and State

NEITHER THIS 6% SECURED CONVERTIBLE PROMISSORY NOTE (THE "NOTE") NOR THE SECURITIES ISSUABLE IN CONNECTION WITH THIS NOTE HAVE BEEN REGISTERED UNDER THE SECURITIES ACT OF 1933, AS AMENDED ("ACT"), OR THE SECURITIES LAWS OF ANY STATE. NEITHER THIS NOTE NOR THE SECURITIES ISSUABLE IN CONNECTION WITH THIS NOTE MAY BE SOLD, PLEDGED OR OTHERWISE TRANSFERRED WITHOUT REGISTRATION UNDER THE ACT AND ANY APPLICABLE STATE SECURITIES LAWS OR DELIVERY TO TORCHLIGHT ENERGY RESOURCES, INC. OF AN OPINION OF LEGAL COUNSEL SATISFACTORY TO TORCHLIGHT ENERGY RESOURCES, INC. THAT SUCH REGISTRATION IS NOT REQUIRED UNDER THE ACT OR ANY APPLICABLE STATE SECURITIES LAWS.

6% SECURED CONVERTIBLE PROMISSORY NOTE
OF
TORCHLIGHT ENERGY RESOURCES, INC.

NOTE NO. _____

September 18, 2020

FOR VALUE RECEIVED, TORCHLIGHT ENERGY RESOURCES, INC., a Nevada corporation with its principal office located at 5700 Plano Parkway, Ste. 3600, Plano, Texas 75093 (the "Company" or "Debtor"), unconditionally promises to pay to McCabe Petroleum Corporation whose address is 500 W Texas Ave, Ste. 890, Midland, Texas 79702, or the registered assignee, upon presentation of this 6% Secured Convertible Promissory Note (the "Note") by the registered holder hereof (the "Registered Holder" or "Holder") at the office of the Company, the principal amount of \$1,500,000 ("Principal Amount"), together with the accrued and unpaid interest thereon and other sums as hereinafter provided, subject to the terms and conditions as set forth below. The effective date of execution and issuance of this Note is September 18, 2020 ("Original Issue Date").

1. **Schedule for Payment of Principal and Interest.** The Principal Amount outstanding hereunder, along with all accrued and unpaid interest shall be paid in one lump sum payment on or before May 10, 2021 (the "Maturity Date"). All interest on the Principal Amount outstanding hereunder shall be payable at the rate of 6% per annum and shall be due and payable on the Maturity Date. Accrual of interest on the outstanding Principal Amount, shall commence on the date of receipt of funds by the Company and shall continue until payment in full of the outstanding Principal Amount has been made hereunder. The principal and interest so payable will be paid to the person whose name is registered on the records of the Company regarding registration and transfers of this Note (the "Note Register").

2. **Payment.** Payment of any sums due to the Holder under the terms of this Note shall be made in United States Dollars by check or wire transfer at the option of the Company. Payment shall be made at the address last appearing on the Note Register of the Company as designated in writing by the Holder hereof from time to time. If any payment hereunder would otherwise become due and payable on a day on which commercial banks in Plano, Texas, are permitted or required to be closed, such payment shall become due and payable on the next succeeding day on which commercial banks in Plano, Texas, are not permitted or required to be closed ("Business Day") and, with respect to payments of Principal Amount, interest thereon shall be payable at the then applicable rate during such extension, if any. The forwarding of such funds shall constitute a payment of outstanding principal and interest hereunder and shall satisfy and discharge the liability for principal and interest on this Note to the extent of the sum represented by such payment. Except as provided in Section 3 hereof, this Note may not be prepaid without the prior written consent of the Holder.

3. **Company's Option to Redeem Note.** On or after the Original Issue Date, up to 100%, in whole or in part, of the outstanding Principal Amount of the Note, plus any accrued and unpaid interest, will be subject to redemption at the option of the Company. Additionally, the Company shall pay the Holder all unpaid interest on the portion of the Principal Amount redeemed that would have been earned from the Redemption Payment Date (as defined below) through the Maturity Date. Any amount of the Note subject to redemption, as set forth herein (the "**Redemption Amount**"), may be redeemed by the Company at any time and from time to time, upon not less than 10 nor more than 30 days notice to the Holder. The Company shall deliver to the Holder a written Notice of Redemption (the "**Notice of Redemption**") specifying the date for the redemption (the "**Redemption Payment Date**"), which date shall be at least 10 but not more than 30 days after the date of the Notice of Redemption (the "**Redemption Period**"). A Notice of Redemption shall not be effective with respect to any portion of this Note for which the Holder has previously delivered a Notice of Conversion (as defined in Section 4(b) below) or for conversions elected to be made by the Holder pursuant to Section 4 during the Redemption Period. The Redemption Amount shall be determined as if the Holder's conversion elections had been completed immediately prior to the date of the Notice of Redemption. On the Redemption Payment Date, the Redemption Amount must be paid in good funds to the Holder.

4. **Conversion Rights.**

(a) **Conversion.** If (i) the Company and Meta (as defined in Section 21) do not enter into a Definitive Agreement (as defined in Section 21) by the later of October 15, 2020 or such later date that is agreed to by the Company and Meta in writing, or (ii) the Company and Meta enter into a Definitive Agreement but the Transaction (as defined in Section 21) is terminated prior to closing or otherwise does not close by the Maturity Date of this Note, then at such time and until the Maturity Date, the Holder of this Note will have the right, at the Holder's option, to convert up to \$500,000 of the remaining Principal Amount, plus all unpaid interest accrued under the Note (see Section 21(c)), into shares of common stock, par value \$.001 per share, of the Company ("**Common Stock**"). Any such conversion under this paragraph will occur in the manner and in accordance with Section 4(b) below (unless earlier paid or redeemed) at the conversion price as set forth below in Section 4(c) (subject to adjustment as described herein). The right to convert the Principal Amount or interest thereon of this Note called for redemption will terminate at the close of business on the Business Day prior to the Redemption Payment Date for such Note, unless the Company subsequently fails to pay the applicable Redemption Amount. The shares of Common Stock to be issued upon conversion under this Section 4 are hereinafter referred to as the "**Conversion Shares**".

(b) **Mechanics of Holder's Conversion.** In the event that the Holder elects to convert any portion of this Note into Common Stock, the Holder shall give notice of such election by delivering an executed and completed notice of conversion ("**Notice of Conversion**") to the Company. The Notice of Conversion will provide a breakdown in reasonable detail of the Principal Amount and/or accrued interest that is being converted and state the denominations in which such Holder wishes the certificate or certificates for the Conversion Shares to be issued. The Registered Holder must surrender this Note to the Company with the Notice of Conversion, unless such Notice of Conversion is only for accrued interest and no Principal Amount. On each Conversion Date (as hereinafter defined) and in accordance with its Notice of Conversion, the Company shall make the appropriate reduction to the Principal Amount and/or accrued interest as entered in its records and shall provide written notice thereof to the Holder within five (5) Business Days after the Conversion Date. Each date on which a Notice of Conversion is delivered or telecopied to the Company in accordance with the provisions hereof shall be deemed a Conversion Date (the "**Conversion Date**"). Pursuant to the terms of the Notice of Conversion, the Company will issue instructions to its transfer agent as soon as practicable thereafter, to cause to be issued and delivered to the Holder certificates for the number of full shares of Conversion Shares to which such Holder shall be entitled as aforesaid and, if necessary, the Company shall cause to be issued and delivered to the Holder a new promissory note representing any unconverted portion of this Note. The Company shall not issue fractional Conversion Shares upon conversion, and the number of Conversion Shares to be received by any Holder upon conversion shall be rounded down to the next whole number. In the case of the exercise of the conversion rights set forth herein the conversion privilege shall be deemed to have been exercised and the Conversion Shares issuable upon such conversion shall be deemed to have been issued upon the date of receipt by the Company of the Notice of Conversion. The Holder shall be treated for all purposes as the record holder of the Conversion Shares, unless the Holder provides the Company written instructions to the contrary.

(c) Conversion Price. The Conversion Price of the Common Stock into which the Principal Amount, or the then outstanding interest due thereon, of this Note is convertible shall be \$0.375 per share (subject to adjustment as described herein).

(d) Adjustment Provisions. The Conversion Price and number and kind of shares or other securities to be issued upon conversion pursuant to this Note shall be subject to adjustment from time to time upon the happening of certain events while this conversion right remains outstanding, as follows:

(i) Reclassification. In case of any reclassification, consolidation or merger of the Company with or into another entity or any merger of another entity with or into the Company, or in the case of any sale, transfer or conveyance of all or substantially all of the assets of the Company (computed on a consolidated basis), each Note then outstanding will, without the consent of any Holder, become convertible only into the kind and amount of securities, cash or other property receivable upon such reclassification, consolidation, merger, sale, transfer or conveyance by a Holder of the number of shares of Common Stock into which such Note was convertible immediately prior thereto, after giving effect to any adjustment event.

(ii) Stock Split, Dividend. If the number of shares of Common Stock outstanding at any time after the date hereof is increased by a subdivision or split of Common Stock, or by the declaration of a dividend on the Common Stock, which dividend is wholly or partially in the form of additional shares of Common Stock or any other securities of the Company, then immediately after the effective date of such subdivision or split-up, or the record date with respect to such dividend, as the case may be, the Conversion Price shall be appropriately reduced so that the holder of this Note thereafter exchanged shall be entitled to receive the percentage of shares of Common Stock which such holder would have owned immediately following such action had this Note been exchanged immediately prior thereto;

(iii) Reverse Split. If the number of Common Stock outstanding at any time after the date hereof is decreased by a combination of the outstanding Common Stock or reverse split, then, immediately after the effective date of such combination, the Conversion Price shall be appropriately increased so that the holder of this Note thereafter exchanged shall be entitled to receive the percentage of shares of Common Stock which such holder would have owned immediately following such action had this Note been exchanged immediately prior thereto.

(e) **Issuance of New Note.** Upon any partial conversion of this Note, a new promissory note containing the same date and provisions of this Note shall be issued by the Company to the Holder for the principal balance of this Note and interest which shall not have been converted or paid. The Holder shall not pay any costs, fees or any other consideration to the Company for the production and issuance of a new promissory note.

(f) **Reservation of Shares.** The Company shall at all times reserve for issuance and maintain available, out of its authorized but unissued Common Stock, solely for the purpose of effecting the full conversion of the Note, the full number of shares of Common Stock deliverable upon the conversion of the Note from time to time outstanding. The Company shall from time to time (subject to obtaining necessary director and stockholder action), in accordance with the laws of the State of Nevada, increase the authorized number of shares of its Common Stock if at any time the authorized number of shares of its Common Stock remaining unissued shall not be sufficient to permit the conversion of the Note.

5. **Required Conversion.** On or after the Original Issue Date, if the Transaction (as defined in Section 21) closes, then 100% of the outstanding Principal Amount of the Note will automatically convert immediately prior to such closing. The Conversion Shares subject to such required conversion are hereinafter referred to as the "**Required Conversion Shares**".

At least 3 Business Days prior to the Transaction closing, the Company must deliver to the Registered Holder a written notice of required conversion (the "**Notice of Required Conversion**"). The Notice of Required Conversion will provide the date of closing of the Transaction and a breakdown in reasonable detail of the Principal Amount and interest that is being converted. The date of closing of the Transaction is deemed the "**Required Conversion Date**," on which date and in accordance with its Notice of Required Conversion, the Company shall make the appropriate reduction to the Principal Amount and interest as entered in its records. The Registered Holder must surrender this Note to the Company within 1 Business Day of receipt of the Notice of Required Conversion. Pursuant to the terms of the Notice of Required Conversion, the Company will issue instructions to its transfer agent to cause to be issued and delivered to the Holder certificates for the number of full shares of Required Conversion Shares to which such Holder shall be entitled as aforesaid. The Company shall not issue fractional Required Conversion Shares upon conversion, and the number of Required Conversion Shares to be received by any Holder upon conversion shall be rounded down to the next whole number. In the case of the required conversion set forth herein, the conversion shall be deemed to have been effected and the Required Conversion Shares issuable upon such conversion shall be deemed to have been issued upon the Required Conversion Date. If the closing of the Transaction does not occur (for any reason) after the Notice of Required Conversion is delivered, the Company shall provide Holder notice of the cancellation of the subject required conversion hereunder and will return the Note to the Holder as soon as practicable, and the Holder will return the Required Conversion Shares to the Company (if issued) as soon as practicable.

6. **Representations and Warranties of the Company.** The Company represents and warrants to the Holder that:

(a) **Organization.** The Company is validly existing and in good standing under the laws of the state of Nevada and has the requisite power to own, lease and operate its properties and to carry on its business as now being conducted. The Company is duly qualified to do business and is in good standing in each jurisdiction in which the character or location of the properties owned or leased by the Company or the nature of the business conducted by the Company makes such qualification necessary or advisable, except where the failure to do so would not have a material adverse effect on the Company.

(b) **Power and Authority.** The Company has the requisite power to execute, deliver and perform this Note, and to consummate the transactions contemplated hereby. The execution and delivery of this Note by the Company and the consummation of the transactions contemplated hereby have been duly authorized by all necessary corporate action on the part of the Company. This Note has been duly executed and delivered by the Company and constitutes a legal, valid and binding obligation of the Company and is enforceable against the Company in accordance with its terms except (i) that such enforcement may be subject to bankruptcy, insolvency, moratorium or similar laws affecting creditors' rights and (ii) that the remedy of specific performance and injunctive and other forms of equitable relief are subject to certain equitable defenses and to the discretion of the court before which any proceedings therefor may be brought.

(c) **Approvals.** No authorization, approval or consent of any court, governmental body, regulatory agency, self-regulatory organization, or stock exchange or market is required to be obtained by the Company for the issuance and sale of the Note and common stock as contemplated by this Note, except such authorizations, approvals and consents that have been obtained.

7. **Events of Defaults and Remedies.** The following are deemed to be an event of default ("**Event of Default**") hereunder: (i) the failure by the Company to pay any installment of interest on this Note as and when due and payable and the continuance of any such failure for 10 days; (ii) the failure by the Company to pay all or any part of the principal on this Note when and as the same become due and payable as set forth above, at maturity, by acceleration or otherwise; (iii) the failure of the Company to perform any conversion of the Note required under this Note and the continuance of any such failure for 10 days; (iv) the failure by the Company to observe or perform any covenant or agreement contained in this Note and the continuance of such failure for a period of 30 days after the written notice is given to the Company; (v) the assignment by the Company for the benefit of creditors, or an application by the Company to any tribunal for the appointment of a trustee or receiver of a substantial part of the assets of the Company, or the commencement of any proceedings relating to the Company under any bankruptcy, reorganization, arrangement, insolvency, readjustment of debts, dissolution or other liquidation law of any jurisdiction; or the filing of such application, or the commencement of any such proceedings against the Company and an indication of consent by the Company to such proceedings, or the appointment of such trustee or receiver, or an adjudication of the Company bankrupt or insolvent, or approval of the petition in any such proceedings, and such order remains in effect for 60 days; (vi) the declaration of an event of default or default, occurring after the Original Issue Date, under any other contract, agreement, debt or obligation of the Company with a monetary amount in excess of \$1,000,000; or (vii) the entry of a judgment against the Company, which is not otherwise appealable, or for which all appeals have been exhausted and for which the Company has not posted a bond to satisfy the amount of the judgment in excess of \$2,500,000.

8. **The Holder's Rights and Remedies upon the Occurrence of an Event of Default** If any Event of Default occurs and is not otherwise cured, and the Holder shall have provided written notice to the Company, that the full unpaid principal amount of this Note, together with interest owing in respect thereof, is immediately due and payable, time being of the essence, and said principal sum shall bear interest from the date of the Event of Default at the rate per annum 4% in excess of the applicable rate of interest provided in Section 1 (subject to Section 21(c) of this Note). Failure to exercise this option shall not constitute a waiver of the right to exercise the same in the event of a subsequent Event of Default. If the Note for which the then outstanding principal amount, together with interest owing in respect thereof, shall have been paid in accordance herewith, the Note shall promptly be surrendered to or as directed by the Company.

9. **Limitation on Merger, Sale or Consolidation.** The Company may not, directly or indirectly, consolidate with or merge into another person or sell, lease, convey or transfer all or substantially all of its assets (computed on a consolidated basis), whether in a single transaction or a series of related transactions, to another person or group of affiliated persons, unless either (i) in the case of a merger or consolidation, the Company is the surviving entity or (ii) the resulting, surviving or transferee entity expressly assumes by supplemental agreement all of the obligations of the Company in connection with the Note. Upon any consolidation or merger or any transfer of all or substantially all of the assets of the Company in accordance with the foregoing, the successor entity formed by such consolidation or into which the Company is merged or to which such transfer is made, shall succeed to, and be substituted for, and may exercise every right and power of the Company under the Note with the same effect as if such successor entity had been named therein as the Company, and the Company will be released from its obligations under the Note, except as to any obligations that arise from or as a result of such transaction.

10. **Listing of Registered Holder of Note.** This Note will be registered as to principal amount in the Holder's name on the books of the Company at its principal office in Plano, Texas (the "Note Register"), after which no transfer hereof shall be valid unless made on the Company's books at the office of the Company, by the Holder hereof, in person, or by attorney duly authorized in writing, and similarly noted hereon.

11. **Registered Holder Not Deemed a Stockholder.** No Holder, as such, of this Note shall be entitled to vote or receive dividends or be deemed the holder of shares of the Company for any purpose, nor shall anything contained in this Note be construed to confer upon the Holder hereof, as such, any of the rights of a stockholder of the Company or any right to vote, give or withhold consent to any corporate action (whether any reorganization, issue of stock, reclassification of stock, consolidation, merger, conveyance or otherwise), receive notice of meetings, receive dividends or subscription rights, or otherwise.

12. **Waiver of Demand, Presentment, Etc.** The Company hereby expressly waives demand and presentment for payment, notice of nonpayment, protest, notice of protest, notice of dishonor, notice of acceleration or intent to accelerate, bringing of suit and diligence in taking any action to collect amounts called for hereunder and shall be directly and primarily liable for the payment of all sums owing and to be owing hereunder, regardless of and without any notice, diligence, act or omission as or with respect to the collection of any amount called for hereunder.

13. **Attorney's Fees.** The Company agrees to pay all costs and expenses, including without limitation reasonable attorney's fees, which may be incurred by the Holder in collecting any amount due under this Note.

14. **Enforceability.** In case any provision of this Note is held by a court of competent jurisdiction to be excessive in scope or otherwise invalid or unenforceable, such provision shall be adjusted rather than voided, if possible, so that it is enforceable to the maximum extent possible, and the validity and enforceability of the remaining provisions of this Note will not in any way be affected or impaired thereby.

15. **Intent to Comply with Usury Laws.** In no event will the interest to be paid on this Note exceed the maximum rate provided by law. It is the intent of the parties to comply fully with the usury laws of the State of Texas; accordingly, it is agreed that notwithstanding any provisions to the contrary in this Note, in no event shall such Note require the payment or permit the collection of interest (which term, for purposes hereof, shall include any amount which, under Texas law, is deemed to be interest, whether or not such amount is characterized by the parties as interest) in excess of the maximum amount permitted by the laws of the State of Texas. If any excess of interest is unintentionally contracted for, charged or received under this Note, or in the event the maturity of the indebtedness evidenced by the Note is accelerated in whole or in part, or in the event that all or part of the Principal Amount or interest of this Note shall be prepaid, so that the amount of interest contracted for, charged or received under this Note, on the amount of the Principal Amount actually outstanding from time to time under this Note shall exceed the maximum amount of interest permitted by the applicable usury laws, then in any such event (i) the provisions of this paragraph shall govern and control, (ii) neither the Company nor any other person or entity now or hereafter liable for the payment thereof, shall be obligated to pay the amount of such interest to the extent that it is in excess of the maximum amount of interest permitted by such applicable usury laws, (iii) any such excess which may have been collected shall be either applied as a credit against the then unpaid principal amount thereof or refunded to the Company at the Holder's option, and (iv) the effective rate of interest shall be automatically reduced to the maximum lawful rate of interest allowed under the applicable usury laws as now or hereafter construed by the courts having jurisdiction thereof. It is further agreed that without limitation of the foregoing, all calculations of the rate of interest contracted for, charged or received under the Note which are made for the purpose of determining whether such rate exceeds the maximum lawful rate of interest, shall be made, to the extent permitted by applicable laws, by amortizing, prorating, allocating and spreading in equal parts during the period of the full stated term of the Note evidenced thereby, all interest at any time contracted for, charged or received from the Company or otherwise by the Holders in connection with this Note.

16. **Governing Law; Consent to Jurisdiction.** This Note shall be governed by and construed in accordance with the laws of the State of Texas without regard to the conflict of laws provisions thereof. In any action between or among any of the parties, whether arising out of this Note or otherwise, each of the parties irrevocably consents to the exclusive jurisdiction and venue of the federal and/or state courts located in Collin County, Texas.

17. **Amendment and Waiver.** Any waiver or amendment hereto shall be in writing signed by the Holder. No failure on the part of the Holder to exercise, and no delay in exercising, any right hereunder shall operate as a waiver thereof, nor shall any single or partial exercise by the Holder of any right hereunder preclude any other or further exercise thereof or the exercise of any other rights. The remedies herein provided are cumulative and not exclusive of any other remedies provided by law.

18. **Restrictions Against Transfer or Assignment.** Neither this Note nor any of the shares issuable in connection with this Note may be sold, transferred, assigned, pledged, hypothecated or otherwise disposed of by the Registered Holder hereof, in whole or in part, unless and until either (i) the Note or the shares issuable in connection with the Note have been duly and effectively registered for resale under the Securities Act of 1933, as amended, and under any then applicable state securities laws; or (ii) the Registered Holder delivers to the Company a written opinion acceptable to the Company's counsel that an exemption from such registration requirements is then available with respect to any such proposed sale or disposition. Any transfer of this Note otherwise permissible hereunder shall be made only at the principle office of the Company upon surrender of this Note for cancellation and upon the payment of any transfer tax or other government charge connected therewith, and upon any such transfer a new Note will be issued to the transferee in exchange therefor.

19. **Entire Agreement; Headings.** This Note constitutes the entire agreement between the Holder and the Company pertaining to the subject matter hereof and supersedes all prior and contemporaneous agreements, representations and understandings, written or oral, of such parties. The headings are for reference purposes only and shall not be used in construing or interpreting this Note.

20. **Notices.** Any notices or other communications required or permitted hereunder shall be sufficiently given if in writing and delivered in person, or sent by registered or certified mail (return receipt requested) or recognized overnight delivery service, postage pre-paid, or sent by email addressed as follows, or to such other address as such party may notify to the other parties in writing:

(a) If to the Company, to it at the following address:

5700 Plano Parkway, Ste. 3600
Plano, Texas 75093
Attn: John Brda, President
Email: john@torchlightenergy.com

(b) If to Registered Holder, then to the address listed on the front of this Note, unless changed, by notice in writing as provided for herein.

A notice or communication will be effective (i) if delivered in person or by overnight courier, on the Business Day it is delivered, (ii) if sent by registered or certified mail, the earlier of the date of actual receipt by the party to whom such notice is required to be given or three (3) days after deposit in the United States mail and (iii) if sent by email, on the date sent. If any notice or other communication is sent by email, the party providing such notice shall, no later than the next business day after such emailed notice is sent, send a written notice by registered or certified mail (return receipt requested) or recognized overnight delivery service, postage pre-paid.

21. **Use of Proceeds and Security.**

(a) **Business Combination Transaction.** The Company and Metamaterial Inc., an Ontario business corporation (“**Meta**”), are presently negotiating a business combination between the Company and Meta through a merger or other transaction (the “**Transaction**”), which Transaction will be effected under the terms and conditions of a definitive agreement between such parties (the “**Definitive Agreement**”).

(b) **Use of Proceeds.** In connection with the proposed Transaction, the Company shall use the net proceeds from the funds received under this Note as follows:

i. The Company will lend \$500,000 to Meta pursuant to an 8% Unsecured Convertible Promissory Note (the “**First Meta Note**”);

ii. The Company will retain and use \$500,000 for general corporate purposes, including without limitation, expenses incurred by the Company in connection with the Transaction; and

iii. The Company will deposit \$500,000 into an escrow account, to be held in escrow for the benefit of the Company. If the Company and Meta enter into a Definitive Agreement by the later of October 15, 2020 or such later date that is agreed to by the Company and Meta in writing, the \$500,000 from this escrow account will be released to the Company, and the Company will lend this \$500,000 to Meta pursuant to another 8% Unsecured Convertible Promissory Note (the “**Second Meta Note**”). If the Company and Meta do not enter into a Definitive Agreement by the later of October 15, 2020 or such later date that is agreed to by the Company and Meta in writing, the \$500,000 from this escrow account will be released to the Holder and deducted from the Principal Amount outstanding under this Note.

(c) **Security.** This Note is secured by the Company's pledge of the First Meta Note and the Second Meta Note (if issued). If the Company and Meta do not enter into a Definitive Agreement by the later of October 15, 2020 or such later date that is agreed to by the Company and Meta in writing, then promptly after that date, the Company will assign to the Holder of this Note the First Meta Note in full repayment and discharge of \$500,000 of the Principal Amount of this Note, and the remaining \$500,000 of the Principal Amount, plus all unpaid interest accrued under the Note, will remain subject to this Note. If a Definitive Agreement is entered into by the later of October 15, 2020 or such later date that is agreed to by the Company and Meta in writing, but the Transaction is terminated prior to closing or otherwise does not close by the Maturity Date of this Note, then the Company will assign to the Holder of this Note both the First Meta Note and Second Meta Note in full repayment and discharge of \$1,000,000 of the Principal Amount of this Note, and the remaining \$500,000 of the Principal Amount, plus all unpaid interest accrued under the Note, will remain subject to this Note.

22. **Survival.** The representations, warranties, obligations and covenants of the Company shall survive execution of this Note.

IN WITNESS WHEREOF, Torchlight Energy Resources, Inc. has caused this Note to be duly executed in its corporate name by the manual signature of its President/CEO.

TORCHLIGHT ENERGY RESOURCES, INC.

By: /s/ John Brda
John Brda, President/CEO

6% Secured Convertible Promissory Note
Page 10 of 12

ANNEX A

NOTICE OF CONVERSION

The undersigned hereby elects to convert principal and/or interest under the 6% Secured Convertible Promissory Note due May 10, 2021 of Torchlight Energy Resources, Inc., a Nevada corporation (the "Company"), into shares of common stock, \$0.001 par value per share, (the "Common Stock") of the Company, according to the conditions hereof, as of the date written below. No fee will be charged to the Holder for any conversion.

Conversion Calculations:

Date to Effect Conversion:

Principal Amount of 6% Secured Convertible Promissory Note to be Converted:

Interest Amount of 6% Secured Convertible Promissory Note to be Converted:

Number of Shares of Common Stock to be Issued:

If Holder is a Natural Person:

Print Name: _____

Signature: _____

Print Name (if joint investment): _____

Signature: _____

Telephone No. _____

E-mail Address: _____

Street Address _____

City, State, Zip _____

If Holder is an Entity:

Print Name of Entity: _____

Signature: _____

Print Name of Signatory: _____

Title: _____

Telephone No. _____

E-mail Address: _____

Street Address _____

City, State, Zip _____

FORM OF ASSIGNMENT

FOR VALUE RECEIVED, _____ hereby sells, assigns and transfers to each assignee set forth below all of the rights of the undersigned under the attached 6% Secured Convertible Promissory Note (the "Note") with respect to the principal amount of the Note (plus interest thereon) covered thereby as set forth opposite the name of such assignee:

<u>Name of Assignee</u>	<u>Address</u>	<u>Principal Amount of Note Assigned</u>
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If the total principal amount of the Note shall not be assigned, the undersigned requests that a new Note evidencing the balance of the principal amount due and owing on the Note not so assigned be issued in the name of and delivered to the undersigned.

Dated: _____ Name of Holder (Print): _____

(Signature of Holder)

AMENDMENT TO PROMISSORY NOTE

THIS AMENDMENT TO PROMISSORY NOTE (“Amendment”) dated as of September 22, 2020, is to become affixed to, modify and become a part of that certain 6% Secured Convertible Promissory Note in the original principal sum of \$1,500,000 dated as of September 18, 2020 (“Original Issue Date”), and which promissory note (the “Note”) was made and executed by **Torchlight Energy Resources, Inc.**, a Nevada corporation (the “Debtor”), and payable to the order of **McCabe Petroleum Corporation** (the “Holder”), which Note is due and payable on May 10, 2021 (“Maturity Date”).

WHEREAS, of the Holder and Debtor desire to amend the Note; and

NOW, THEREFORE, in consideration of the premises, the mutual covenants and agreements and the respective representations and warranties herein contained, and on the terms and subject to the conditions herein set forth, the parties hereto, intending to be legally bound, hereby agree as follows:

1. The Note is amended and modified by amending section 4(a) of the Note so that reference to “October 15, 2020” is changed to “November 2, 2020.”
2. The Note is amended and modified by amending and restating in its entirety the first paragraph of section 5 as follows:

“On or after the Original Issue Date, if the Transaction (as defined in Section 21) closes, then 100% of the outstanding Principal Amount of the Note, and all accrued and unpaid interest thereon, will automatically convert immediately prior to such closing, into shares of Common Stock at the Conversion Price. The shares subject to such required conversion are hereinafter referred to as the **“Required Conversion Shares.”**”

3. The Note is amended and modified by amending section 21(b)(iii) of the Note so that references to “October 15, 2020” are changed to “November 2, 2020.”
4. The Note is amended and modified by amending and restating in its entirety section 21(c) as follows:

“Security. This Note is secured by the Company’s pledge of the First Meta Note and the Second Meta Note (if issued). If the Company and Meta do not enter into a Definitive Agreement by the later of November 2, 2020 or such later date that is agreed to by the Company and Meta in writing, then promptly after that date, the Company will assign to the Holder of this Note the First Meta Note in full repayment and discharge from the Principal Amount of this Note an amount equal to \$500,000 plus all accrued and unpaid interest under the First Meta Note, and the remaining \$500,000 (less an amount equal to the accrued and unpaid interest under the First Meta Note) of the Principal Amount, plus all unpaid interest accrued under this Note, will remain subject to this Note. If a Definitive Agreement is entered into by the later of November 2, 2020 or such later date that is agreed to by the Company and Meta in writing, but the Transaction is terminated prior to closing or otherwise does not close by the Maturity Date of this Note, then the Company will assign to the Holder of this Note both the First Meta Note and Second Meta Note in full repayment and discharge from the Principal Amount of this Note an amount equal to \$1,000,000 plus all accrued and unpaid interest under the First Meta Note and Second Meta Note, and the remaining \$500,000 (less an amount equal to the accrued and unpaid interest under the First Meta Note and Second Meta Note) of the Principal Amount, plus all unpaid interest accrued under this Note, will remain subject to this Note.”

5. All terms and conditions of the Note shall, except as amended and modified by this Amendment, will remain in full force and effect and all rights, duties, obligations and responsibilities of the Debtor and the Holder shall be governed and determined by the Note as the same has been amended and modified by this Amendment.

6. THIS AMENDMENT IS TO BE CONSTRUED UNDER THE LAWS OF THE STATE OF TEXAS.

7. This Amendment shall be of no force and effect until receipt and execution of it by the Debtor and the Holder. This Amendment may be executed in counterparts, each of which shall be deemed an original, but all of which shall be deemed one instrument, by facsimile signature or by e-mail delivery of a “.pdf” format data file signature of any of the parties, each of which shall be deemed an original for all purposes.

IN WITNESS WHEREOF, each of the undersigned has executed and delivered this Amendment to the Note as of the date first written above.

DEBTOR:

TORCHLIGHT ENERGY RESOURCES, INC.

By: /s/ John Brda

John Brda, President/CEO

HOLDER:

MCCABE PETROLEUM CORPORATION

By: /s/ Greg McCabe

Printed Name: Greg McCabe

Title: President

CERTIFICATION PURSUANT TO SECTION 302 OF THE
SARBANES-OXLEY ACT OF 2002

I, John A. Brda, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Torchlight Energy Resources, Inc. for the period ended September 30, 2020;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the small business issuer, including its consolidated subsidiary, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, 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;
 - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures, and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's fourth quarter that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over the financial reporting; and
5. I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

/s/ John A. Brda

John A. Brda
Chief Executive Officer
(Principal Executive Officer)
Date: November 9, 2020

CERTIFICATION PURSUANT TO SECTION 302 OF THE
SARBANES-OXLEY ACT OF 2002

I, Roger Wurtele, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Torchlight Energy Resources, Inc. for the period ended September 30, 2020;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the small business issuer, including its consolidated subsidiary, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, 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;
 - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures, and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's fourth quarter that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over the financial reporting; and
5. I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

/s/ Roger Wurtele

Roger Wurtele,
Chief Financial Officer
(Principal Financial Officer)
Date: November 9, 2020

CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO SECTION 906
OF THE SARBANES-OXLEY ACT OF 2002

I, John A. Brda, certify pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that the quarterly report on Form 10-Q of Torchlight Energy Resources, Inc. for the period ended September 30, 2020, fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 and that information contained in such quarterly report on Form 10-Q fairly presents, in all material respects, the financial condition and results of operations of Torchlight Energy Resources, Inc.

/s/ John A. Brda

John A. Brda,
Chief Executive Officer (Principal Executive Officer)

Date: November 9, 2020

I, Roger Wurtele, certify pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that the quarterly report on Form 10-Q of Torchlight Energy Resources, Inc. for the period ended September 30, 2020, fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 and that information contained in such quarterly report on Form 10-Q fairly presents, in all material respects, the financial condition and results of operations of Torchlight Energy Resources, Inc.

/s/ Roger Wurtele

Roger Wurtele,
Chief Financial Officer (Principal Financial Officer)

Date: November 9, 2020

The foregoing certification is not deemed filed with the Securities and Exchange Commission for purposes of Section 18 of the Securities Exchange Act of 1934, as amended ("Exchange Act"), and is not to be incorporated by reference into any filing of Torchlight Energy Resources, Inc. under the Securities Act of 1933, as amended, or the Exchange Act, whether made before or after the date hereof, regardless of any general incorporation language in such filing.
