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

FORM 10-Q

(Mark One)

☒ QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15 (d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended May 31, 2021

OR

☐ TRANSITION REPORT PURSUANT TO SECTION 13 OR 15 (d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from ______________ to _______________

Commission File Number: 000-50107

DAYBREAK OIL AND GAS, INC.

(Exact name of registrant as specified in its charter)

Washington	**91-0626366**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
1101 N. Argonne Road, Suite A 211, Spokane Valley, WA	**99212**
(Address of principal executive offices)	(Zip code)

(509) 232-7674
(Registrant's telephone number, including area code)

(Former name, former address and former fiscal year, if changed since last report)

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

Title of each class	Trading Symbol(s)	Name of each exchange on which registered
n/a	n/a	n/a

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 and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit 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. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act.

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

At July 14, 2021 the registrant had 60,491,122 outstanding shares of $0.001 par value common stock.

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PART I
FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

DAYBREAK OIL AND GAS, INC.
Balance Sheets – Unaudited

		As of May 31, 2021		As of February 28, 2021
ASSETS				
CURRENT ASSETS:				
Cash and cash equivalents	$	112,723	$	33,528
Accounts receivable:				
Crude oil sales		94,690		108,993
Joint interest participants		51,029		79,411
Prepaid expenses and other current assets		33,817		61,307
Total current assets		292,259		283,239
LONG-TERM ASSETS:				
Crude oil properties, successful efforts method, net				
Proved properties		546,288		556,456
Unproved properties		55,978		55,978
Prepaid drilling costs		16,452		16,452
Vehicles and equipment, net		7,975		—
Total long-term assets		626,693		628,886
Total assets	$	918,952	$	912,125
LIABILITIES AND STOCKHOLDERS' DEFICIT				
CURRENT LIABILITIES:				
Accounts payable and other accrued liabilities	$	1,707,919	$	1,710,922
Accounts payable – related parties		1,023,004		988,966
Accrued interest		136,186		123,659
Note Payable		120,000		120,000
Note payable - related party, current, net of unamortized discount of $729 and $728, respectively		7,927		7,870
12% Notes payable		315,000		315,000
12% Notes payable – related party		250,000		250,000
Production revenue payable, current, net of unamortized discount		98,336		111,753
Line of credit		832,796		840,904
Total current liabilities		4,491,168		4,469,074
LONG TERM LIABILITIES:				
Paycheck protection program (PPP) second-draw loan		72,800		—
Note payable - related party, net of current portion and net unamortized discount of $9,897 and $10,080, respectively		133,457		135,460
Production revenue payable, net of unamortized discount and current portion		1,435,611		1,391,669
Asset retirement obligation		34,233		33,062
Total long-term liabilities		1,676,101		1,560,191
Total liabilities		6,167,269		6,029,265
COMMITMENTS AND CONTINGENCIES				
STOCKHOLDERS' DEFICIT:				
Preferred stock - 10,000,000 shares authorized, $0.001 par value;		—		—
Series A Convertible Preferred stock – 2,400,000 shares authorized, $0.001 par value, 6% cumulative dividends; 709,568 shares issued and outstanding, respectively		710		710
Common stock – 200,000,000 shares authorized; $0.001 par value, 60,491,122 shares issued and outstanding, respectively		60,491		60,491
Additional paid-in capital		24,252,030		24,250,556
Accumulated deficit		(29,561,548)		(29,428,897)
Total stockholders' deficit		(5,248,317)		(5,117,140)
Total liabilities and stockholders' deficit	$	918,952	$	912,125

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

DAYBREAK OIL AND GAS, INC.
Statements of Operations – Unaudited

		Three Months Ended May 31, 2021		Three Months Ended May 31, 2020
REVENUE:				
Crude oil sales	$	147,300	$	69,199
OPERATING EXPENSES:				
Production		46,726		39,195
Depreciation, depletion and amortization		13,948		14,159
General and administrative		167,625		152,369
Total operating expenses		228,299		205,723
OPERATING LOSS		(80,999)		(136,524)
OTHER EXPENSE:				
Gain on asset disposal		9,614		—
Interest expense, net		(61,266)		(60,473)
NET LOSS		(132,651)		(196,997)
Cumulative convertible preferred stock dividend requirement		(32,191)		(32,191)
NET LOSS AVAILABLE TO COMMON SHAREHOLDERS	$	(164,842)	$	(229,188)
NET LOSS PER COMMON SHARE – Basic and diluted	$	(0.003)	$	(0.004)
WEIGHTED AVERAGE NUMBER OF COMMON SHARES OUTSTANDING – Basic and diluted		60,491,122		53,532,364

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

DAYBREAK OIL AND GAS, INC.
Statements of Changes in Stockholders' Deficit - Unaudited
For the Three Months Ended May 31, 2021 and 2020

	Series A Convertible Preferred Stock		Common Stock		Additional Paid-In	Accumulated	
	Shares	Amount	Shares	Amount	Capital	Deficit	Total
BALANCE, FEBRUARY 28, 2021	709,568	$ 710	60,491,122	$ 60,491	$ 24,250,556	$ (29,428,897)	$ (5,117,140)
Recognition of warrants issued for:							
Investor relations services	—	—	—	—	1,474	—	1,474
Net loss	—	—	—	—	—	(132,651)	(132,651)
BALANCE, MAY 31, 2021	709,568	$ 710	60,491,122	$ 60,491	$ 24,252,030	$ (29,561,548)	$ (5,248,317)

	Series A Convertible Preferred Stock		Common Stock		Additional Paid-In	Accumulated	
	Shares	Amount	Shares	Amount	Capital	Deficit	Total
BALANCE, FEBRUARY 29, 2020	709,568	$ 710	53,532,364	$ 53,532	$ 24,223,783	$ (28,916,632)	$ (4,638,607)
Issuance of warrants issued for:							
Investor relations services	—	—	—	—	1,474	—	1,474
Net loss	—	—	—	—	—	(196,997)	(196,997)
BALANCE, MAY 31, 2020	709,568	$ 710	53,532,364	$ 53,532	$ 24,225,257	$ (29,113,629)	$ (4,834,130)

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

DAYBREAK OIL AND GAS, INC.
Statements of Cash Flows – Unaudited

	Three Months Ended	
	May 31, 2021	May 31, 2020
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net loss	$ (132,651)	$ (196,997)
Adjustments to reconcile net cash used in operating activities:		
Depreciation, depletion and ARO expense	13,948	14,159
Amortization of debt discount	30,707	31,970
Operating lease expense in conjunction with right of use asset	—	2,196
Warrant issued for investor relations services	1,474	1,474
Changes in assets and liabilities:		
Accounts receivable – crude oil sales	14,303	19,219
Accounts receivable - joint interest participants	28,382	(14,256)
Prepaid expenses and other current assets	27,490	22,383
Accounts payable and other accrued liabilities	26,229	(10,186)
Accounts payable - related parties	34,038	7,144
Operating lease liability change in conjunction with right of use asset	—	(2,196)
Accrued interest	19,419	19,813
Net cash provided by (used in) operating activities	63,339	(105,277)
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchase of vehicles and equipment	(8,500)	—
Additions to oil and gas properties	(2,084)	—
Net cash used in investing activities	(10,584)	—
CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds from paycheck protection program (PPP) loan	72,800	74,355
Insurance financing repayments	(29,232)	(16,960)
Payments to note payable – related party	(2,128)	—
Payments to line of credit	(15,000)	(15,000)
Net cash provided by financing activities	26,440	42,395
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	79,195	(62,882)
CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD	33,528	94,043
CASH AND CASH EQUIVALENTS AT END OF PERIOD	$ 112,723	$ 31,161
CASH PAID FOR:		
Interest	$ 4,169	$ 1,224
Income taxes	$ —	$ —
SUPPLEMENTAL CASH FLOW INFORMATION:		
Non-cash increase to line of credit due to monthly interest	$ 6,892	$ 7,389

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

DAYBREAK OIL AND GAS, INC.
NOTES TO UNAUDITED FINANCIAL STATEMENTS

NOTE 1 — ORGANIZATION AND BASIS OF PRESENTATION:

Organization

Originally incorporated as Daybreak Uranium, Inc., ("Daybreak Uranium") on March 11, 1955, under the laws of the State of Washington, Daybreak Uranium was organized to explore for, acquire, and develop mineral properties in the Western United States. In August 1955, the assets of Morning Sun Uranium, Inc. were acquired by Daybreak Uranium. In May 1964, Daybreak Uranium changed its name to Daybreak Mines, Inc. During 2005, management of the Company decided to enter the crude oil and natural gas exploration, development and production industry. On October 25, 2005, the Company shareholders approved a name change from Daybreak Mines, Inc. to Daybreak Oil and Gas, Inc. (referred to herein as "Daybreak" or the "Company") to better reflect the business of the Company.

All of the Company's crude oil production is sold under contracts which are market-sensitive. Accordingly, the Company's financial condition, results of operations, and capital resources are highly dependent upon prevailing market prices of, and demand for, crude oil. These commodity prices are subject to wide fluctuations and market uncertainties due to a variety of factors that are beyond the control of the Company. These factors may include the level of global demand for petroleum (hydrocarbon) products; foreign supply of crude oil and natural gas; the establishment of and compliance with production quotas by oil-exporting countries; the relative strength of the U.S. dollar; weather conditions; the price and availability of alternative fuels; overall economic conditions, both foreign and domestic; crude oil price disputes between OPEC and non-OPEC members; and national and international pandemics like the coronavirus outbreak.

Basis of Presentation

The accompanying unaudited interim financial statements and notes for the Company have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information and with the instructions to Form 10-Q for quarterly reports under Section 13 or 15 (d) of the Securities Exchange Act of 1934 (the "Exchange Act"). Accordingly, they do not include all of the information and footnote disclosures normally required by accounting principles generally accepted in the United States of America for complete financial statements.

In the opinion of management, all adjustments considered necessary for a fair presentation of the financial statements have been included and such adjustments are of a normal recurring nature. Operating results for the three months ended May 31, 2021 are not necessarily indicative of the results that may be expected for the fiscal year ending February 28, 2022.

These financial statements should be read in conjunction with the audited financial statements and notes thereto included in the Company's Annual Report on Form 10-K for the fiscal year ended February 28, 2021.

Use of Estimates

In preparing financial statements in conformity with accounting principles generally accepted in the United States of America, management is required to make estimates and assumptions. These estimates and assumptions may affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements, and revenues and expenses during the reporting period. Actual results could differ materially from those estimates. The accounting policies most affected by management's estimates and assumptions are as follows:

- The reliance on estimates of proved reserves to compute the provision for depreciation, depletion and amortization and to determine the amount of any impairment of proved properties;
- The valuation of unproved acreage and proved crude oil properties to determine the amount of any impairment of crude oil properties;
- Judgment regarding the productive status of in-progress exploratory wells to determine the amount of any provision for abandonment;
- Estimates regarding abandonment obligations; and
- Estimates regarding projected cash flows used in determining the production revenue payable discount.

Earnings per Share

The Company follows ASC Topic 260, *Earnings per Share*, to account for the earnings per share. Basic earnings per common share (“EPS”) calculations are determined by dividing net income (loss) by the weighted average number of shares of common stock outstanding during the period. Diluted earnings per common share calculations are determined by dividing net income (loss) by the weighted average number of common shares and dilutive common share equivalents outstanding. During periods when common stock equivalents, if any, are anti-dilutive they are not considered in the computation.

NOTE 2 — GOING CONCERN:

Financial Condition

The Company’s financial statements for the three months ended May 31, 2021 have been prepared on a going concern basis, which contemplates the realization of assets and the settlement of liabilities in the normal course of business. The Company has incurred net operating losses since entering the crude oil exploration industry and as of May 31, 2021 has an accumulated deficit of $29.6 million and a working capital deficit of $4.2 million, which raises substantial doubt about the Company’s ability to continue as a going concern.

Management Plans to Continue as a Going Concern

The Company continues to implement plans to enhance its ability to continue as a going concern. Daybreak currently has a net revenue interest (“NRI”) in 20 producing crude oil wells in its East Slopes Project located in Kern County, California (the “East Slopes Project”). The revenue from these wells has created a steady and reliable source of income for the Company. The Company’s average working interest in these wells is 36.6% and the average net revenue interest (“NRI”) is 28.4% for these same wells.

In December 2019, the 2019 novel coronavirus (“COVID-19") surfaced in Wuhan, China. The World Health Organization declared a global emergency on January 30, 2020, with respect to the outbreak and most countries throughout the world initiated travel restrictions to and from other countries. This widespread health crisis and the governmental restrictions associated with it, have adversely affected demand for crude oil, depressed crude oil prices, and affected our ability to access capital. These factors, in turn, have had a negative impact on our operations, and financial condition as evidenced by the unprecedented decline in crude oil prices and our revenues during this same time period.

On March 27, 2020, the Coronavirus Aid, Relief, and Economic Security Act commonly referred to as the CARES Act became law. One component of the CARES Act was the paycheck protection program (“PPP”) which provides small business with the resources needed to maintain their payroll and cover applicable overhead. The PPP is implemented by the Small Business Administration (“SBA”) with support from the Department of the Treasury. The Company applied for, and was accepted to participate in this program. On May 11, 2020, the Company received funding for approximately $74,355. In February 2021, the Company applied for full loan forgiveness and later that month was notified by our lender that the SBA had forgiven our original loan in full. On March 15, 2021, the Company received $72,800 in funding through the SBA second draw paycheck protection program. Second Draw PPP loans can be used to help fund payroll costs, including benefits. Funds can also be used to pay for mortgage interest, rent and utilities over a 24 week period. The Company plans on also applying for loan forgiveness on this PPP second draw loan.

The Company anticipates its revenue will continue to increase as the Company participates in the drilling of more wells in the East Slopes Project in California and as our exploratory drilling project begins in Michigan. However, given the current volatility and instability in hydrocarbon prices; the timing of any drilling activity in California and Michigan will be dependent on a sustained improvement in hydrocarbon prices and success in securing financing for its drilling programs.

The Company believes that its liquidity will improve when there is a sustained improvement in hydrocarbon prices. Daybreak’s sources of funds in the past have included the debt or equity markets and the sale of assets. It will be necessary for the Company to obtain additional funding from the private or public debt or equity markets in the future. However, the Company cannot offer any assurance that it will be successful in executing the aforementioned plans to continue as a going concern.

Daybreak’s financial statements as of May 31, 2021 do not include any adjustments that might result from the inability to implement or execute Daybreak’s plans to improve our ability to continue as a going concern.

NOTE 3 — CONCENTRATION OF CREDIT RISK:

Substantially all of the Company's trade accounts receivable consists of receivables from the sale of crude oil production from operations by the Company and receivables from the Company's working interest partners in crude oil projects in which the Company acts as Operator of the project. This concentration of customers and joint interest owners may impact the Company's overall credit risk, as these entities could be affected by similar changes in economic conditions including lower crude oil prices as well as other related factors. Trade accounts receivable are generally not collateralized.

At the Company's East Slopes project in California, there is only one buyer for the purchase of crude oil production. The Company has no natural gas production in California. At May 31, 2021 and February 28, 2021 this one customer represented 100.0% of crude oil sales receivable. If this buyer is unable to resell its products or if they lose a significant sales contract, the Company may incur difficulties in selling its crude oil production.

Crude oil sales receivables balances of $94,690 and $108,993 at May 31, 2021 and February 28, 2021, were from one customer, Plains Marketing; and represent crude oil sales that occurred in May and February 2021, respectively.

Joint interest participant receivables balances of $51,029 and $79,411 at May 31, 2021 and February 28, 2021, respectively, represent amounts due from working interest partners in California, where the Company is the Operator. There were no allowances for doubtful accounts for the Company's trade accounts receivable at May 31, 2021 and February 28, 2021, as the joint interest owners have a history of paying their obligations.

NOTE 4 — CRUDE OIL PROPERTIES:

Crude oil property balances at May 31, 2021 and February 28, 2021 are set forth in the table below.

	May 31, 2021	February 28, 2021
Proved leasehold costs	$ 115,119	$ 115,119
Costs of wells and development	2,294,008	2,291,924
Capitalized exploratory well costs	1,341,494	1,341,494
Cost of proved crude oil properties	3,750,621	3,748,537
Accumulated depletion, depreciation, amortization and impairment	(3,204,333)	(3,192,081)
Total proved crude oil properties, net	$ 546,288	$ 556,456
Unproved leasehold costs	55,978	55,978
Total proved and unproved crude oil properties, net	$ 602,266	$ 612,434

NOTE 5 — ACCOUNTS PAYABLE:

On March 1, 2009, the Company became the operator for its East Slopes Project located in Kern County, California. Additionally, the Company then assumed certain original defaulting partners' approximate $1.5 million liability representing a 25% working interest in the drilling and completion costs associated with the East Slopes Project four earning wells program. The Company subsequently sold the same 25% working interest on June 11, 2009. Of the original $1.5 million liability, approximately $244,849 remains unpaid and is included in the May 31, 2021 and February 28, 2021, accounts payable balance. Payment of this liability has been delayed until the Company's cash flow situation improves. On October 17, 2018, a working interest partner in California filed a UCC financing statement in regards to payables owed to the partner by the Company. At May 31, 2021 and February 28, 2021, the balance owed this working interest partner was $84,132 and $88,905, respectively, and is included in the approximate $1.71 million and $1.71 million accounts payable balances at May 31, 2021 and February 28, 2021, respectively.

NOTE 6 — RELATED PARTIES TRANSACTIONS:

The May 31, 2021 and February 28, 2021 accounts payable – related parties balances of approximately $1.0 million and $0.99 million respectively, were comprised primarily of deferred salaries of one of the Company's Executive Officers and certain employees; directors' fees; expense reimbursements; and deferred interest payments on a 12% Subordinated Notes owed to the Company's Chairman, President and Chief Executive Officer. Payment of any of these deferred items has been delayed until the Company's cash flow situation improves.

In California at the East Slopes Project, two of the vendors that the Company uses for services are partially owned by a related party, the Company's Chief Operating Officer. The Company's Chief Operating Officer is 50% owner in both Great Earth Power and ABPlus Net Holdings. Great Earth Power began providing a portion of the solar power electrical service for production operations in July 2020. ABPlus Net Holdings began providing portable tank rentals to the Company as a part of its water treatment and disposal operations in September 2020. The services provided by Great Earth Power and ABPlus Net Holdings are competitive with other vendors and save the Company significant expense. For the three months ended May 31, 2021, Great Earth Power and ABPlus Net Holdings were paid $6,300 and $3,840, respectively.

NOTE 7 — SHORT-TERM AND LONG-TERM BORROWINGS:

Note Payable

In December 2018, the Company was able to settle an outstanding balance owed to one of its third-party vendors. This settlement resulted in a $120,000 note payable being issued to the vendor. Additionally, the Company agreed to issue 2,000,000 shares of the Company's common stock as a part of the settlement agreement. Based on the closing price of the Company's common stock on the date of the settlement agreement, the value of the common stock transaction was determined to be $6,000. The common stock shares were issued during the twelve months ended February 29, 2020. The note has a maturity date of January 1, 2022 and bears an interest rate of 10% rate per annum. Monthly interest is accrued and payable on January 1st of each anniversary date until maturity of the note. At May 31, 2021, the accrued interest had not been paid and was outstanding. The accrued interest on the Note was $29,000 and $26,000 at May 31, 2021 and February 28, 2021, respectively.

Note Payable – Related Party

On December 22, 2020, the Company entered into a Secured Promissory Note (the "*Note*"), as borrower, with James Forrest Westmoreland and Angela Marie Westmoreland, Co-Trustees of the James and Angela Westmoreland Revocable Trust, or its assigns (the "*Noteholder*"), as the lender. James F. Westmoreland is the Company's Chairman, President and Chief Executive Officer. Pursuant to the Note, the Noteholder loaned the Company an aggregate principal amount of $155,548. After the deduction of loan fees of $10,929 the net proceeds from the loan were $144,619. The loan fees are being amortized as original issue discount (OID) over the term of the loan. The interest rate of the loan is 2.25%. The Note requires monthly payments on the Note balance until repaid in full. The maturity date of the Note is December 21, 2035. For the three months ended May 31, 2021, the Company made principal payments of $2,128 and amortized debt discount of $182. The obligations under the Note are secured by a lien on and security interest in the Company's oil and gas assets located in Kern County, California, as described in a Deed of Trust entered into by the Company in favor of the Noteholder to secure the obligations under the Note. Such lien shall be a first priority lien, subject only to a pre-existing lien filed by a working interest partner of the Company.

The Company may prepay the Note at any time. Upon the occurrence of any Event of Default and expiration of any applicable cure period, and at any time thereafter during the continuance of such Event of Default, the Noteholder may at its option, by written notice to the Company: (a) declare the entire principal amount of the Note, together with all accrued interest thereon and all other amounts payable hereunder, immediately due and payable; (b) exercise any of its remedies with respect to the collateral set forth in the Deed of Trust; and/or (c) exercise any or all of its other rights, powers or remedies under applicable law.

Current portion of note payable –related party balances at May 31, 2021 and February 28, 2021 are set forth in the table below:

	May 31, 2021	February 28, 2021
Note payable –related party, current portion	$ 8,656	$ 8,598
Unamortized debt issuance expenses	(729)	(728)
Note payable – related party, current portion, net	$ 7,927	$ 7,870

Note payable –related party long-term balances at May 31, 2021 and February 28, 2021 are set forth in the table below:

	May 31, 2021	February 28, 2021
Note payable – related party, non-current	$ 143,354	$ 145,540
Unamortized debt issuance expenses	(9,897)	(10,080)
Note payable– related party, non-current, net	$ 133,457	$ 135,460

Future estimated payments on the outstanding note payable – related party are set forth in the table below:

Twelve month periods ending May 31	
2022	$ 7,927
2023	8,159
2024	8,397
2025	8,642
2026	8,893
Thereafter	99,366
Total	$ 141,384

12% Subordinated Notes

The Company's 12% Subordinated Notes ("the Notes") issued pursuant to a January 2010 private placement offering to accredited investors, resulted in $595,000 in gross proceeds (of which $250,000 was from a related party) to the Company and accrue interest at 12% per annum, payable semi-annually on January 29th and July 29th. On January 29, 2015, the Company and 12 of the 13 holders of the Notes agreed to extend the maturity date of the Notes for an additional two years to January 29, 2017. Effective January 29, 2017, the maturity date of the Notes and the expiration date of the warrants that were issued in conjunction with the Notes were extended for an additional two years to January 29, 2019.

The Company has informed the Note holders that the payment of principal and final interest will be late and is subject to future financing being completed. The Notes principal of $565,000 was payable in full at the amended maturity date of the Notes, January 29, 2019, and has not been paid. The terms of the Notes, state that should the Board of Directors decide that the payment of the principal and any unpaid interest would impair the financial condition or operations of the Company, the Company may then elect a mandatory conversion of the unpaid principal and interest into the Company's common stock at a conversion rate equal to 75% of the average closing price of the Company's common stock over the 20 consecutive trading days preceding December 31, 2018. As of May 31, 2021, no conversion of the unpaid principal and interest into the Company's common stock has occurred. The accrued interest on the 12% Notes at May 31, 2021 and February 28, 2021 was $357,132 and $340,042, respectively.

12% Note balances at May 31, 2021 and February 28, 2021 are set forth in the table below:

	May 31, 2021	February 28, 2021
12% Subordinated Notes	$ 315,000	$ 315,000
12% Subordinated Notes, related party	250,000	250,000
Total 12% Subordinated Note balance	$ 565,000	$ 565,000

The accrued interest owed on the 12% Subordinated Note to the related party is presented on the Company's Balance Sheets under the caption *Accounts payable – related party* rather than under the caption *Accrued interest*.

Production Revenue Payable

Beginning in December 2018, the Company conducted a fundraising program to fund the drilling of future wells in California and Michigan and to settle some of its historical debt. The purchaser(s) of a production revenue payment interest received a production revenue payment on future wells to be drilled in California and Michigan in exchange for their purchase. As of May 31, 2021, the production revenue payment program balance was $950,100 of which $550,100 was owed to a related party - the Company's Chairman, President and Chief Executive Officer.

The production payment interest entitles the purchasers to receive production payments equal to twice their original amount paid, payable from a percentage of the Company's future net production payments from wells drilled after the date of the purchase and until the Production Payment Target (as described below) is met. The Company shall pay fifty percent of its net production payments from the relevant wells to the purchasers until each purchaser has received two times the purchase price (the "Production Payment Target"). Once the Company pays the purchasers amounts equal to the Production Payment Target, it shall thereafter pay a pro-rated eight percent (8%) of $1.3 million on its net production payments from the relevant wells to each of the purchasers. However, if the total raised is less than the target $1.3 million, then the payment will be a proportionate amount of the eight percent (8%). Additionally, if the Production Payment Target is not met within the first three years, the Company shall pay seventy-five percent of its production payments from the relevant wells to the purchasers until the Production Payment Target is met.

The Company accounted for the amounts received from these sales in accordance with ASC 470-10-25 and 470-10-35 which require amounts recorded as debt to be amortized under the interest method as described in ASC 835-30, Interest Method. Consequently, the program balance of $950,100 has been recognized as a production revenue payable. The Company determined an effective interest rate based on future expected cash flows to be paid to the holders of the production payment interests. This rate represents the discount rate that equates estimated cash flows with the initial proceeds received from the sales and is used to compute the amount of interest to be recognized each period. Estimating the future cash outflows under this agreement requires the Company to make certain estimates and assumptions about future revenues and payments and such estimates are subject to significant variability. Therefore, the estimates are likely to change which may result in future adjustments to the accretion of the interest expense and the amortized cost based carrying value of the related payables.

Accordingly, the Company has estimated the cash flows associated with the production revenue payments and determined a discount of $1,077,642 as of May 31, 2021, which is being accounted as interest expense over the estimated period over which payments will be made based on expected future revenue streams. For the three months ended May 31, 2021 and 2020, amortization of the debt discount on these payables amounted to $30,525 and $31,970, respectively, which has been included in interest expense in the statements of operations.

Production revenue payable balances at May 31, 2021 and February 28, 2021 are set forth in the table below:

	May 31, 2021	February 28, 2021
Estimated payments of production revenue payable	$ 2,029,742	$ 2,000,258
Less: unamortized discount	(495,795)	(496,836)
	1,533,947	1,503,422
Less: current portion	(98,336)	(111,753)
Net production revenue payable – long term	$ 1,435,611	$ 1,391,669

Line of Credit

The Company has an existing $890,000 line of credit for working capital purposes with UBS Bank USA ("UBS"), established pursuant to a Credit Line Agreement dated October 24, 2011 that is secured by the personal guarantee of its Chairman, President and Chief Executive Officer. On July 10, 2017, a $700,000 portion of the outstanding line of credit balance was converted to a 24 month fixed term annual interest rate of 3.244% with interest payable monthly. On July 10, 2019, the 24-month fixed term loan amount of $700,000 was renewed at the same annual percentage interest rate of 3.244% for an additional 24 months. The remaining principal balance of the line of credit has a stated reference rate of 0.249% + 337.5 basis points with interest payable monthly. The reference rate is based on the 30 day LIBOR ("London Interbank Offered Rate") and is subject to change from UBS.

During the three months ended May 31, 2021 and 2020, the Company did not receive any advances on the line of credit. During the three months ended May 31, 2021 and 2020, the Company made payments to the line of credit of $15,000 and $15,000, respectively. Interest converted to principal for the three months ended May 31, 2021 and 2020 was $6,892 and $7,389, respectively. At May 31, 2021 and February 28, 2021, the line of credit had an outstanding balance of $832,796 and $840,904, respectively.

Paycheck Protection Program (PPP) Loans

In March 2020, the Coronavirus Aid, Relief, and Economic Security Act commonly referred to as the CARES Act became law. One component of the CARES Act was the paycheck protection program ("PPP") which provides small business with the resources needed to maintain their payroll and cover applicable overhead. The PPP is implemented by the Small Business Administration ("SBA") with support from the Department of the Treasury. The Company applied for, and was accepted to participate in this program. On May 11, 2020, the Company received funding for approximately $74,355. On February 12, 2021, the Company applied for loan forgiveness under the provisions of Section 1106 of the CARES Act. Loan forgiveness was subject to the sole approval of the SBA. On February 23, 2021, the SBA notified our lender that the loan was forgiven and repaid the loan in full.

On March 4, 2021, the Company applied for, and was accepted to participate in the SBA PPP Second Draw program with funding pursuant to the Economic Aid Act that was passed in December, 2020. On March 15, 2021, Daybreak received funding for $72,800. The second-draw loan is a five-year loan with a maturity date of March 6, 2026. The loan bears an annual interest rate of 1%. The monthly payment is $1,670 with the first payment due on July 6, 2022. We intend to use the loan proceeds to partially subsidize direct payroll, rent and utility expenses. It is the Company's intent to apply for loan forgiveness for the PPP Second Draw PPP loan. Loan forgiveness is subject to the sole approval of the SBA.

Encumbrances

On October 17, 2018, a working interest partner in California filed a UCC financing statement in regards to payable amounts owed to the partner by the Company. As of May 31, 2021, we had no encumbrances on our crude oil project in Michigan.

NOTE 8 — GAIN ON ASSET DISPOSAL:

During the three months ended May 31, 2021, the Company recognized a gain on asset disposal of $9,614. The gain was the result of an insurance settlement on the theft of a company vehicle that was fully depreciated.

NOTE 9 — LEASES:

The Company leases approximately 988 rentable square feet of office space from an unaffiliated third party for our corporate office located in Spokane Valley, Washington. Additionally, we lease approximately 416 and 695 rentable square feet from unaffiliated third parties for our regional operations office in Friendswood, Texas and storage and auxiliary office space in Wallace, Idaho, respectively. The lease in Friendswood is a 12-month lease that expires in October 2021 and as such is considered a short-term lease. The Company has elected to not apply the recognition requirements of ASC 842 to this short-term lease. The Spokane Valley and Wallace leases are currently on a month-to-month basis. The Company's lease agreements do not contain any residual value guarantees, restrictive covenants or variable lease payments. The Company has not entered into any financing leases.

Rent expense for the three months ended May 31, 2021 and 2020 was $5,947 and $5,872, respectively.

NOTE 10 — STOCKHOLDERS' DEFICIT:

Preferred Stock

The Company is authorized to issue up to 10,000,000 shares of preferred stock with a par value of $0.001. The Company's preferred stock may be entitled to preference over the common stock with respect to the distribution of assets of the Company in the event of liquidation, dissolution, or winding-up of the Company, whether voluntarily or involuntarily, or in the event of any other distribution of assets of the Company among its shareholders for the purpose of winding-up its affairs. The authorized but unissued shares of preferred stock may be divided into and issued in designated series from time to time by one or more resolutions adopted by the Board of Directors. The directors in their sole discretion shall have the power to determine the relative powers, preferences, and rights of each series of preferred stock.

Series A Convertible Preferred Stock

The Company has designated 2,400,000 shares of the 10,000,000 preferred shares as Series A Convertible Preferred Stock ("Series A Preferred"), with a $0.001 par value. At May 31, 2021 and February 28, 2021, there were 709,568 shares issued and outstanding, that had not been converted into our common stock. As of May 31, 2021 and February 28, 2021, there were 44 accredited investors who had converted 690,197 Series A Preferred shares into 2,070,591 shares of Daybreak common stock.

The conversions of Series A Preferred that have occurred since the Series A Preferred was first issued in July 2006 are set forth in the table below.

Fiscal Period Ended	Shares of Series A Preferred Converted to Common Stock	Shares of Common Stock Issued from Conversion	Number of Accredited Investors
Periods prior to February 29, 2014	662,200	1,986,600	41
February 28, 2015	3,000	9,000	1
February 29, 2016	10,000	30,000	1
February 28, 2017	—	—	—
February 28, 2018	14,997	44,991	1
February 28, 2019	—	—	—
February 29, 2020	—	—	—
February 28, 2021	—	—	—
May 31, 2021	—	—	—
Totals	690,197	2,070,591	44

Holders of Series A Preferred shall accrue dividends, in the amount of 6% of the original purchase price per annum. Dividends may be paid in cash or common stock at the discretion of the Company. Dividends are cumulative whether or not in any dividend period or periods we have assets legally available for the payment of such dividends. Accumulations of dividends on Series A Preferred do not bear interest. Dividends are payable upon declaration by the Board of Directors.

As of May 31, 2021 no dividends have been declared or paid. Dividends earned since issuance by fiscal year and the three months ended May 31, 2021 are set forth in the table below:

Fiscal Period Ended	Shareholders at Period End	Accumulated Dividends
Periods prior to February 28, 2014		$ 1,447,943
February 28, 2015	58	132,634
February 29, 2016	57	130,925
February 28, 2017	57	130,415
February 28, 2018	56	128,231
February 28, 2019	56	127,714
February 29, 2020	56	128,063
February 28, 2021	56	127,714
May 31, 2021	56	32,191
		$ 2,385,830

Common Stock

The Company is authorized to issue up to 200,000,000 shares of $0.001 par value common stock of which 60,491,122 shares were issued and outstanding as of May 31, 2021 and February 28, 2021, respectively.

NOTE 11 — WARRANTS:

During the twelve months ended February 29, 2020 there were 2.1 million warrants issued to a third party for investor relations services. The fair value of the warrants was determined by the Black-Scholes pricing model, was $17,689, and is being amortized over the three year vesting period of the warrants. The Black-Scholes valuation encompassed the following assumptions: a risk free interest rate of 1.68%; volatility rate of 260.23%; and a dividend yield of 0.0%. The warrant contains a vesting blocking provision that prevents the vesting of any warrants that such vesting would cause the warrant holder's beneficial ownership (as such term is defined in Section 13d-3 of the Securities Exchange Act of 1934, as amended) to exceed more than four and ninety-nine one-hundredths percent (4.99%) of the Company's outstanding Common Stock. The foregoing restriction may not be waived by either party. The warrants vest in equal parts over a three year period beginning on January 2, 2020 and all warrants expire on January 2, 2024. At May 31, 2021, both the outstanding warrants and the exercisable warrants have a weighted average exercise price of $0.01, a weighted average remaining life of 2.58 years. The outstanding warrants an intrinsic value of $56,700, while the exercisable warrants have an intrinsic value of $14,270. For the three months ended May 31, 2021 and 2020, the recorded amount of warrant expense was $1,474 and $1,474, respectively.

Warrant activity for the three months ended May 31, 2021 is set forth in the table below:

	Warrants	Weighted Average Exercise Price
Warrants outstanding, February 28, 2021	2,100,000	$ 0.01
Changes during the three months ended May 31, 2021:		
Issued	—	$ —
Expired / cancelled / forfeited	—	$ —
Warrants outstanding, May 31, 2021	2,100,000	$ 0.01
Warrants exercisable, May 31, 2021	528,507	$ 0.01

NOTE 12 — INCOME TAXES:

On December 22, 2017, the federal government enacted a tax bill H.R.1, an act to provide for reconciliation pursuant to Titles II and V of the concurrent resolution on the budget for fiscal year 2018, commonly referred to as the Tax Cuts and Jobs Act. The Tax Cuts and Jobs Act contains significant changes to corporate taxation, including, but not limited to, reducing the U.S. federal corporate income tax rate from 35% to 21% and modifying or limiting many business deductions. We re-measured deferred tax liabilities based on rates at which they are expected to be utilized in the future, which is generally 21%.

Reconciliation between actual tax expense (benefit) and income taxes computed by applying the U.S. federal income tax rate and state income tax rates to income from continuing operations before income taxes is set forth in the table below:

	May 31, 2021	February 28, 2021
Computed at U.S. and state statutory rates (40%)	$ (39,583)	$ (152,860)
Permanent differences	10,006	15,342
Changes in valuation allowance	29,577	137,518
Total	$ —	$ —

Tax effects of temporary differences that give rise to significant portions of the deferred tax assets and deferred liabilities are set forth in the table below:

	May 31, 2021	February 28, 2021
Deferred tax assets:		
Net operating loss carryforwards	$ 5,613,903	$ 5,587,416
Crude oil properties	66,528	63,438
Stock based compensation	66,187	66,187
Other	27,838	27,838
Less valuation allowance	(5,774,456)	(5,744,879)
Total	$ —	$ —

At May 31, 2021, Daybreak had estimated net operating loss ("NOL") carryforwards for federal and state income tax purposes of approximately $18,813,351 which will begin to expire, if unused, beginning in 2024. Under the Tax Cuts and Jobs Act, the NOL portion of the loss incurred in the year ended February 28, 2018 of $340,749; the loss incurred for the year ended February 29, 2020 of $339,299; the loss incurred for the year ended February 28, 2021 of $416,918 and the loss incurred for three months ended May 31, 2021 in the amount of $88,765 will not expire and will carry over indefinitely. The valuation allowance increased $29,577 for the three months ended May 31, 2021 and increased approximately $137,518 for the year ended February 28, 2021, respectively. Section 382 of the Internal Revenue Code places annual limitations on the Company's net operating loss (NOL) carryforward.

The above estimates are based on management's decisions concerning elections which could change the relationship between net income and taxable income. Management decisions are made annually and could cause estimates to vary significantly. The Company files federal income tax returns with the United States Internal Revenue Service and state income tax returns in various state tax jurisdictions. As a general rule the Company's tax returns for the fiscal years after 2016 currently remain subject to examinations by appropriate tax authorities. None of our tax returns are under examination at this time.

NOTE 13 — COMMITMENTS AND CONTINGENCIES:

Various lawsuits, claims and other contingencies arise in the ordinary course of the Company's business activities. While the ultimate outcome of any future contingency is not determinable at this time, management believes that any liability or loss resulting therefrom will not materially affect the financial position, results of operations or cash flows of the Company.

The Company, as an owner or lessee and operator of crude oil properties, is subject to various federal, state and local laws and regulations relating to discharge of materials into, and protection of, the environment. These laws and regulations may, among other things, impose liability on the lessee under a crude oil lease for the cost of pollution clean-up resulting from operations and subject the lessee to liability for pollution damages. In some instances, the Company may be directed to suspend or cease operations in the affected area. The Company maintains insurance coverage that is customary in the industry, although the Company is not fully insured against all environmental risks.

The Company is not aware of any environmental claims existing as of May 31, 2021. There can be no assurance, however, that current regulatory requirements will not change or that past non-compliance with environmental issues will not be discovered on the Company's crude oil properties.

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

The following discussion is management's assessment of the current and historical financial and operating results of the Company and of our financial condition. It is intended to provide information relevant to an understanding of our financial condition, changes in our financial condition and our results of operations and cash flows and should be read in conjunction with our unaudited financial statements and notes thereto included elsewhere in this Quarterly Report on Form 10-Q for the three months ended May 31, 2021 and in our Annual Report on Form 10-K for the year ended February 28, 2021. References to "Daybreak", the "Company", "we", "us" or "our" mean Daybreak Oil and Gas, Inc.

Cautionary Statement Regarding Forward-Looking Statements

Certain statements contained in our Management's Discussion and Analysis of Financial Condition and Results of Operations ("MD&A") are intended to be covered by the safe harbor provided for under Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Exchange Act.

All statements other than statements of historical fact contained in this MD&A report are inherently uncertain and are forward-looking statements. Statements that relate to results or developments that we anticipate will or may occur in the future are not statements of historical fact. Words such as "anticipate," "believe," "could," "estimate," "expect," "intend," "may," "plan," "predict," "project," "will" and similar expressions identify forward-looking statements. Examples of forward-looking statements include, without limitation, statements about the following:

- Our future operating results;
- Our future capital expenditures;
- Our future financing;
- Our expansion and growth of operations; and
- Our future investments in and acquisitions of crude oil properties.

We have based these forward-looking statements on assumptions and analyses made in light of our experience and our perception of historical trends, current conditions, and expected future developments. However, you should be aware that these forward-looking statements are only our predictions and we cannot guarantee any such outcomes. Future events and actual results may differ materially from the results set forth in or implied in the forward-looking statements. Important factors that could cause actual results to differ materially from our expectations include, but are not limited to, the following risks and uncertainties:

- General economic and business conditions;
- National and international pandemics such as the novel coronavirus COVID-19 outbreak;
- Exposure to market risks in our financial instruments;
- Fluctuations in worldwide prices and demand for crude oil;
- Our ability to find, acquire and develop crude oil properties;
- Fluctuations in the levels of our crude oil exploration and development activities;
- Risks associated with crude oil exploration and development activities;
- Competition for raw materials and customers in the crude oil industry;
- Technological changes and developments in the crude oil industry;
- Legislative and regulatory uncertainties, including proposed changes to federal tax law and climate change legislation, regulation of hydraulic fracturing and potential environmental liabilities;
- Our ability to continue as a going concern;
- Our ability to secure financing under any commitments as well as additional capital to fund operations; and
- Other factors discussed elsewhere in this Form 10-Q and in our other public filings, press releases, and discussions with Company management.

Our reserve estimates are determined through a subjective process and are subject to periodic revision.

In December 2019, the 2019 novel coronavirus ("COVID-19") surfaced in Wuhan, China. The World Health Organization declared a global emergency on January 30, 2020, with respect to the outbreak and most countries throughout the world initiated severe travel restrictions to and from other countries. This widespread health crisis and the governmental restrictions associated with it, have adversely affected demand for crude oil and natural gas, depressed crude oil prices, and affected our ability to access capital. These factors, in turn, have had a negative impact on our operations, and financial condition as evidenced by the unprecedented decline in crude oil prices and our revenues during this same time period.

Should one or more of the risks or uncertainties described above or elsewhere in our Form 10-K for the year ended February 28, 2021 and in this Form 10-Q for the three months ended May 31, 2021 occur, or should any underlying assumptions prove incorrect, our actual results and plans could differ materially from those expressed in any forward-looking statements. We specifically undertake no obligation to publicly update or revise any information contained in any forward-looking statement or any forward-looking statement in its entirety, whether as a result of new information, future events, or otherwise, except as required by law.

All forward-looking statements attributable to us are expressly qualified in their entirety by this cautionary statement.

Introduction and Overview

We are an independent crude oil and natural gas exploration, development and production company. Our basic business model is to increase shareholder value by finding and developing crude oil and natural gas reserves through exploration and development activities, and selling the production from those reserves at a profit. To be successful, we must, over time, be able to find crude oil and natural gas reserves and then sell the resulting production at a price that is sufficient to cover our finding costs, operating expenses, administrative costs and interest expense, plus offer us a return on our capital investment. A secondary means of generating returns can include the sale of either producing or non-producing lease properties.

Our long-term success depends on, among many other factors, the acquisition and drilling of commercial grade crude oil and natural gas properties and on the prevailing sales prices for crude oil and natural gas along with associated operating expenses. The volatile nature of the energy markets makes it difficult to estimate future prices of crude oil and natural gas; however, any prolonged period of depressed prices, such as we have experienced in the last 15 months, will have a material adverse effect on our results of operations and financial condition.

Our operations are focused on identifying and evaluating prospective crude oil and natural gas properties and funding projects that we believe have the potential to produce crude oil and natural gas in commercial quantities. We conduct all of our drilling, exploration and production activities in the United States, and all of our revenues are derived from sales to customers within the United States. Currently, we are in the process of developing a multi-well oilfield project in Kern County, California and an exploratory joint drilling project in Michigan.

Our management cannot provide any assurances that Daybreak will ever operate profitably. While, in the past, we have had positive cash flow from our crude oil operations in California, we have not yet generated sustainable positive cash flow or earnings on a company-wide basis. As a small company, we are more susceptible to the numerous business, investment and industry risks that have been described in Item 1A. Risk Factors of our Annual Report on Form 10-K for the fiscal year ended February 28, 2021 and in Part III, Item 1A. Risk Factors of this 10-Q Report. Throughout this Quarterly Report on Form 10-Q, crude oil is shown in barrels ("Bbls"); natural gas is shown in thousands of cubic feet ("Mcf") unless otherwise specified, and hydrocarbon totals are expressed in barrels of crude oil equivalent ("BOE").

Below is brief summary of our crude oil projects in California and Michigan. Refer to our discussion in Item 2. Properties, in our Annual Report on Form 10-K for the year ended February 28, 2021 for more information on our multi-well oilfield project in California and our exploratory joint drilling project in Michigan.

Kern County, California (East Slopes Project)

The East Slopes Project is located in the southeastern part of the San Joaquin Basin near Bakersfield, California. Drilling targets are porous and permeable sandstone reservoirs that exist at depths of 1,200 feet to 4,500 feet. Since January 2009, we have participated in the drilling of 25 wells in this project. We have been the Operator at the East Slopes Project since March 2009.

The crude oil produced from our acreage in the Vedder Sand is considered heavy oil. The crude oil ranges from 14° to 16° API (American Petroleum Institute) gravity and must be heated to separate and remove water prior to sale. Our crude oil wells in the East Slopes Project produce from five reservoirs at our Sunday, Bear, Black, Ball and Dyer Creek locations. The Sunday property has six producing wells, while the Bear property has nine producing wells. The Black property is the smallest of all currently producing reservoirs, and currently has two producing wells at this property. The Ball property also has two producing wells while the Dyer Creek property has one producing well. During the three months ended May 31, 2021, we had production from 20 crude oil wells. Our average working interest and net revenue interest ("NRI") in these 20 wells is 36.6% and 28.4%, respectively.

We plan on acquiring additional acreage exhibiting the same seismic characteristics and on trend with the Bear, Black and Dyer Creek reservoirs. Some of these prospects, if successful, would utilize the Company's existing production facilities. In addition to the current field development, there are several other exploratory prospects that have been identified from the seismic data, which we plan to drill in the future.

California Drilling Plans

Planned drilling activity and implementation of our oilfield development plan will not begin until there is a sustained improvement in crude oil prices and additional financing is in put in place. We do not plan to make any capital investments within the East Slopes Project area in the 2021-2022 fiscal year if no new financing is in place. If new financing is secured, we plan to spend approximately $435,000 drilling three development wells in the 2021-2022 fiscal year.

Michigan Acreage Acquisition

In January 2017, we acquired a 30% working interest in 1,400 acres in the Michigan Basin. Multiple drilling targets were identified through a 2-D seismic interpretation. A 3-D seismic survey was obtained in January and February of 2017 on the first prospect. An analysis of the 3-D seismic survey confirmed the first prospect originally identified on the 2-D seismic, as well as several additional drilling locations. We have plans to obtain an additional 3-D survey on the second prospect after drilling a well on the first prospect, however the two prospects are independent of each other and the success or lack of results of either prospect does not affect the potential of the other prospect. The wells will be drilled vertically with conventional completions and no hydraulic fracturing is anticipated. With the settlement of our debt obligations to a former lender in December 2018, we acquired an additional 40% working interest, bringing our aggregate working interest to 70% in Michigan. The first well is expected to be drilled when additional financing is secured.

Encumbrances

On October 17, 2018, a working interest partner in California filed a UCC financing statement in regards to payables owed to the partner by the Company. As of May 31, 2021, we had no encumbrances on our crude oil project in Michigan.

Results of Operations – Three Months Ended May 31, 2021 compared to the Three Months Ended May 31, 2020

California Crude Oil Prices

The price we receive for crude oil sales in California is based on prices posted for Midway-Sunset crude oil delivery contracts, less deductions that vary by grade of crude oil sold and transportation costs. The posted Midway-Sunset price generally moves in correlation to, and at a discount to, prices quoted on the New York Mercantile Exchange (NYMEX") for spot West Texas intermediate ("WTI") crude oil, Cushing, Oklahoma delivery contracts. We do not have any natural gas revenues in California.

There continues to be a significant amount of volatility in crude oil prices and a dramatic fluctuation in our realized sale price of crude oil since June of 2014, when the monthly average price of WTI crude oil was $105.79 per barrel and our realized sale price per barrel of crude oil was $98.78. As an example, for the month of April 2020 the monthly average closing price of WTI crude oil was $16.55 and our monthly realized oil price was $16.96 per barrel. This volatility in crude oil prices continued through most of our 2020-2021 fiscal year. The volatility and decline in the price of crude oil has had a substantial negative impact on our cash flow from our producing California properties. While there has been some improvement in crude oil prices for the three months ended May 31, 2021, there is no guarantee that this trend will continue. It is beyond our ability to accurately predict crude oil prices over any substantial length of time.

A comparison of the average WTI price and the average realized crude oil sales price for the three months ended May 31, 2021 and 2020 is shown in the table below:

	Three Months Ended		
	May 31, 2021	May 31, 2020	Percentage Change
Average three month WTI crude oil price (Bbl)	$ 63.07	$ 24.77	154.6%
Average three month realized crude oil sales price (Bbl)	$ 61.65	$ 24.29	153.8%

For the three months ended May 31, 2021, the average WTI price was $63.07 and our average realized crude oil sale price was $61.65, representing a discount of $1.42 per barrel or 2.3% lower than the average WTI price. In comparison, for the three months ended May 31, 2020, the average WTI price was $24.77 and our average realized sale price was $24.29 representing a discount of $0.48 per barrel or 1.9% lower than the average WTI price. Historically, the sale price we receive for California heavy crude oil has been less than the quoted WTI price because of the lower API gravity of our California crude oil in comparison to the API gravity of quoted WTI crude oil.

California Crude Oil Revenue and Production

Crude oil revenue in California for the three months ended May 31, 2021 increased $78,101 or 112.9% to $147,300 in comparison to revenue of $69,199 for the three months ended May 31, 2020. The average realized sale price of a barrel of crude oil for the three months ended May 31, 2021 was $61.65 in comparison to $24.29 for the three months ended May 31, 2020. The 2019 novel coronavirus ("COVID-19") that has spread to countries throughout the world including the United States had a substantial negative impact on the demand for crude oil and is largely responsible for the decline in crude oil prices for the three months ended May 31, 2020. The increase in the average realized sale price of a barrel of crude oil of $37.36 or 153.8% accounted for 136.3% of the increase in revenue for the three months ended May 31, 2021, offset by a decline of 36.3% in revenue due to the 16.1% decline in production volume.

Our net sales volume for the three months ended May 31, 2021 was 2,389 barrels of crude oil in comparison to 2,849 barrels sold for the three months ended May 31, 2020. This decrease in crude oil sales volume of 460 barrels or 16.1% was primarily due to the timing of oil sales that occurred for the three months ended May 31, 2021.

The gravity of our produced crude oil in California ranges between 14° API and 16° API. Production for the three months ended May 31, 2021 was from 20 wells resulting in 1,809 well days of production in comparison to 1,838 well days of production for the three months ended May 31, 2020.

Our crude oil sales revenue for the three months ended May 31, 2021 and 2020 is set forth in the following table:

	Three Months Ended May 31, 2021		Three Months Ended May 31, 2020	
Project	Revenue	Percentage	Revenue	Percentage
California – East Slopes Project	$ 147,300	100.0%	$ 69,199	100.0%

*Our average realized sale price on a BOE basis for the three months ended May 31, 2021 was $61.65 in comparison to $24.29 for the three months ended May 31, 2020, representing an increase of $37.36 or 153.8% per barrel.

Operating Expenses

Our total operating expenses for the three months ended May 31, 2021 were $228,299, an increase of $22,576 or 11.0% compared to $205,723 for the three months ended May 31, 2020. Operating expenses for the three months ended May 31, 2021 and 2020 are set forth in the table below:

	Three Months Ended May 31, 2021			Three Months Ended May 31, 2020		
	Expenses	Percentage	BOE Basis	Expenses	Percentage	BOE Basis
Production expenses	$ 46,726	20.5%		$ 39,195	19.0%	
Exploration and drilling expenses	—	0.0%		—	0.0%	
Depreciation, depletion, amortization ("DD&A")	13,948	6.1%		14,159	6.9%	
General and administrative ("G&A") expenses	167,625	73.4%		152,369	74.1%	
Total operating expenses	$ 228,299	100.0%	$ 95.56	$ 205,723	100.0%	$ 72.21

Production expenses include expenses associated with the production of crude oil. These expenses include pumpers, electricity, road maintenance, control of well insurance, property taxes and well workover costs; and, relate directly to the number of wells that are in production. For the three months ended May 31, 2021, these expenses increased by $7,531 or 19.2% to $46,726 in comparison to $39,195 for the three months ended May 31, 2020. For the three months ended May 31, 2021 and 2020, we had 20 wells on production in California. Production expense on a barrel of oil equivalent ("BOE") basis for the three months ended May 31, 2021 and 2020 were $19.56 and $13.76, respectively. Production expenses represented 20.5% and 19.0% of total operating expenses for the three months ended May 31, 2021 and 2020, respectively.

Exploration and drilling expenses include geological and geophysical ("G&G") expenses as well as leasehold maintenance, plugging and abandonment ("P&A") expenses and dry hole expenses. For the three months ended May 31, 2021, these expenses were $-0- in comparison to $-0- for the three months ended May 31, 2020. Exploration and drilling expenses represented 0.0% of total operating expenses for the three months ended May 31, 2021 and 2020, respectively.

Depreciation, depletion and amortization ("DD&A") expenses relate to equipment, proven reserves and property costs, along with impairment, and is another component of operating expenses. For the three months ended May 31, 2021, DD&A expenses decreased $211 or 1.5% to $13,948 in comparison to $14,159 for the three months ended May 31, 2020. On a BOE basis DD&A expense was $5.84 and $4.97 for the three months ended May 31, 2021 and 2020, respectively. DD&A and impairment expenses represented 6.1% and 6.9% of total operating expenses for the three months ended May 31, 2021 and 2020, respectively.

General and administrative (“G&A”) expenses include the salaries of five employees, including management. Other items included in our G&A expenses are legal and accounting expenses, director fees, stock compensation, travel expenses, insurance, Sarbanes-Oxley (“SOX”) compliance expenses and other administrative expenses necessary for an operator of crude oil properties as well as for running a public company. For the three months ended May 31, 2021, these expenses increased $15,256 or 10.0% to $167,625 in comparison to $152,369 for the three months ended May 31, 2020. For the three months ended May 31, 2021, we received, as Operator, administrative overhead reimbursement of $13,322 for the East Slopes Project which was used to directly offset certain employee salaries. We are continuing a program of reducing all of our G&A costs wherever possible. G&A expenses represented 73.4% and 74.1% of total operating expenses for the three months ended May 31, 2021 and 2020, respectively.

During the three months ended May 31, 2021, the Company recognized a gain on asset disposal of $9,614. The gain was the result of an insurance settlement on the theft of a company vehicle that was fully depreciated.

Interest expense, net for the three months ended May 31, 2021 increased $793 or 1.3% to $61,266 in comparison to $60,473 for the three months ended May 31, 2020.

In December 2019, the 2019 novel coronavirus (“COVID-19") surfaced in Wuhan, China. The World Health Organization declared a global emergency on January 30, 2020, with respect to the outbreak and most countries throughout the world initiated travel restrictions to and from other countries. This widespread health crisis and the governmental restrictions associated with it, adversely affected demand for oil and gas, depressed crude oil prices, and affected our ability to access capital. These factors, in turn, had a negative impact our operations, and financial condition for the three months ended May 31, 2020 and the twelve months ended February 28, 2021 as evidenced by the unprecedented decline in crude oil prices and our revenues during this same time period.

On March 27, 2020, the Coronavirus Aid, Relief, and Economic Security Act commonly referred to as the CARES Act became law. One component of the CARES Act was the paycheck protection program (“PPP”) which provided small business with the resources needed to maintain their payroll and cover applicable overhead. The PPP is implemented by the Small Business Administration (“SBA”) with support from the Department of the Treasury. The Company applied for, and was accepted to participate in this program. On May 11, 2020, the Company received funding for approximately $74,355. In February 2021, the Company applied for full loan forgiveness and later that month was notified by our lender that the SBA had forgiven our original loan in full. On March 15, 2021, the Company received $72,800 in funding through the SBA second draw paycheck protection program. Second Draw PPP loans can be used to help fund payroll costs, including benefits. Funds can also be used to pay for mortgage interest, rent and utilities over a 24 week period. We plan on also applying for loan forgiveness on this second draw PPP loan.

Due to the nature of our business, we expect that revenues, as well as all categories of expenses, will continue to fluctuate substantially on a quarter-to-quarter and year-to-year basis. Revenues are highly dependent on the volatility of hydrocarbon prices as seen during the last 18 months and production volumes. Production expenses will fluctuate according to the number and percentage ownership of producing wells as well as the amount of revenues we receive based on the price of crude oil. Exploration and drilling expenses will be dependent upon the amount of capital that we have to invest in future development projects, as well as the success or failure of such projects. Likewise, the amount of DD&A expense will depend upon the factors cited above including the size of our proven reserves base and the market price of energy products. G&A expenses will also fluctuate based on our current requirements, but will generally tend to increase as we expand the business operations of the Company. An ongoing goal of the Company is to improve cash flow to cover the current level of G&A expenses and to fund our drilling programs in California and Michigan.

Capital Resources and Liquidity

Our primary financial resource is our proven crude oil reserve base. Our ability to fund any future capital expenditure programs is dependent upon the prices we receive from crude oil sales, the success of our drilling programs in California and Michigan and the availability of capital resource financing. There continues to be a significant amount of volatility in crude oil prices and dramatic fluctuation in our realized sale price of crude oil since June of 2014, when the monthly average price of WTI crude oil was $105.79 per barrel, and our realized sale price per barrel of crude oil was $98.78. As an example, for the month of April 2020 the monthly average closing price of WTI crude oil was $16.55 and our monthly realized oil price was $16.96 per barrel. This volatility in crude oil prices continued through most of our 2020-2021 fiscal year. The volatility and decline in the price of crude oil has had a substantial negative impact on our cash flow from our producing California properties. While there has been some improvement in crude oil prices for the three months ended May 31, 2021, there is no guarantee that this trend will continue. It is beyond our ability to accurately predict crude oil prices over any substantial length of time.

We plan to spend approximately $435,000 drilling three development wells in the current 2021-2022 fiscal year if new financing is secured; however our actual expenditures may vary significantly from this estimate if our plans for exploration and development activities change during the year or if we are not able to obtain financing to fund these capital investments. Factors such as changes in operating margins and the availability of capital resources could increase or decrease our ultimate level of expenditures during the current fiscal year.

Changes in our capital resources at May 31, 2021 in comparison with February 28, 2021 are set forth in the table below:

	May 31, 2021		February 28, 2021		Increase (Decrease)		Percentage Change
Cash	$	112,723	$	33,528	$	79,195	236.2%
Current assets	$	292,259	$	283,239	$	9,020	3.2%
Total assets	$	918,952	$	912,125	$	6,827	0.7%
Current liabilities	$	(4,491,168)	$	(4,469,074)	$	22,094	0.5%
Total liabilities	$	(6,167,269)	$	(6,029,265)	$	138,004	2.3%
Working capital	$	(4,198,909)	$	(4,185,835)	$	13,074	0.3%

Our working capital deficit increased approximately $13,074 or 0.3% to $4.199 million at May 31, 2021 in comparison to $4.186 million at February 28, 2021. The increase in our working capital deficit was primarily due to an increase on our current liabilities. We anticipate an increase in our cash flow will occur when we are able to return to our planned drilling program that will result in an increase in the number of wells on production.

Our business is capital intensive. Our ability to grow is dependent upon favorably obtaining outside capital and generating cash flows from operating activities necessary to fund our investment activities. There is no assurance that we will be able to achieve profitability. Since our future operations will continue to be dependent on successful exploration and development activities and our ability to seek and secure capital from external sources, should we be unable to achieve sustainable profitability this could cause any equity investment in the Company to become worthless.

Major sources of funds in the past for us have included the debt or equity markets and we anticipate that we will have to rely on these capital markets to fund future operations and growth. Our business model is focused on acquiring exploration or development properties as well as existing production. Our ability to generate future revenues and operating cash flow will depend on successful exploration, and/or acquisition of crude oil producing properties, which may very likely require us to continue to raise equity or debt capital from outside sources.

Daybreak has ongoing capital commitments to develop certain leases pursuant to their underlying terms. Failure to meet such ongoing commitments may result in the loss of the right to participate in future drilling on certain leases or the loss of the lease itself. These ongoing capital commitments will cause us to seek additional forms of financing through various methods, including issuing debt securities, equity securities, bank debt, or combinations of these instruments which could result in dilution to existing security holders and increased debt and leverage. The current uncertainty in the credit and capital markets as well as the instability and volatility in crude oil prices since June of 2014, has restricted our ability to obtain needed capital. The 2019 novel coronavirus (“COVID-19") that spread to countries throughout the world including the United States had a substantial negative impact on the demand for crude oil and is largely responsible for the decline in crude oil prices. No assurance can be given that we will be able to obtain funding under any loan commitments or any additional financing on favorable terms, if at all. Sales of interests in our assets may be another source of cash flow available to us.

The Company’s financial statements for the three months ended May 31, 2021 have been prepared on a going concern basis, which contemplates the realization of assets and the settlement of liabilities in the normal course of business. We have incurred a cumulative net loss since entering the crude oil exploration industry and as of three months ended May 31, 2021 have an accumulated deficit of $29.6 million and a working capital deficit of $4.2 million which raises substantial doubt about our ability to continue as a going concern.

In the current fiscal year, we will continue to seek additional financing for our planned exploration and development activities in California and Michigan. We could obtain financing through one or more various methods, including issuing debt securities, equity securities, or bank debt, or combinations of these instruments, which could result in dilution to existing security holders and increased debt and leverage. No assurance can be given that we will be able to obtain funding under any loan commitments or any additional financing on favorable terms, if at all. Sales of interests in our assets may be another source of cash flow.

Changes in Financial Condition

During the three months ended May 31, 2021, we received crude oil sales revenue from 20 wells in our East slopes Project in Kern County, California. Our commitment to improving corporate profitability remains unchanged. Since June 2014, there has been significant volatility and uncertainty in the WTI price of crude oil and correspondently in the realized price we receive from oil sales. This volatility in the price of crude oil has created a substantial negative impact on the cash flow of our producing crude oil properties in California. During the three months ended May 31, 2021 and 2020, crude oil revenue from California was $147,300 and $69,199, respectively. For the three months ended May 31, 2021 and 2020, we had an operating loss of $80,999 and $136,524, respectively.

Our balance sheet at May 31, 2021 reflects total assets of approximately $0.92 million in comparison to approximately $0.91 million at February 28, 2021. At May 31, 2021, total liabilities were approximately $6.2 million in comparison to approximately $6.0 million at February 28, 2021. The increase in liabilities was primarily due to recognition of the PPP 2nd Draw loan we received for $72,800, changes in estimates of the production revenue payable debt discount and increase in accounts payable - related parties.

Common stock shares issued and outstanding were 60,491,122 at May 31, 2021 and February 28, 2021, respectively.

Cash Flows

Changes in the net funds provided by and (used in) our operating, investing and financing activities are set forth in the table below:

	Three Months Ended May 31, 2021	Three Months Ended May 31, 2020	Increase (Decrease)	Percentage Change
Net cash provided by used in operating activities	$ 63,339	$ (105,277)	168,616	160.2%
Net cash used in investing activities	$ (10,584)	$ —	(10,584)	100%
Net cash provided by financing activities	$ 26,440	$ 42,395	(15,955)	(37.6%)

Cash Flow Provided By (Used In) Operating Activities

Cash flow from operating activities is derived from the production of our crude oil reserves and changes in the balances of non-cash accounts, receivables, payables or other non-energy property asset account balances. For the three months ended May 31, 2021, cash flow provided by operating activities was $63,339 in comparison to $105,277 used in operating activities for the three months ended May 31, 2020. This increase of $168,616 in our cash flow operating activities was due to a reduction in our net loss and decreases in both our accounts receivable and accounts payable for the three months ended May 31, 2021 in comparison to the three months ended May 31, 2020. Variations in cash flow from operating activities may impact our level of exploration and development expenditures.

Our expenditures in operating activities consist primarily of exploration and drilling expenses, production expenses, geological, geophysical and engineering services and maintenance of existing mineral leases. Our expenses also consist of consulting and professional services, employee compensation, legal, accounting, travel and other G&A expenses that we have incurred in order to address normal and necessary business activities.

Cash Flow Used In Investing Activities

Cash flow from investing activities is derived from changes in oil and gas property balances and other investment activities. Cash flow used in investing activities for the three months ended May 31, 2021 and 2020 was $10,584 and $-0-, respectively.

Cash Flow Provided By Financing Activities

Cash flow from financing activities is derived from changes in long-term liability account balances, our borrowing activities or in equity account balances, excluding retained earnings. Cash flow provided by financing activities for the three months ended May 31, 2021 was $26,440 in comparison to $42,395 provided by financing activities in the three months ended May 31, 2020.

The following discussion is a summary of cash flows provided by or used in our financing activities at May 31, 2020.

Current debt (Short-term borrowings)

Note Payable

In December 2018, the Company was able to settle an outstanding balance owed to one of its third-party vendors. This settlement resulted in a $120,000 note payable being issued to the vendor. Additionally, the Company agreed to issue 2,000,000 shares of the Company's common stock as a part of the settlement agreement. Based on the closing price of the Company's common stock on the date of the settlement agreement, the value of the common stock transaction was determined to be $6,000. The common stock shares were issued during the twelve months ended February 29, 2020. The note has a maturity date of January 1, 2022 and bears an interest rate of 10% rate per annum. Monthly interest is accrued and payable on January 1st of each anniversary date until maturity of the note. At February 28, 2021, the accrued interest had not been paid and was outstanding. The accrued interest on the Note was $29,000 and $26,000 at May 31, 2021 and February 28, 2021, respectively.

Note Payable – Related Party

On December 22, 2020, the Company entered into a Secured Promissory Note (the "*Note*"), as borrower, with James Forrest Westmoreland and Angela Marie Westmoreland, Co-Trustees of the James and Angela Westmoreland Revocable Trust, or its assigns (the "*Noteholder*"), as the lender. James F. Westmoreland is the Company's Chairman, President and Chief Executive Officer. Pursuant to the Note, the Noteholder loaned the Company an aggregate principal amount of $155,548. After the deduction of loan fees of $10,929 the net proceeds from the loan were $144,619. The loan fees are being amortized as original issue discount (OID) over the term of the loan. The interest rate of the loan is 2.25%. The Note requires monthly payments on the Note balance until repaid in full. The maturity date of the Note is December 21, 2035. For the three months ended May 31, 2021, the Company made principal payments of $2,128 and amortized debt discount of $182. The obligations under the Note are secured by a lien on and security interest in the Company's oil and gas assets located in Kern County, California, as described in a Deed of Trust entered into by the Company in favor of the Noteholder to secure the obligations under the Note. Such lien shall be a first priority lien, subject only to a pre-existing lien filed by a working interest partner of the Company.

The Company may prepay the Note at any time. Upon the occurrence of any Event of Default and expiration of any applicable cure period, and at any time thereafter during the continuance of such Event of Default, the Noteholder may at its option, by written notice to the Company: (a) declare the entire principal amount of the Note, together with all accrued interest thereon and all other amounts payable hereunder, immediately due and payable; (b) exercise any of its remedies with respect to the collateral set forth in the Deed of Trust; and/or (c) exercise any or all of its other rights, powers or remedies under applicable law.

Current portion of note payable –related party balances at May 31, 2021 and February 28, 2021 are set forth in the table below:

	May 31, 2021	February 28, 2021
Note payable –related party, current portion	$ 8,655	$ 8,598
Unamortized debt issuance expenses	(729)	(728)
Note payable – related party, current portion, net	$ 7,927	$ 7,870

Note payable –related party long-term balances at May 31, 2021 and February 28, 2021 are set forth in the table below:

	May 31, 2021	February 28, 2021
Note payable – related party, non-current	$ 143,354	$ 145,540
Unamortized debt issuance expenses	(9,897)	(10,080)
Note payable– related party, non-current, net	$ 133,457	$ 135,460

Future estimated payments on the outstanding note payable – related party are set forth in the table below:

Twelve month periods ending February 28/29	
2022	$ 7,927
2023	8,159
2024	8,397
2025	8,642
2026	8,893
Thereafter	99,366
Total	$ 141,384

12% Subordinated Notes

The Company's 12% Subordinated Notes ("the Notes") issued pursuant to a January 2010 private placement offering to accredited investors, resulted in $595,000 in gross proceeds (of which $250,000 was from a related party) to the Company and accrue interest at 12% per annum, payable semi-annually on January 29th and July 29th. On January 29, 2015, the Company and 12 of the 13 holders of the Notes agreed to extend the maturity date of the Notes for an additional two years to January 29, 2017. Effective January 29, 2017, the maturity date of the Notes and the expiration date of the warrants that were issued in conjunction with the Notes were extended for an additional two years to January 29, 2019.

The Company has informed the Note holders that the payment of principal and final interest will be late and is subject to future financing being completed. The Notes principal of $565,000 was payable in full at the amended maturity date of the Notes, January 29, 2019, and has not been paid. The terms of the Notes, state that should the Board of Directors decide that the payment of the principal and any unpaid interest would impair the financial condition or operations of the Company, the Company may then elect a mandatory conversion of the unpaid principal and interest into the Company's common stock at a conversion rate equal to 75% of the average closing price of the Company's common stock over the 20 consecutive trading days preceding December 31, 2018. As of May 31, 2021, no conversion of the unpaid principal and interest into the Company's common stock has occurred. The accrued interest on the 12% Notes at May 31, 2021 and February 28, 2021 was $357,132 and $340,042, respectively.

12% Note balances at May 31, 2021 and February 28, 2021 are set forth in the table below:

	May 31, 2021	February 28, 2021
12% Subordinated Notes	$ 315,000	$ 315,000
12% Subordinated Notes, related party	250,000	250,000
Total 12% Subordinated Note balance	$ 565,000	$ 565,000

The accrued interest owed on the 12% Subordinated Note to the related party is presented on the Company's Balance Sheets under the caption *Accounts payable – related party* rather than under the caption *Accrued interest*.

Production Revenue Payable

Beginning in December 2018, the Company conducted a fundraising program to fund the drilling of future wells in California and Michigan and to settle some of its historical debt. The purchaser(s) of a production revenue payment interest would receive a production revenue payment on future wells to be drilled in California and Michigan in exchange for their purchase. As of May 31, 2021, the production revenue payment program balance was $950,100 of which $550,100 was owed to a related party - the Company's Chairman, President and Chief Executive Officer.

The production payment interest entitles the purchasers to receive production payments equal to twice their original amount paid, payable from a percentage of the Company's future net production payments from wells drilled after the date of the purchase and until the Production Payment Target (as described below) is met. The Company shall pay fifty percent of its net production payments from the relevant wells to the purchasers until each purchaser has received two times the purchase price (the "Production Payment Target"). Once the Company pays the purchasers amounts equal to the Production Payment Target, it shall thereafter pay a pro-rated eight percent (8%) of $1.3 million on its net production payments from the relevant wells to each of the purchasers. However, if the total raised is less than the target $1.3 million, then the payment will be a proportionate amount of the eight percent (8%). Additionally, if the Production Payment Target is not met within the first three years, the Company shall pay seventy-five percent of its production payments from the relevant wells to the purchasers until the Production Payment Target is met.

The Company accounted for the amounts received from these sales in accordance with ASC 470-10-25 and 470-10-35 which require amounts recorded as debt to be amortized under the interest method as described in ASC 835-30, Interest Method. Consequently, the program balance of $950,100 has been recognized as a production revenue payable. The Company determined an effective interest rate based on future expected cash flows to be paid to the holders of the production payment interests. This rate represents the discount rate that equates estimated cash flows with the initial proceeds received from the sales and is used to compute the amount of interest to be recognized each period. Estimating the future cash outflows under this agreement requires the Company to make certain estimates and assumptions about future revenues and payments and such estimates are subject to significant variability. Therefore, the estimates are likely to change which may result in future adjustments to the accretion of the interest expense and the amortized cost based carrying value of the related payables.

Accordingly, the Company has estimated the cash flows associated with the production revenue payments and determined a discount of $1,077,642 as of May 31, 2021, which is being accounted as interest expense over the estimated period over which payments will be made based on expected future revenue streams. For the three months ended May 31, 2021 and 2020, amortization of the debt discount on these payables amounted to $30,525 and $31,970, respectively, which has been included in interest expense in the statements of operations.

Production revenue payable balances at May 31, 2021 and February 28, 2021 are set forth in the table below:

	May 31, 2021	February 28, 2021
Estimated payments of production revenue payable	$ 2,029,742	$ 2,000,258
Less: unamortized discount	(495,795)	(496,836)
	1,533,947	1,503,422
Less: current portion	(98,336)	(111,753)
Net production revenue payable – long term	$ 1,435,611	$ 1,391,669

Line of Credit

The Company has an existing $890,000 line of credit for working capital purposes with UBS Bank USA ("UBS"), established pursuant to a Credit Line Agreement dated October 24, 2011 that is secured by the personal guarantee of its Chairman, President and Chief Executive Officer. On July 10, 2017, a $700,000 portion of the outstanding line of credit balance was converted to a 24 month fixed term annual interest rate of 3.244% with interest payable monthly. On July 10, 2019, the 24-month fixed term loan amount of

$700,000 was renewed at the same annual percentage interest rate of 3.244% for an additional 24 months. The remaining principal balance of the line of credit has a stated reference rate of 0.249% + 337.5 basis points with interest payable monthly. The reference rate is based on the 30 day LIBOR ("London Interbank Offered Rate") and is subject to change from UBS.

During the three months ended May 31, 2021 and 2020, the Company did not receive any advances on the line of credit. During the three months ended May 31, 2021 and 2020, the Company made payments to the line of credit of $15,000 and $15,000, respectively. Interest converted to principal for the three months ended May 31, 2021 and 2020 was $6,892 and $7,389, respectively. At May 31, 2021 and February 28, 2021, the line of credit had an outstanding balance of $832,796 and $840,904, respectively.

Paycheck Protection Program (PPP) Loans

In March 2020, the Coronavirus Aid, Relief, and Economic Security Act commonly referred to as the CARES Act became law. One component of the CARES Act was the paycheck protection program ("PPP") which provides small business with the resources needed to maintain their payroll and cover applicable overhead. The PPP is implemented by the Small Business Administration ("SBA") with support from the Department of the Treasury. The Company applied for, and was accepted to participate in this program. On May 11, 2020, the Company received funding for approximately $74,355. On February 12, 2021, the Company applied for loan forgiveness under the provisions of Section 1106 of the CARES Act. Loan forgiveness was subject to the sole approval of the SBA. On February 23, 2021, the SBA notified our lender that the loan was forgiven and repaid the loan in full.

On March 4, 2021, the Company applied for, and was accepted to participate in the SBA PPP Second Draw program with funding pursuant to the Economic Aid Act that was passed in December, 2020. On March 15, 2021, Daybreak received funding for $72,800. The second-draw loan is a five-year loan with a maturity date of March 6, 2026. The loan bears an annual interest rate of 1%. The monthly payment is $1,670 with the first payment due on July 6, 2022. We intend to use the loan proceeds to partially subsidize direct payroll, rent and utility expenses. It is the Company's intent to apply for loan forgiveness for the PPP Second Draw PPP loan. Loan forgiveness is subject to the sole approval of the SBA.

Encumbrances

On October 17, 2018, a working interest partner in California filed a UCC financing statement in regards to payables owed to the partner by the Company. As of May 31, 2021 we had no encumbrances on our crude oil project in Michigan.

Operating Leases

We lease approximately 988 rentable square feet of office space from an unaffiliated third party for our corporate office located in Spokane Valley, Washington. Additionally, we lease approximately 416 and 695 rentable square feet from unaffiliated third parties for our regional operations office in Friendswood, Texas and storage and auxiliary office space in Wallace, Idaho, respectively. The lease in Friendswood is a 12 month lease that expires in October 2021 and as such is considered a short-term lease. The Company has elected to not apply the recognition requirements of ASC 842 to this short-term lease. The Spokane Valley and Wallace leases are currently on a month-to-month basis. Our lease agreements do not contain any residual value guarantees, restrictive covenants or variable lease payments. We have not entered into any financing leases.

We determine if an arrangement is a lease at inception. Operating leases are recorded in operating lease right of use assets, net, operating lease liability – current, and operating lease liability, long-term on its balance sheet.

Rent expense for the three months ended May 31, 2021 and 2020 was $5,947 and $5,872, respectively.

Capital Commitments

Daybreak has ongoing capital commitments to develop certain leases pursuant to their underlying terms. Failure to meet such ongoing commitments may result in the loss of the right to participate in future drilling on certain leases or the loss of the lease itself. These ongoing capital commitments may also cause us to seek additional capital from sources outside of the Company. The current uncertainty in the credit and capital markets, and the economic downturn, may restrict our ability to obtain needed capital.

Management Plans to Continue as a Going Concern

We continue to implement plans to enhance Daybreak's ability to continue as a going concern. The Company currently has a net revenue interest in 20 producing crude oil wells in our East Slopes Project located in Kern County, California. The revenue from these wells has created a steady and reliable source of revenue for the Company. Our average working interest in these wells is 36.6% and the average net revenue interest is 28.5%.

In December 2019, the 2019 novel coronavirus ("COVID-19") surfaced in Wuhan, China. The World Health Organization declared a global emergency on January 30, 2020, with respect to the outbreak and most countries throughout the world initiated severe travel restrictions to and from other countries. This widespread health crisis and the governmental restrictions associated with it, have adversely affected demand for crude oil, depressed crude oil prices, and affected our ability to access capital. These factors, in turn, have had a negative impact on our operations, and financial condition as evidenced by the unprecedented decline in crude oil prices and our revenues during this same time period.

On March 27, 2020, the Coronavirus Aid, Relief, and Economic Security Act commonly referred to as the CARES Act became law. One component of the CARES Act was the paycheck protection program ("PPP") which provides small business with the resources needed to maintain their payroll and cover applicable overhead. The PPP is implemented by the Small Business Administration ("SBA") with support from the Department of the Treasury. The Company applied for, and was accepted to participate in this program. On May 11, 2020, the Company received funding for approximately $74,355. In February 2021, the Company applied for full loan forgiveness and later that month was notified by our lender that the SBA had forgiven our original loan in full. On March 15, 2021, the Company received $72,800 in funding through the SBA second draw paycheck protection program. Second Draw PPP loans can be used to help fund payroll costs, including benefits. Funds can also be used to pay for mortgage interest, rent and utilities over a 24 week period. We plan on also applying for loan forgiveness on this second draw PPP loan.

We anticipate revenues will continue to increase as the Company participates in the drilling of more wells in the East Slopes Project in California and as our drilling operations begin in Michigan. However given the current volatility and instability in hydrocarbon prices, the timing of any drilling activity in California and Michigan will be dependent on a sustained improvement in hydrocarbon prices and a successful refinancing or restructuring of our credit facility.

We believe that our liquidity will improve when there is a sustained improvement in hydrocarbon prices. Our sources of funds in the past have included the debt or equity markets and the sale of assets. While the Company does have positive cash flow from its crude oil properties, it has not yet established a positive cash flow on a company-wide basis. It will be necessary for the Company to obtain additional funding from the private or public debt or equity markets in the future. However, we cannot offer any assurance that we will be successful in executing the aforementioned plans to continue as a going concern.

Our financial statements as of May 31, 2021 do not include any adjustments that might result from the inability to implement or execute Daybreak's plans to improve our ability to continue as a going concern.

Critical Accounting Policies

Refer to Daybreak's Annual Report on Form 10-K for the fiscal year ended February 28, 2021.

Off-Balance Sheet Arrangements

As of May 31, 2021, we did not have any off-balance sheet arrangements or relationships with unconsolidated entities or financial partners that have been, or are reasonably likely to have, a material effect on our financial position or results of operations.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

As a smaller reporting company, we are not required to provide the information otherwise required by this Item.

ITEM 4. CONTROLS AND PROCEDURES

Management's Evaluation of Disclosure Controls and Procedures

As of the end of the reporting period, May 31, 2021, an evaluation was conducted by Daybreak management, including our President and Chief Executive Officer, who is also serving as our interim principal finance and accounting officer, as to the effectiveness of the design and operation of our disclosure controls and procedures pursuant to Rule 13a-15(e) of the Exchange Act. Such disclosure controls and procedures are designed to ensure that information required to be disclosed by a company in the reports that it files under the Exchange Act is recorded, processed, summarized and reported within required time periods specified by the SEC rules and forms. Additionally, it is vital that such information is accumulated and communicated to our management, including our President and Chief Executive Officer, in a manner to allow timely decisions regarding required disclosures. Based on that evaluation, our management concluded that our disclosure controls were effective as of May 31, 2021.

Changes in Internal Control over Financial Reporting

There have not been any changes in the Company's internal control over financial reporting during the three months ended May 31, 2021 that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

Limitations

Our management does not expect that our disclosure controls or internal controls over financial reporting will prevent all errors or all instances of fraud. A control system, no matter how well designed and operated, can provide only reasonable, not absolute, assurance that the control system's objectives will be met. Further, the design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs.

Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within our company have been detected. These inherent limitations include the realities that judgments in decision-making can be faulty, and that breakdowns can occur because of simple error or mistake. Controls can also be circumvented by the individual acts of some persons, by collusion of two or more people, or by management override of the controls. The design of any system of controls is based in part upon certain assumptions about the likelihood of future events, and any design may not succeed in achieving its stated goals under all potential future conditions.

Over time, controls may become inadequate because of changes in conditions or deterioration in the degree of compliance with policies or procedures. Because of the inherent limitation of a cost-effective control system, misstatements due to error or fraud may occur and not be detected.

PART II
OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

None

ITEM 1A. RISK FACTORS

In addition to the other information set forth in this report, you should carefully consider the factors discussed in Part I, Item 1A. Risk Factors in our Annual Report on Form 10-K for the period ended February 28, 2021, which could materially affect our business, financial condition or future results. The risks described in this report are not the only risks we face. Additional risks and uncertainties not currently known to us or that we currently deem to be immaterial could have a material adverse effect on our business, financial condition and results of operations.

ITEM 6. EXHIBITS

The following Exhibits are filed as part of the report:

Exhibit Number	Description
31.1[(1)]	Certification of principal executive and principal financial officer as required pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1[(1)]	Certification of principal executive and principal financial officer as required pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101.INS[(2)]	XBRL Instance Document
101.SCH[(2]	XBRL Taxonomy Schema
101.CAL[(2)]	XBRL Taxonomy Calculation Linkbase
101.DEF[(2)]	XBRL Taxonomy Definition Linkbase
101.LAB[(2)]	XBRL Taxonomy Label Linkbase
101.PRE[(2)]	XBRL Taxonomy Presentation Linkbase

(1) Filed herewith.
(2) Furnished herewith.

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.

DAYBREAK OIL AND GAS, INC.

By: /s/ JAMES F. WESTMORELAND
James F. Westmoreland, its
President, Chief Executive Officer and interim
principal finance and accounting officer
(Principal Executive Officer, Principal Financial
Officer and Principal Accounting Officer)

Date: July 14, 2021

Exhibit 31.1

Certification

I, James F. Westmoreland, certify that:

(1) I have reviewed this interim report on Form 10-Q of Daybreak Oil and Gas, Inc.

(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 15(d)-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 my supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to me 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 most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

(5) The registrant's other certifying officer and 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.

Date: July 14, 2021

By /s/ JAMES F. WESTMORELAND
James F. Westmoreland, President, Chief Executive Officer
and interim principal finance and accounting officer
(Principal Executive Officer, Principal Financial Officer and Principal Accounting Officer)

Exhibit 32.1

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

In connection with the Interim Report of Daybreak Oil and Gas, Inc. on Form 10-Q for the period ending May 31, 2021, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, the undersigned, in the capacity and on the date indicated below, hereby certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

(1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

(2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: July 14, 2021

By /s/ JAMES F. WESTMORELAND
James F. Westmoreland, President, Chief Executive Officer
and interim principal finance and accounting officer
(Principal Executive Officer, Principal Financial Officer and Principal Accounting Officer)