ROOSTER ENERGY LTD.

Condensed Interim Consolidated Financial Statements

Three and Nine Months Ended September 30, 2014 and 2013

(unaudited)

NOTICE OF NO AUDITOR REVIEW

Pursuant to National Instrument 51-102, Part 4, subsection 4.3(3)(a), the accompanying unaudited condensed interim consolidated financial statements have been prepared by management. The Company's independent auditors have not performed a review of these financial statements in accordance with standards established by the Canadian Institute of Chartered Accountants for a review of interim financial statements by an entity's auditor.

Contents

Rooster Energy Ltd.
Condensed Interim Consolidated Balance Sheets
(amounts in US dollars)
(unaudited)

	Notes	September 30, 2014	December 31, 2013
Assets			
Current assets			
Cash and cash equivalents		$ 1,582,703	$ 964,040
Restricted cash	3(b), 7	3,462,000	5,620,635
Accounts receivable	3(b)	6,807,059	4,071,505
Prepaid expenses and deposits	8	2,562,958	1,173,832
Total current assets		14,414,720	11,830,012
Exploration and evaluation assets	4	-	186,152
Property and equipment	5	105,413,893	95,208,469
Asset retirement deposits	7	300,000	300,000
Total assets		$ 120,128,613	$ 107,524,633
Liabilities and shareholders' equity			
Current liabilities			
Accounts payable and accrued liabilities	3(c)	21,898,048	19,839,404
Loans payable	6	39,458,887	27,469,712
Accrued interest payable	6	5,938,500	2,016,897
Due to related parties	16	5,172,044	3,970,348
Asset retirement obligations	7	5,392,167	5,392,167
Total current liabilities		77,859,646	58,688,528
Long-term liabilities			
Loans payable	6	-	3,223,626
Financing warrants	6	697,000	1,092,000
Accrued interest payable	6	-	84,618
Deferred income taxes	12(b)	4,438,000	4,575,000
Asset retirement obligations	7	12,153,969	13,203,660
Total liabilities		95,148,615	80,867,432
Shareholders' equity			
Share capital	9	40,911,182	40,911,182
Contributed surplus	10	2,673,569	1,511,146
Deficit		(18,604,753)	(15,765,127)
Total shareholders' equity		24,979,998	26,657,201
Total liabilities and shareholders' equity		$ 120,128,613	$ 107,524,633

Subsequent events (notes 3, 6, 15 and 18)
Commitments (note15)
Contingencies (note 17)

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

Approved by the Board: ***(signed)”Paul Crilly “*** ***(signed)”Richard S. Buski “***

Rooster Energy Ltd.

Condensed Interim Consolidated Statements of Income (Loss) and Comprehensive Income (Loss)

(amounts in US dollars)
(unaudited)

	Notes	Three Months Ended September 30, 2014	Three Months Ended September 30, 2013	Nine Months Ended September 30, 2014	Nine Months Ended September 30, 2013
Revenue					
Petroleum and natural gas revenue		$ 6,507,598	$ 10,630,237	$ 22,079,367	$ 32,920,020
Expenses					
Lease operating		4,327,571	2,791,161	10,454,413	9,415,848
Depreciation and depletion	5	1,213,634	2,142,053	3,853,200	6,806,797
Exploration and evaluation, net	5	-	3,205	-	2,162,364
General and administrative		1,245,486	1,243,870	3,607,286	3,737,816
Transaction costs		310,357	-	310,357	-
Bad debt expense (recovery)	3(b)	(2,734,759)	125,584	(2,558,483)	2,796,446
Impairment recovery	5	-	-	(714,050)	-
Stock-based compensation	10	344,521	200,085	1,162,423	595,382
Total expenses		4,706,810	6,505,958	16,115,146	25,514,653
Operating income (loss)		1,800,788	4,124,279	5,964,221	7,405,367
Unrealized gain on financing warrants	6	682,000	921,000	395,000	(543,000)
Finance expenses	11	(4,104,884)	(1,861,305)	(9,335,847)	(4,426,071)
Income (loss) before income taxes		(1,622,096)	3,183,974	(2,976,626)	2,436,296
Deferred income tax expense (recovery)	12(a)	(441,000)	1,161,000	(137,000)	1,076,000
Income (loss) and comprehensive income (loss)		$ (1,181,096)	$ 2,022,974	$ (2,839,626)	$ 1,360,296
Income (loss) per share	13				
Basic		$ (0.01)	$ 0.02	$ (0.03)	$ 0.01
Diluted		$ (0.01)	$ 0.02	$ (0.03)	$ 0.01

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

Rooster Energy Ltd.
Condensed Interim Consolidated Statements of Changes in Shareholders' Equity
(amounts in US dollars)
(unaudited)

	Notes	Number of Common Shares [1]	Common Share Capital Stated Value	Number of Proportionate Voting Shares[1]	Proportionate Voting Shares Stated Value	Contributed Surplus	Deficit	Total Shareholders' Equity
Balance, December 31, 2012		40,394,823	$ 11,746,587	65,071	$ 29,162,552	$ 507,298	$ (13,731,276)	$ 27,685,161
Issued on cashless exercise of stock options	10	2,500	2,043	-	-	(2,043)	-	-
Stock-based compensation	10	-	-	-	-	595,382	-	595,382
Income for the period		-	-	-	-	-	1,360,296	1,360,296
Balance, September 30, 2013		40,397,323	11,748,630	65,071	29,162,552	1,100,637	(12,370,980)	29,640,839
Stock-based compensation	10	-	-	-	-	410,509	-	410,509
Loss for the period		-	-	-	-	-	(3,394,147)	(3,394,147)
Balance, December 31, 2013		40,397,323	11,748,630	65,071	29,162,552	1,511,146	(15,765,127)	26,657,201
Stock-based compensation	10	-	-	-	-	1,162,423	-	1,162,423
Loss for the period		-	-	-	-	-	(2,839,626)	(2,839,626)
Balance, September 30, 2014		40,397,323	$ 11,748,630	65,071	$ 29,162,552	$ 2,673,569	$ (18,604,753)	$ 24,979,998

[1] The issued share capital of the Company consists of 40,397,323 common shares and 65,071 Proportionate Voting Shares (1,000 to 1 conversion rights), for issued share capital on a fully diluted basis equivalent to 105,468,323 common shares (prior to the exercise of 9,468,404 stock options and 9,000,000 warrants).

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

Rooster Energy Ltd.

Condensed Interim Consolidated Statements of Cash Flows

(amounts in US dollars)
(unaudited)

	Notes	Three Months Ended September 30, 2014	Three Months Ended September 30, 2013	Nine Months Ended September 30, 2014	Nine Months Ended September 30, 2013
Cash and cash equivalents provided by (used in):					
Cash flows from operating activities					
Net Income (loss)		$ (1,181,096)	$ 2,022,974	$ (2,839,626)	$ 1,360,296
Adjustments for:					
Depreciation and depletion	5	1,213,634	2,142,053	3,853,200	6,806,797
Dry hole costs included in exploration and evaluation expenses	5	-	3,205	-	2,162,364
Impairment recovery	5	-	-	(714,050)	-
Stock-based compensation	10	344,521	200,085	1,162,423	595,382
Unrealized (gain) loss on financing warrants	6	(682,000)	(921,000)	(395,000)	543,000
Unrealized foreign exchange (gain) loss on related party credit facility	11	(238,058)	-	(185,113)	-
Accretion of loans payable discounts	11	409,564	390,906	2,440,507	1,127,369
Asset retirement obligation accretion	11	119,449	142,185	356,544	426,556
Deferred income tax expense (recovery)	12(a)	(441,000)	1,161,000	(137,000)	1,076,000
Funds generated from operations		(454,986)	5,141,408	3,541,885	14,097,764
Cash abandonment costs	7	(1,054,570)	(45,170)	(1,490,889)	(769,150)
Changes in non-cash working capital	14	11,184,988	2,501,417	9,301,259	3,935,255
Net cash flows provided by operating activities		9,675,432	7,597,655	11,352,255	17,263,869
Cash flows from (used in) investing activities					
Capital expenditures for petroleum and natural gas properties	5	(10,508,918)	(16,368,560)	(13,054,342)	(26,266,088)
Capital expenditures for office furnishings and improvements	5	(2,513)	(821)	(19,426)	(23,324)
Exploration and evaluation expenditures related to dry holes	5	-	(3,205)	-	(2,162,364)
Proceeds relating to assets and liabilities held for sale		-	-	-	159,255
Changes in non-cash working capital	14	(4,125,770)	3,169,418	(6,688,151)	2,836,133
Net cash flows used in investing activities		(14,637,201)	(13,203,168)	(19,761,919)	(25,456,388)
Cash flows from financing activities					
Proceeds from loans payable	6	-	-	6,500,000	-
Change in accrued interest payable		2,633,274	639,704	3,847,140	824,671
Changes in non-cash working capital		(1,318,813)	-	(1,318,813)	-
Net cash flows provided by financing activities		1,314,461	639,704	9,028,327	824,671
Net increase (decrease) in cash and cash equivalents		(3,647,308)	(4,965,809)	618,663	(7,367,848)
Cash and cash equivalents, beginning of period		5,230,011	4,965,809	964,040	7,367,848
Cash and cash equivalents, end of period	14	$ 1,582,703	$ -	$ 1,582,703	$ -

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

1. General business description

Rooster Energy Ltd. (the "Company") is an independent company engaged in the acquisition, development and exploration of petroleum and natural gas. The Company's only area of operations is in the US Gulf of Mexico. The Company is incorporated in Canada under the British Columbia Corporations Act and is traded on the TSX Venture Exchange under the symbol "COQ".

The address and principal place of business of the Company is 16285 Park Ten Place, Suite 120, Houston, Texas, USA, 77804.

2. Basis of preparation

(a) Statement of compliance

These condensed interim consolidated financial statements have been prepared in accordance with International Accounting Standard 34 *Interim Financial Reporting* ("IAS 34"), as issued by the International Accounting Standards Board ("IASB"). Accordingly, certain financial information and disclosures normally included in annual financial statements prepared in accordance with International Financial Reporting Standards ("IFRS") as issued by the IASB have been omitted or condensed.

These condensed interim consolidated financial statements have been prepared using the same accounting policies and methods as those used in the annual financial statements, except as outlined below, and should be read in conjunction with the Company's annual audited consolidated financial statements for the year end December 31, 2013.

These condensed interim consolidated financial statements were approved and authorized for issuance by the Board of Directors on November 21, 2014.

(b) Changes in accounting policies

The Company adopted the following new standards and amendments on January 1, 2014:

The IASB amended IAS 39 to allow hedge accounting to continue in a situation where a derivative, which has been designated as a hedging instrument, is novated to effect clearing with a central counterparty as a result of laws or regulation, if specific conditions are met (in this context, a novation indicates that parties to a contract agree to replace their original counterparty with a new one). The amendment is effective for annual periods beginning on or after January 1, 2014 and did not have an impact on the Company's results or financial position.

The IASB amended IAS 32, "Financial Instruments: Presentation" ("IAS 32") to clarify certain requirements for offsetting financial assets and liabilities. The amendment addresses the meaning and application of the concepts of legally enforceable right of set-off and simultaneous realization and settlement. IAS 32 relates to presentation and disclosures. The amendment is effective for annual periods beginning on or after January 1, 2014 and did not have an impact on the Company's results or financial position.

The IASB amended IAS 36, "Impairment of Assets" to require disclosure of the recoverable amount of an asset (including goodwill) or a cash generating-unit ("CGU") when an impairment loss has been recognized or reversed in the period. When the recoverable amount is based on fair value less costs of disposal, the valuation techniques and key assumptions must also be disclosed.

The Company adopted International Financial Reporting Interpretations Committee ("IFRIC") 21 – Levies ("IFRIC 21") on the accounting for levies imposed by governments clarifies the obligating event that gives rise to a liability to pay a levy. Adoption of this standard had no material impact on the Company's financial statements.

(c) Basis of measurement

These condensed interim financial statements have been prepared on the historical cost basis, except for certain financial instruments which are measured at fair value.

(d) Functional and presentation currency

These condensed interim financial statements are presented in US dollars, except as otherwise noted, which is the functional currency of the Company and its subsidiaries.

(e) Basis of consolidation

These condensed interim consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries, Rooster Energy, L.L.C., Rooster Petroleum LLC, Rooster Oil & Gas LLC and Probe Resources US Ltd.

(f) Use of estimates and judgments

The preparation of condensed interim financial statements in conformity with IFRS requires management to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, earnings and expenses. Actual results may differ from these estimates.

Estimates and judgments are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. Accounting estimates will, by definition, seldom equal the actual results. Revisions to accounting estimates are recognized in the period in which the estimates are revised and in any future years affected.

There have been no significant changes in the Company's critical accounting estimates and assumptions applied during the nine months ended September 30, 2014 relative to those disclosed in the Company's most recent annual audited consolidated financial statements as at and for the year ended December 31, 2013.

3. Financial instruments and risk management

(a) Fair value of financial instruments

The fair values of cash and cash equivalents, restricted cash, accounts receivable, asset retirement deposits, accounts payable and accrued liabilities, loans payable, accrued interest payable, and due to related parties, approximate their carrying values due to the short-term maturity of those instruments.

(amounts in US dollars)

The fair values of any notional derivative contracts, such as forward contracts, collars and swaps, are determined by discounting the difference between the contracted prices and published forward price curves as at the balance sheet date, using the remaining contracted petroleum and natural gas volumes and a risk-free interest rate (based on published government rates) adjusted for the Company's non-performance risk of the counterparty.

The significance of inputs used in making fair value measurements for financial instruments carried at fair value are examined and classified according to a fair value hierarchy. Fair values of assets and liabilities included in Level 1 are determined by reference to quoted prices in active markets for identical assets and liabilities. Assets and liabilities in Level 2 include valuations using inputs other than quoted prices for which all significant outputs are observable, either directly or indirectly, and are based on valuation models and techniques where the inputs are derived from quoted indices. Level 3 valuations are based on inputs that are unobservable and significant to the overall fair value measurement.

Cash and cash equivalents are measured at fair value based on a Level 1 designation. Financing warrants are measured using a Level 2 designation.

The valuation of the Company's assets and liabilities measured on a fair value basis at September 30, 2014 and December 31, 2013, are as follows:

	Total	Level 1	Level 2	Level 3
September 30, 2014				
Assets				
Cash and cash equivalents	$ 1,582,703	$ 1,582,703	$ -	$ -
Liabilities				
Financing warrants	$ 697,000	$ -	$ 697,000	$ -

	Total	Level 1	Level 2	Level 3
December 31, 2013				
Assets				
Cash and cash equivalents	$ 964,040	$ 964,040	$ -	$ -
Liabilities				
Financing warrants	$ 1,092,000	$ -	$ 1,092,000	$ -

(amounts in US dollars)

(b) Credit risk

Credit risk is the risk of financial loss to the Company if a customer or counterparty to a financial instrument fails to meet its contractual obligations. The maximum exposure to credit risk at September 30, 2014 and December 31, 2013, is as follows:

	September 30, 2014	December 31, 2013
Cash and cash equivalents	$ 1,582,703	$ 964,040
Restricted cash	3,462,000	5,620,635
Accounts receivable	6,807,059	4,071,505
Asset retirement deposits	300,000	300,000
	$ 12,151,762	$ 10,956,180

Cash and cash equivalents

Cash and cash equivalents may include cash bank balances and short-term deposits. The Company manages the credit exposure related to cash and cash equivalents by selecting financial institutions with high credit ratings and monitors short-term deposits to ensure an adequate rate of return. Given these credit ratings, management does not expect any counterparty to fail to meet its obligations.

Restricted cash

As of September 30, 2014 the Company had $3,462,000 (December 31, 2013 - $3,462,000) in restricted cash representing cash collateral for performance bonds for specific well and facility abandonments (note 7).

In addition, restricted cash at December 31, 2013 included $2,158,635 of disputed revenue proceeds held in escrow related to Vermilion Area Block 376 #A-3 and A-4 wells, with the offsetting amount included in accounts payable and accrued liabilities. The amount was paid during the three months ended September 30, 2014 as a result of the settlement as disclosed further in note 17.

All funds are held in financial institutions with high credit ratings and as such, management does not expect any credit risk losses.

Accounts receivable

All of the Company’s operations are conducted in the United States. The Company’s exposure to credit risk is influenced mainly by the individual characteristics of each customer and/or partner. Significant changes in industry conditions and risks that negatively impact customers' or partners’ ability to generate cash flow will increase the risk of not collecting receivables. Management believes the risk is mitigated by the size and reputation of the companies to which they extend credit.

(amounts in US dollars)

During the nine month period ended September 30, 2014, the Company sold a substantial portion of its product to one customer. Sales to this customer aggregated approximately $16.8 million or approximately 76% of total revenue (September 30, 2013 – three customers for $30.2 million and 92%). At September 30, 2014, amounts due from these customers included in accounts receivable totalled approximately $1.4 million (December 31, 2013 - $2.2 million). The Company historically has not experienced any collection issues related to these customers. The credit rating of the customers of the Company's petroleum and natural gas production is closely monitored by the Company's management to ensure no collection issues arise.

When determining whether past due accounts are collectible, the Company factors in the past credit history of the counterparties. The Company considers all amounts greater than 90 days as past due.

As of September 30, 2014, substantially all of the Company's accounts receivable are due from petroleum and natural gas purchasers and joint operation partners. Management has evaluated receivables for collectability and as such, has recorded an allowance for doubtful accounts totalling $603,952 (December 31, 2013 - $3,187,396). Bad debt (recovery) expense for the three month periods ended September 30, 2014 and 2013 totalled $(2,734,759) and $125,584, respectively, and for the nine month periods ended September 30, 2014 and 2013 totalled $(2,558,483), and $2,796,446, respectively. Bad debt expense for 2013 primarily relates to an allowance for non-payment of operating costs and capital expenditures by joint operating partners. Please refer to note 5 regarding the recovery of bad debt expense for the three and nine months ended September 30, 2014.

As of September 30, 2014 and December 31, 2013, the Company's accounts receivable were comprised of the following:

	September 30, 2014	December 31, 2013
Petroleum and natural gas revenue	$ 2,012,783	$ 2,432,759
Joint operation receivables	5,397,728	4,826,142
	7,410,511	7,258,901
Allowance for doubtful accounts	(603,452)	(3,187,396)
Total accounts receivable	$ 6,807,059	$ 4,071,505

As of September 30, 2014 and December 31, 2013, the Company's accounts receivables were aged as follows:

	September 30, 2014	December 31, 2013
Current (0 - 30 days)	$ 6,551,128	$ 4,062,088
31 to 60 days	97,165	33,199
61 to 90 days	42,552	53,068
Past due (greater than 90 days)	719,666	3,110,546
Allowance for doubtful accounts	(603,452)	(3,187,396)
Total accounts receivable	$ 6,807,059	$ 4,071,505

(amounts in US dollars)

Asset retirement deposits

Asset retirement deposits (note 7) consist of amounts deposited to secure a performance bond related to asset retirement obligations which were acquired by the Company in connection with the reverse acquisition of Probe Resources Ltd. during 2012. The exposure to credit risk has been assessed by management to be minimal.

(c) Liquidity risk

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they are due. The Company's approach to managing liquidity is to ensure it will have sufficient liquidity to meet its liabilities when due.

The Company's trade accounts payable are normally due within 30 - 60 days from receipt of invoice.

The Company's accounts payable and accrued liabilities as of September 30, 2014 and December 31, 2013, are aged as follows:

	September 30, 2014	December 31, 2013
Current (0 - 30 days)	$ 18,110,458	$ 7,960,672
31 to 60 days	835,370	1,729,709
61 to 90 days	1,576,767	6,307,520
Greater than 90 days	1,375,453	3,841,503
Total accounts payable and accrued liabilities	$ 21,898,048	$ 19,839,404

The repayment terms relating to the Company's due to related parties are disclosed in notes 16 and 18.

The repayment terms relating to the Company's loans payable are disclosed in notes 6 and 18.

The Company is also subject to future commitments and contingencies as disclosed in notes 15 and 17.

Refer to note 3(e) for the Company's management of capital.

At September 30, 2014, the Company had a working capital deficiency of $63,444,926, including outstanding loans payable amounts which were due within a year from September 30, 2014. Management has taken a number of steps to address the Company's liquidity situation as further described in note 18. As a result, management believes that it will be able to satisfy its liabilities as they become due over the next twelve months.

(d) Market risk

Market risk is the risk that changes in market prices, such as commodity prices, interest rates and foreign exchange rates will affect the Company's net income or the value of financial instruments. The objective of the Company is to manage and mitigate market risk exposures within acceptable limits, while maximizing returns.

Foreign currency risk

Prices received by the Company for petroleum and natural gas are generally denominated in US dollars. The Company had nominal working capital amounts denominated in currencies other than US dollars other than the related party subordinated secured credit facility which is denominated in Canadian dollars ("CDN") (note 6), and had no forward exchange rate contracts in place as of or during the period ended September 30, 2014 or the year ended December 31, 2013. Shares of the Company are traded in Canadian dollars.

A 5% upward (downward) change in the US-CDN exchange rate would increase (decrease) the Company's net loss for the three and nine months ended September 30, 2014 by approximately $30,000 and $90,000, respectively, based on the outstanding balance of the related party subordinated secured credit facility at September 30, 2014.

Interest rate risk

Interest rate risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates. The Company is exposed to interest rate risk to the extent that changes in market interest rates impact floating rate borrowings. The Company's loans payable at September 30, 2014 are at fixed interest rates (note 6) and therefore are not subject to interest rate risk. The Company had no interest rate swaps or financial contracts in place as of or during nine month period ended September 30, 2014.

Commodity price risk

The Company entered into certain fixed price physical delivery contracts during 2013 pursuant to which it was agreed to sell certain quantities of natural gas and crude oil. These contracts were entered into for the purpose of physical delivery of a non-financial item; therefore, the physical delivery contracts are not fair valued. Settlements on these contracts are included in petroleum and natural gas revenue as they occur. The Company currently does not have any derivative financial commodity contracts.

As of September 30, 2014, the Company did not have any fixed price physical delivery contracts outstanding. Please refer to note 18 regarding fixed swap agreements entered into subsequent to September 30, 2014.

(e) Capital management

The Company's capital management policy is to maintain a strong capital base that optimizes the Company's ability to grow, to maintain investor and creditor confidence and to provide a platform to create value for its shareholders. The Company maintains a flexible capital structure to maximize its ability to pursue petroleum and natural gas exploration opportunities and sustain the future development of the business. The Company monitors the level of risk associated for each capital project to balance the proportion of debt and equity in its capital structure. The Company's management is responsible for managing the Company's capital and does so through quarterly meetings and regular reviews of financial information. The Company's Board of Directors are responsible for overseeing this process. The Company considers working capital to form its capital structure and strives to maintain positive working capital. When working capital deficits arise in the normal course of operations, the Company responds by minimizing capital and operating expenses and, when prudent, through selective asset divestitures until adequate working capital is restored.

(amounts in US dollars)

The Company's working capital surplus (deficiency) is as follows:

	September 30, 2014	December 31, 2013
Current assets	$ 14,414,720	$ 11,830,012
Current liabilities	(77,859,646)	(58,688,528)
Total	$ (63,444,926)	$ (46,858,516)

The Company is required to meet certain financial covenants relating to its loans payable as disclosed in note 6 and see also note 18 for certain other financial covenants the Company will be required to meet. The Company is not subject to any other externally imposed capital requirements. There has been no change to management's approach to managing capital during the nine months ended September 30, 2014. Please refer to note 18 regarding how the Company has addressed its working capital deficiency at September 30, 2014. As a result, management believes that the Company will be able to meet all of its obligations when due.

4. Exploration and evaluation assets and expenses

	September 30, 2014	December 31, 2013
Balance, beginning of period	$ 186,152	$ -
Exploration and evaluation expenditures	-	186,152
Transfers to property and equipment (note 5)	(186,152)	-
Balance, end of period	$ -	$ 186,152

Exploration and evaluation assets include undeveloped properties, seismic and other assets that management has not fully evaluated for technical feasibility and commercial viability. Capital expenditures represent the Company's share of costs incurred on exploration and evaluation assets during the period. Transfers to property and equipment, if any, represent successful drilling and related costs for which technical feasibility and commercial viability are determined to exist.

Exploration and evaluation expenses are charged to income (loss) and include pre-license seismic and other pre-license evaluation costs incurred, net of any recoveries from joint operations partners, and transfers from property and equipment related to unsuccessful drilling costs.

(amounts in US dollars)

5. Property and equipment

	Petroleum and natural gas interests	Office furnishings and improvements	Total
Cost			
Balance at December 31, 2012	$ 103,969,910	$ 604,160	$ 104,574,070
Additions	38,633,909	25,228	38,659,137
Transfers to exploration and evaluation expenses related to dry holes	(2,483,731)	-	(2,483,731)
Asset retirement obligations (note 7)	994,388	-	994,388
Balance at December 31, 2013	$ 141,114,476	$ 629,388	$ 141,743,864
Additions	6,681,594	19,426	6,701,020
Asset acquisition	6,372,748	-	6,372,748
Transfers from exploration and evaluation assets (note 4)	186,152	-	186,152
Asset retirement obligations (note 7)	84,654	-	84,654
Balance at September 30, 2014	$ 154,439,624	$ 648,814	$ 155,088,438
Depletion, depreciation and impairment			
Balance at December 31, 2012	$ 32,071,418	$ 366,707	$ 32,438,125
Depletion and depreciation for the year	8,646,027	62,182	8,708,209
Impairment expense	5,389,061	-	5,389,061
Balance at December 31, 2013	$ 46,106,506	$ 428,889	$ 46,535,395
Depletion and depreciation	3,794,612	58,588	3,853,200
Impairment recovery	(714,050)	-	(714,050)
Balance at September 30, 2014	$ 49,187,068	$ 487,477	$ 49,674,545
Net book value			
December 31, 2013	$ 95,007,970	$ 200,499	$ 95,208,469
September 30, 2014	$ 105,252,556	$ 161,337	$ 105,413,893

The calculation of depletion and depreciation for the nine month period ended September 30, 2014 included estimated future development costs of $48,773,000 (December 31, 2013 - $55,340,000) associated with the development of the Company's proved and probable reserves.

The Company has not capitalized any interest or general and administrative expenses during the nine months ended September 30, 2014 or 2013, or the year ended December 31, 2013.

At September 30, 2014, the Company tested its CGUs for impairment. The recoverable amount of each cash-generating unit was estimated based on fair value less costs of disposal. The estimate of fair value less costs of disposal was determined using forecasted proved plus probable reserves before tax cash flows, discounted at 10%, using escalating forward pricing and net of future development costs, as obtained from an independently prepared reserve report at December 31, 2013 and updated internally by Company management to September 30, 2014. In determining the appropriate discount rate, the Company considered acquisition metrics of recent transactions completed on assets similar to those in the specific CGU and an approximate cost of capital for potential acquirers of the Company or the Company's CGUs. Fair value less cost of disposal is determined using a level 3 hierarchy.

During the nine month period ended September 30, 2014, the Company recognized recovery of impairments for the Company's interest in the High Island Block 141 lease totalling $714,050, as a result of a reduction in future development costs required to produce the lease. The recoverable amount for High Island Block 141 is $1,356,350 at September 30, 2014.

On July 16, 2014, the Company completed the acquisition of additional working interest from its joint operation partner in the Vermillion Area Block 376 #A-3 and A-4 wells for cash consideration of $3.5 million plus a recovery of year ended December 31, 2013 bad debt expense of $2.8 million, owed by the joint operation partner to the Company (note 17). This property acquisition was recognized as a business combination, as the assets acquired met the definition of a business. The acquisition has been accounted for using the acquisition method and the recognized amounts of identifiable assets acquired and liabilities assumed at fair value are as follows: $6.4 million of petroleum and natural gas interests and $85 thousand of asset retirement obligations. Revenue and net loss since the closing date and pro forma consolidated revenue and net loss giving effect to the acquisition of assets as if the acquisition had occurred on January 1, 2014, are not practicable to determine.

(amounts in US dollars)

6. Loans payable and warrants

Loans payable at September 30, 2014 and December 31, 2013, consisted of the following:

	September 30, 2014	December 31, 2013
Senior secured notes dated October 22, 2012 for $22,500,000 with interest at 18%, per annum, payable quarterly, with an initial maturity date of October 22, 2014, secured by first priority security interest on all assets (the "Notes") (i)	$ 22,500,000	$ 21,006,712
Related party notes payable dated April 26, 2012, with initial maturity dates of April 26, 2014 and subordinated to the Notes, with interest at 14.5%, per annum, payable at maturity, and secured by certain petroleum and natural gas properties (ii)	6,463,000	6,463,000
Related party subordinated secured credit facility dated October 11, 2013 for CDN $4,000,000, payable 181 days following repayment of the Notes, subordinated to the Notes, with interest at 9%, per annum, payable at maturity, and secured by certain petroleum and natural gas properties (iii)	3,436,963	3,223,626
Related party subordinated secured credit facility dated March 7, 2014 for $7,150,000, payable 181 days following repayment of the Notes, subordinated to the Notes, with interest at 14%, per annum, payable at maturity, and secured by certain petroleum and natural gas properties (iv)	7,058,924	-
	$ 39,458,887	$ 30,693,338
Less: Short-term portion	(39,458,887)	(27,469,712)
Long-term portion	$ -	$ 3,223,626

At September 30, 2014, all loans payable are scheduled to mature within one year. Subsequent to September 30, 2014, all loans payable are due after one year (note 18).

(i) On October 22, 2012, the Company entered into a Note Purchase Agreement and issued Senior Secured Notes (the “Senior Secured Notes”) in the amount of $22,500,000, with an initial maturity date of October 22, 2014. The Company is required to meet certain covenants including a quarterly collateral coverage covenant under the terms of the Note Payable Agreement. The collateral coverage ratio, which is a non-IFRS measure, is defined as the ratio between the value of proved developed producing reserves, as defined in the Note Purchase Agreement, plus cash and cash equivalents, to the outstanding unpaid principal and unpaid accrued interest of the Senior Secured Notes plus any outstanding accounts payable.

During the year ended December 31, 2013, the Company negotiated an amendment to the Note Purchase Agreement. Pursuant to same, the Company and the Note holders agreed to covenant revisions related to altering the approved plan of drilling by the Company. The Company also received approval to enter into a subordinated secured credit facility for borrowings up to CDN $8.0 million, as more specifically described below (note 6(iii)). The Company paid a consent fee of $450,000 to the Note holders and legal fees incurred by the Note holders which are included in the discount on the related party subordinated credit facility (note 6(iii)).

As at September 30, 2014 and December 31, 2013, the Company was not in compliance with all covenants, obligations and conditions under the agreements governing the Senior Secured Notes. As a result of the non-compliance, the stated interest rate increased to 18% from 12%, per annum. In order to enter into the membership interest contribution agreements to acquire Cochon Properties, LLC ("Cochon") and Morrison Well Services, LLC ("Well Services") (note 18), the Company obtained the consent of the holders of the Notes pursuant to a Limited Consent and Forbearance Agreement dated March 7, 2014 (the "Limited Consent"). Therein, the holders of the Senior Secured Notes and the Company acknowledged that the Company was in existing and continuing default of the collateral coverage ratio covenant of the Senior Secured Notes as at December 31, 2013. In order to allow for the acquisition of Cochon and Well Services, the Limited Consent provides that, the holders of the Senior Secured Notes will forbear from exercising certain rights and remedies under the Note Purchase Agreement and certain related documents in respect of the default until July 7, 2014, or such earlier date if certain events of insolvency or other customary events of default occur. On July 7, 2014, the Limited Consent was extended in respect of default by the Company to August 31, 2014, and the Company agreed to a premium repayment amount of 5% to 7% based on the actual repayment date between August 1 and August 31, 2014. On August 29, 2014, the Company entered into a fifth amendment to the Note Purchase Agreement and a second amendment to the Limited Consent extending the termination date therein to September 30, 2014 and agreed to a premium repayment amount of up to 7.5% to 9% based on the actual repayment date between September 1, 2014 and September 30, 2014 and has been accrued and included in accrued interest payable at September 30, 2014.

Subsequent to September 30, 2014, the Company has entered into a $45 million private offering of senior secured notes to resolve its working capital deficiency (see note 18).

Unpaid interest of $3,060,000 and $690,000 has been included in accrued interest payable at September 30, 2014 and December 31, 2013, respectively.

In conjunction with the issuance of the Senior Secured Notes, the Company also issued warrants exercisable for up to 9,000,000 common shares of the Company at an exercise price of US$1.00 per common share until October 22, 2017. The warrants are also eligible to be exercised on a "cashless" basis in accordance with the terms of the agreement. No warrants have been exercised to date.

The fair value of the warrants was estimated on initial recognition and at the end of each reporting period using a Level 2 fair value hierarchy, with changes in fair value recognized in income (loss) as unrealized gain (loss) on financing warrants. The loans payable component, net of the loan origination fees, is measured at amortized cost using the effective interest rate method, and is being accreted to the principal value on maturity, with a corresponding non-cash charge to income (note 11).

(amounts in US dollars)

The fair value of the financing warrants at September 30, 2014 and December 31, 2013, was determined using the Black-Scholes model with the following assumptions:

	September 30, 2014	December 31, 2013
Risk-free interest rate	1.78%	1.75%
Expected life (years)	3.06	3.81
Expected volatility	50.0%	50.0%
Expected annual dividend yield	0.00%	0.00%
Stock price	$0.50	$0.55
Exercise price	$1.00	$1.00
Fair value per warrant	$0.08	$0.12

The following table shows the changes in the financing arrangement balances:

	Loans payable	Financing warrants	Total
Balance, December 31, 2012	$ 19,470,426	$ 1,067,000	$ 20,537,426
Accretion	1,536,286	-	1,536,286
Unrealized loss on revaluation	-	25,000	25,000
Balance, December 31, 2013	21,006,712	1,092,000	22,098,712
Accretion	1,493,288	-	1,493,288
Unrealized loss (gain) on revaluation	-	(395,000)	(395,000)
Balance, September 30, 2014	$ 22,500,000	$ 697,000	$ 23,197,000

(ii) The related party notes payable of $6,463,000 at September 30, 2014 is due to a significant shareholder of the Company. Accrued interest payable totalling $2,037,560 and $1,326,897 at September 30, 2014 and December 31, 2013, respectively, is due at maturity. The initial maturity date was April 26, 2014 subject to other terms of the agreement. However, pursuant to an intercreditor subordination agreement, the principal amount of the note plus accrued interest is subordinate to the Note Purchase Agreement (note 6(i)) and therefore payment is not required prior to repayment of amounts due under the Note Purchase Agreement. Please refer to note 18 regarding repayment terms.

As a result of the Note Purchase Agreement, the related party note payable bears interest at the Notes rate of 12% plus 2.5% per annum.

(iii) Effective October 11, 2013, the Company entered into a First Amendment to the Note Purchase Agreement. Pursuant to same, the Company and the Senior Secured Note holders agreed to covenant revisions related to altering the approved plan of drilling by the Company. The Company also received approval to enter into a subordinated secured credit facility for borrowings up to CDN $8.0 million, as described below. The Company paid a consent fee of $450,000 to the Notes holders and legal fees incurred by the Senior Secured Note holders (note 6(i)).

On October 11, 2013, the Company entered into a subordinated secured credit facility with two related parties who are significant shareholders and/or directors of the Company that provides for borrowing up to CDN $8.0 million to be used for general corporate purposes. The initial advance under the credit facility was CDN $4.0 million (net of a 2% original issue discount and administrative fees of $10,000) resulting in net proceeds of $3,234,466. The discount is being accreted over the term of the facility up to the principal amount on the maturity date using an effective interest rate of approximately 25%, with $218,415, and $388,295 recorded as accretion for the three and nine months ended September 30, 2014, respectively. The interest rate is 9% per annum on all advances, and the credit facility matures 181 days following full satisfaction of the terms of the existing Note Purchase Agreement, as amended. Unpaid interest of $321,192 has been included in accrued interest payable at September 30, 2014 (December 31, 2013 - $84,618). See also note 16 disclosure of accrued interest on (iii) and (iv). Additionally, it is secured only by certain oil and gas properties and proceeds therefrom owned by Probe Resources US Ltd. No further amounts have been drawn on the facility as at or subsequent to September 30, 2014. Please refer to note 18 regarding repayment terms.

(iv) Effective March 7, 2014, the Company entered into an additional second lien credit facility with a related party who is a significant shareholder and director of the Company, for borrowing of up to $10 million. The initial advance was $4.4 million, before an original issue discount of 10%, for a funded amount equal to $4 million. During the nine months ended September 30, 2014, the Company drew an additional $2.75 million on the facility, before an original issue discount of 10%, for a funded amount of $2.5 million. The discounts are being accreted over the term of the facility up to the principal amount on maturity using an effective interest rate of approximately 30%, with $191,149 and $558,924 recorded as accretion for the three and nine month periods ended September 30, 2014, respectively. The credit facility is fully subordinated to the Senior Secured Notes (note 6(i)). Amounts drawn on the credit facility bear interest at 14% per annum, and are repayable 181 days after the full satisfaction of the Senior Secured Notes. Unpaid interest of $519,748 has been included in accrued interest payable at September 30, 2014. See also note 16 disclosure of accrued interest on (iii) and (iv). The credit facility is secured by the Company's petroleum and natural gas properties and assets.

In order to enter into the second lien credit facility, the Company obtained the consent of the holders of the Senior Secured Notes pursuant to a second amendment to the Note Purchase Agreement dated March 7, 2014 (note 6(i)), which provides for various conditions including the requirement for the Company to restrict any payments under the facility as provided for in a subordination agreement. In addition, the Company will be required to pay to the holders of the Senior Secured Notes, an amount equal to 3% of the principal amount of the Notes at the time of repayment, of $214,500. Please refer to note 18 regarding repayment terms.

(amounts in US dollars)

7. Asset retirement obligations and deposits

Asset retirement obligations ("ARO") were determined by management and were based on the Company's net ownership interest, the estimated future costs to reclaim and abandon the wells and facilities, and the estimated timing of when the costs will be incurred.

The following table summarizes changes in ARO for the nine month period ended September 30, 2014 and the year ended December 31, 2013:

	September 30, 2014	December 31, 2013
Asset retirement obligations, beginning of period	$ 18,595,827	$ 18,071,240
Liabilities incurred	-	282,193
Liabilities acquired	84,654	-
Liabilities disposed	-	-
Transfers to liabilities associated with assets held for sale (note 8)	-	-
Liabilities settled	(1,490,889)	(941,614)
Revisions to estimates and changes in discount rate	-	712,195
Loss on plug and abandonments	-	-
Accretion (unwinding of discount)	356,544	471,813
Asset retirement obligations, end of period	$ 17,546,136	$ 18,595,827
Less: Short-term portion	(5,392,167)	(5,392,167)
Long-term portion	$ 12,153,969	$ 13,203,660

The Company's ARO result from its ownership interest in petroleum and natural gas assets, including well sites and gathering systems. The total ARO are estimated based on the Company's net ownership interest in all wells and facilities, estimated costs to reclaim and abandon these wells and facilities and the estimated timing of the costs to be incurred in future years. The estimated inflated undiscounted cash flows required to settle the provisions, before considering salvage, are approximately $19.4 million (December 31, 2013 - $20.9 million), which has been discounted using a risk-free rate of 2.55% (December 31, 2013 - 2.55%). These obligations are to be settled based on the economic lives of the underlying assets, which currently extend up to 15 years into the future and will be funded from general corporate resources at the time of abandonment.

At September 30, 2014 and December 31, 2013, the Company had a $3,762,000 cash deposit held as security by the surety of the supplemental bonds that are required by the Bureau of Ocean Energy Management (BOEM) on the ARO for properties owned by Probe Resources US Ltd. prior to April 30, 2012. These funds are restricted for use in meeting Probe Resources US Ltd.'s ARO specific to those properties and will be released by the surety upon satisfactory completion of plugging and abandonment operations for specific wells and/or structures as the work is completed. The Company is required to abandon certain fields covered by this bond within the next 12 months. As a result, $3,462,000 of the deposit has been classified as short-term and included in restricted cash as at September 30, 2014 and December 31, 2013 (note 3(b)).

(amounts in US dollars)

8. Prepaid expenses and deposits

Prepaid expenses and deposits consist of the following:

		September 30, 2014		December 31, 2013
Prepaid insurance	$	1,006,249	$	997,436
Prepaid bonds		84,425		83,916
Prepaid plug and abandonment		-		-
Prepaid inspection fees		52,800		65,500
Deferred financing costs		1,318,813		-
Prepaid other		100,671		26,980
Total prepaid expenses and deposits	$	2,562,958	$	1,173,832

Deferred financing costs relate to the Note Purchase Agreement as further disclosed in note 18.

9. Share capital

(a) Authorized

The authorized share capital of the Company consists of an unlimited number of voting common shares, voting proportionate shares, and preferred shares.

(b) Issued

The following table summarizes the changes in common shares and proportionate voting shares outstanding:

	Number of Shares		Stated Value
Common shares			
Outstanding, December 31, 2012	40,394,823	$	11,746,587
Issued on cashless exercise of stock options (note 10)	2,500		2,043
Outstanding, December 31, 2013 and September 30, 2014	40,397,323	$	11,748,630
Proportionate voting shares			
Outstanding, December 31, 2013 and September 30, 2014	65,071	$	29,162,552
Total share capital stated value			
December 31, 2013 and September 30, 2014		$	40,911,182

(c) The common shares may at any time, at the option of the holder, be converted into proportionate voting shares of the Company on the basis of 1,000 common shares for one proportionate voting share for no consideration. Each issued and outstanding proportionate voting share may at any time, at the option of the holder, be converted into 1,000 common shares of the Company for no consideration. The common shares and proportionate voting shares have the same rights and are equal in all respects as if they were shares of one class only. For purposes of voting and dividend rights, the proportionate voting shares are multiplied by 1,000, equal to the conversion ratio.

(amounts in US dollars)

(d) There were no stock options exercised during the nine month period ended September 30, 2014. During the year ended December 31, 2013, 6,666 stock options were exercised under a cashless exercise provision of the Company's stock option plan, whereby the Company issued 2,500 common shares in settlement of the stock options (note 10).

10. Stock-based compensation

The Company has a stock option plan under which options may be granted to employees, officers directors and consultants. As at September 30, 2014, the Company had 21,093,164 common shares authorized for issuance under the stock option plan.

On June 5, 2012, 4,820,645 stock options were granted with an exercise price of CDN $0.50. On September 11, 2013, 4,532,759 stock options were granted with an exercise price of CDN $0.82. Additionally, on May 16, 2014, 300,000 stock options were granted with an exercise price of CDN $0.61. Each option is exercisable to acquire one common share of the Company for a period of ten years and vests as to 1/3 on each of the 1st, 2nd and 3rd anniversary dates from the date of grant.

The Company's original stock option plan provided that a holder of an option may, rather than exercise such option, elect a cashless exercise of such option payable in common shares equalling the amount by which the value of an underlying common share at that time exceeded the exercise price of an option to acquire such share. On a cashless exercise, the holder of an option would receive a lesser amount of shares in lieu of paying the exercise price based on the market price of the shares on the exercise date, and withholding taxes, if the holder so elected. The Company's stock option plan was subsequently amended during 2013 to remove the cashless exercise feature for future option grants. In addition, the authorized number of shares for issuance under the plan was amended.

A summary of the changes in the outstanding options awarded under the Company's stock option plan is as follows:

	Nine months ended September 30, 2014			Year ended December 31, 2013		
	Number		Exercise Price(CDN$)	Number		Exercise Price(CDN$)
Outstanding, beginning of period	9,293,404	$	0.66	4,820,645	$	0.50
Granted	300,000		0.61	4,532,759		0.82
Exercised (1)	-		-	(6,666)		0.50
Forfeited	(125,000)		0.50	(53,334)		0.50
Outstanding, end of period	9,468,404	$	0.66	9,293,404	$	0.66
Exercisable, end of period	4,684,683	$	0.60	1,586,882	$	0.50

(1) The difference from the number of shares issued upon exercise of stock options (note 9(d)) is due to the cashless exercise. The price of the Company's common shares at the date the stock options were exercised was CDN $0.80

(amounts in US dollars)

The following table outlines the exercise price and years to expiry of all outstanding options, as well as the number of options exercisable as of September 30, 2014:

Options Outstanding			Options Exercisable	
Exercise Price (CDN$)	Number Outstanding	Remaining Life (Years)	Number Exercisable	Exercise Price (CDN$)
$0.50	4,635,645	7.7	3,173,763	$ 0.50
$0.61	300,000	9.7	-	$ -
$0.82	4,532,759	8.9	1,510,920	$ 0.82
Total	**9,468,404**	**8.0**	**4,684,683**	**$ 0.60**

The fair value of options granted during the nine months ended September 30, 2014 were estimated on the date of grant using the Black-Scholes option-pricing model with the following weighted average assumptions and resulting values:

For the nine month period ended	September 30, 2014	September 30, 2013
Assumptions:		
Stock price (CDN$)	$ 0.61	$ 0.82
Exercise price (CDN$)	$ 0.61	$ 0.82
Risk free interest rate (%)	2%	2%
Expected life (years)	10	10
Expected volatility (%)	50%	50%
Estimated forfeiture rate (%)	5%	5%
Expected dividend yield	-	-
Fair value of options granted (CDN$)	**$ 0.50**	**$ 0.40**
Share price on date of grant (CDN$)	**$ 0.61**	**$ 0.82**

During the three and nine month periods ended September 30, 2014, $344,521 and $1,162,423 (2013 - $200,085 and $595,382), respectively, was recorded as stock-based compensation relating to stock options granted in 2014 and prior years, with a corresponding increase in contributed surplus.

(amounts in US dollars)

11. Finance expenses

	Three Months Ended September 30, 2014	Three Months Ended September 30, 2013	Nine Months Ended September 30, 2014	Nine Months Ended September 30, 2013
Interest expense on senior secured notes (note 6(i))	$ 3,060,000	$ 690,000	$ 5,096,250	$ 2,047,500
Interest on notes payable to related party (note 6(ii))	239,491	639,704	710,663	824,671
Interest on related party subordinated secured credit facilites (notes 6(iii),(iv))	357,531	-	766,476	-
Accretion of discount on senior secured notes (note 6(i))	-	390,906	1,493,288	1,127,370
Accretion of discount on related party subordinated secured credit facilities (notes 6(iii),(iv))	409,564	-	947,219	-
Accretion of asset retirement obligations (note 7)	119,449	142,185	356,544	426,556
Foreign exchange (gain) loss on related party subordinated secured credit facility (note 6(iii))	(238,058)	-	(185,113)	-
Other	156,907	(1,490)	150,520	(26)
Total finance expenses	$ 4,104,884	$ 1,861,305	$ 9,335,847	$ 4,426,071

12. Income taxes

(a) Deferred income tax expense (recovery)

The provision for income taxes differs from the results which would have been obtained by applying the U.S. federal corporate tax rate to the Company's income (loss) before income tax. The difference results from the following items:

	Three Months Ended September 30, 2014	Three Months Ended September 30, 2013	Nine Months Ended September 30, 2014	Nine Months Ended September 30, 2013
Income (loss) before income taxes	$ (1,622,096)	$ 3,183,974	$ (2,976,626)	$ 2,436,296
Statutory tax rate:	35.0 %	35.0 %	35.0 %	35.0 %
Expected income tax expense (recovery)	(568,000)	1,114,000	(1,042,000)	853,000
Difference resulting from:				
Stock-based compensation	210,000	70,000	435,000	208,000
Unrealized (gain) loss on financing warrants	(238,000)	(320,000)	(138,000)	191,000
Accretion of note payable discount	147,000	96,000	600,000	276,000
Changes in permanent differences and other	90,000	201,000	78,000	(452,000)
Change in deferred tax assets not recognized	(82,000)	-	(70,000)	-
Total income tax expense (recovery)	$ (441,000)	$ 1,161,000	$ (137,000)	$ 1,076,000

The US federal corporate tax rate is 35%. All of the Company's producing petroleum and natural gas interests are currently located offshore in US federal waters, and accordingly, no US state taxes have been applied.

(amounts in US dollars)

(b) Deferred income tax assets and liabilities:

The components of the Company's deferred income tax liabilities (assets) and associated movements are as follows:

	December 31, 2013	Recognized in Income	September 30, 2014
Property and equipment assets	$ 29,286,000	$ 930,000	$ 30,216,000
Asset retirement obligations	(6,508,000)	274,000	(6,234,000)
US net operating losses	(18,208,000)	(1,421,000)	(19,629,000)
Canadian non-capital losses	(1,400,000)	(76,000)	(1,476,000)
Share issuance and other temporary differences	(289,000)	226,000	(63,000)
Deferred income tax assets not recognized	1,694,000	(70,000)	1,624,000
	$ 4,575,000	$ (137,000)	$ 4,438,000

The amount and timing of reversals of temporary differences will be dependent upon a number of factors including the Company's future operating results. The US net operating losses are available for deduction against future taxable income until 2034.

Future tax benefits related to tax deductions in Canada for Rooster Energy, Ltd. have been offset with a valuation allowance, applied using a combined Canadian federal and provincial corporate tax rate of 25%, due to the uncertainty of realization. The Canadian non-capital losses expire between 2030 and 2034.

13. Income (loss) per share

The following table summarizes the weighted average number of common shares used in calculating income (loss) per share:

	Three Months Ended September 30,		**Nine Months Ended September 30,**	
	2014	**2013**	**2014**	**2013**
Basic	105,468,323	105,467,997	105,468,323	105,465,898
Effect of dilutive stock options	-	1,193,603	-	-
Diluted	105,468,323	106,661,600	105,468,323	105,465,898

Basic income (loss) per share figures for the three and nine month periods ended September 30, 2014 and 2013 have been calculated using the weighted average number of common shares outstanding plus the weighted average number of proportionate voting shares outstanding at the conversion ratio of 1,000 common shares for each outstanding proportionate voting share. All outstanding options and warrants were excluded from the calculation of diluted loss per share for the three month period ended September 30, 2014 and the nine month periods ended September 30, 2014 and 2013, as they were anti-dilutive.

(amounts in US dollars)

The calculation of diluted net income per share for the three month period ended September 30, 2013 excludes the impact of 9,000,000 warrants and 4,532,759 stock options as the inclusion of these warrants and options would have been anti-dilutive.

The calculation of diluted net income per share for the nine month period ended September 30, 2013 excludes the impact of 9,000,000 warrants and 9,293,404 stock options as the inclusion of these warrants and options would have been anti-dilutive.

14. Supplemental cash flow information

(a) Changes in non-cash working capital, comprise the following:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013
Source (uses) of cash:				
Restricted cash	$ 3,599,426	$ (1,196,940)	$ 2,158,635	$ (1,196,940)
Accounts receivable	(2,329,029)	222,906	(2,735,554)	2,418,783
Prepaid expenses and deposits	(1,120,687)	320,451	(1,389,126)	(2,226,457)
Accounts payable and accrued liabilities	4,618,550	6,198,430	2,058,644	8,741,575
Due to related parties	972,145	125,988	1,201,696	(965,573)
Changes in non-cash working capital	$ 5,740,405	$ 5,670,835	$ 1,294,295	$ 6,771,388
Related to operating activities	$ 11,184,988	$ 2,501,417	$ 9,301,259	$ 3,935,255
Related to investing activities	(4,125,770)	3,169,418	(6,688,151)	2,836,133
Related to financing activities	(1,318,813)	-	(1,318,813)	-
	$ 5,740,405	$ 5,670,835	$ 1,294,295	$ 6,771,388

At September 30, 2014 and December 31, 2013, all of the Company's cash and cash equivalents were comprised of cash on deposit.

(b) Interest and income taxes paid

The Company made interest payments in the amounts of $2,388,750 and $1,882,500 during the nine month periods ended September 30, 2014 and 2013, respectively.

The Company has not paid any income taxes during the nine months ended September 30, 2014 or 2013.

15. Commitments

There were no changes to the commitments during the nine months ended September 30, 2014 as compared to those disclosed in the Company's annual audited consolidated financial statements for the year ended December 31, 2013. See also note 18 regarding fixed swap agreements entered into subsequent to September 30, 2014.

(amounts in US dollars)

16. Other related party transactions

The Company has transactions with affiliates, including field services, rental of equipment, the reimbursement of operating expenses, and the payment of certain administrative services at terms determined by management. In addition, two parties, related to the Company by way of common directors and officers, participated as to a 7.5% working interest in the drilling of the High Island A494 #B-4 well.

Balances due to (from) related parties and related party transactions are as follows:

	September 30 2014	December 31, 2013
Due to related parties (1)	$ 5,172,044	$ 3,970,348
Notes payable due to related party (note 6(ii))	6,463,000	6,463,000
Accrued interest payable on notes payable to related party (note 6(ii))	2,037,560	1,326,897
Subordinated secured credit facility amounts due to related parties (notes 6(iii),(iv))	10,495,887	3,223,626
Accrued interest payable on subordinated secured credit facility amounts due to related parties (note 6(iii),(iv))	840,940	84,618
Accounts receivable due from related parties participating in drilling of well	-	(265,547)
Total	$ 25,009,431	$ 14,802,942

(1) Represents amounts payable to related parties in the ordinary course of business for operating expenses and capital expenditures. Payments are made as cash flows allow within the constraints of the Note Purchase Agreement (note 6(i)). The amounts are unsecured, non-interest bearing, and have no fixed terms of repayment. (See also note 18).

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013
Purchases from related parties	$ 738,050	$ 41,045	$ 967,601	$ 244,675
Interest expense on amounts due to related parties	-	-	-	-
Interest expense on note payable to related party (note 11)	239,491	639,704	710,663	824,671
Interest expense and origination fees on CDN$ related party subordinated secured credit facility (note 11)	82,632	-	246,729	-
Interest expense on related party subordinated secured credit facility (note 11)	274,899	-	519,747	-
Total	$ 1,335,072	$ 680,749	$ 2,444,740	$ 1,069,346

Purchases from related parties during the nine month periods ended September 30, 2014 and 2013 were considered by management to be in the normal course of business and transacted on terms equivalent to those that would have prevailed in an arm's length transaction.

Additional related party transactions relating to the Company's related party loans payable are outlined in note 6.

17. Contingencies

Certain claims and counterclaims have been filed against the Company which arise in the normal course of business. Management has assessed these legal actions to be without merit and/or the Company expects to be fully indemnified, and the likelihood of loss to the Company is remote. Accordingly, no amounts have been accrued in the September 30, 2014 condensed interim consolidated financial statements relating to these actions.

There was only one threatened or pending legal matter that, in the opinion of management, could have a material impact on the Company's consolidated results of operations, financial position or cash flows, as disclosed in the Company's annual audited consolidated financial statement for the year ended December 31, 2013.

On July 16, 2014, the Company entered into a Settlement Agreement that resulted in the dismissal of the litigation. Pursuant to the terms of the settlement, the assignee assigned all of its 25% participation interest in the Vermilion Area Block 376 #A-3 and #A-4 wells to the Company in consideration of the sum of $3,500,574 (note 5). The related amounts held in trust of $3,599,426 (note 3(b)) were also released to the plaintiff in conjunction with the settlement.

18. Other subsequent events

Subsequent to September 30, 2014, the Company, together with all of its wholly-owned subsidiaries, has entered into a Note Purchase Agreement under which the Company has issued Senior Secured Notes (the "Notes") due on the earlier of February 14, 2016 and the date that the Notes shall become due and payable in full in accordance with the agreement, whether by acceleration or otherwise, in the aggregate principal amount of $45 million. The proceeds of the Notes will be used to: 1) repay existing Senior Secured Notes (note 6(i)); 2) fund the cash portion of the purchase price for Morrison Well Services (see below); and 3) payment toward trade accounts payable over 60 days and provide for other general corporate purposes.

Net proceeds to the Company totalled the sum of $8,510,126, after deducting the original issue discount, the outstanding principal, fees, and interest paid to the holders of the Senior Secured Notes, the $10 million portion of the purchase price for Well Services and certain transaction fees and expenses.

The Notes are secured by a first priority security interest, lien and mortgage on all of the Company's oil and natural gas assets and, without limitation, a pledge of equity in each of Rooster's subsidiaries. The Notes include an original issue discount of 2.5%, and bear interest at a rate equal to LIBOR + 11.5% per annum with interest payments due monthly; the minimum interest rate will be 13.0% per annum. No holder of the Note is a related party to Rooster nor is any holder a chartered bank, trust company or treasury bank. The Company is required to meet certain financial covenant and reporting requirements in relation to the Notes.

Rooster previously announced that it had entered into: (i) a membership interest contribution agreement (the “Cochon Agreement”) dated March 7, 2014 with the members of Cochon Properties, LLC (“Cochon”) to acquire 100% of the membership interests in Cochon (the “Cochon Acquisition”); and (ii) a membership interest contribution agreement (the “Well Services Agreement” and, together with the Cochon Agreement, the “Agreements”) dated March 7, 2014 with Morrison Energy Group, LLC, (“MEG”) to acquire 100% of the membership interest in Morrison Well Services, LLC (“Well Services”) (the “Well Services Acquisition”). The Well Services Acquisition together with the Cochon Acquisition, are hereinafter referred to as the “Transaction”.

The Transaction contemplates the purchase of Well Services for $95 million and Cochon for US$30 million, for aggregate consideration of $125 million (the “Purchase Price”), subject to adjustments for working capital. The Purchase Price will be comprised of $115 million in common shares of Rooster (the “Rooster Common Shares”), of which $85 million will be in respect of Well Services and the remaining US$30 million will be in respect of Cochon, and $10 million in cash, all in respect of Well Services.

The Agreements provide that the number of Rooster Common Shares issued to satisfy the Rooster Common Share portion of the Purchase Price will equal that number obtained by dividing US$115 million by the average daily closing price for the Rooster Common Shares for the twenty (20) consecutive trading days on which shares are actually traded and quoted on the TSX Venture Exchange (the “TSXV”) ending on and including the date that is ten (10) business days prior to the special shareholder meeting to approve the Transaction (the “Meeting”), provided that for the purposes of the exchange ratio the closing price of such Rooster Common Shares shall be subject to a minimum price of CDN$0.40 and a maximum price of CDN$0.70.

The average daily closing price for the Rooster Common Shares for the twenty (20) consecutive trading days on which shares were actually traded and quoted on the TSXV ending on and including May 2, 2014 (i.e., 10 business days prior to the Meeting) was CDN$0.577 per share and US$0.526 per share after considering an average currency exchange rate (US$/CDN$) of $0.911. As a result, upon closing of the Transaction, a total of 218,631,179 Rooster Common Shares were issued to satisfy the Rooster Common Shares portion of the Purchase Price. Cochon members received a total of 57,034,221 Rooster Common Shares and MEG received 161,596,958 Rooster Common Shares. On May 16, 2014, the requisite majority of the minority of Rooster shareholders approved the Company’s acquisitions of Cochon and Well Services.

Well Services and Cochon are controlled by a related party who is a significant shareholder and director of the Company.

Simultaneous with the closing of the $45 million term loan facility, on November 17, 2014, Rooster closed the acquisitions of Cochon and Well Services. As consideration for the two acquisitions, the Company has 1) funded the $10 million cash portion of the purchase price of Well Services, and 2) issued 218,631,179 Rooster Common Shares.

Subsequent to the acquisition, the Company will have issued and outstanding 259,028,502 of common shares and 65,071 proportionate voting shares (each convertible to 1,000 common shares) or 374,099,502 common shares after conversion of the proportionate voting shares to common shares.

As a condition for closing the Notes, the Company was required to sell forward certain quantities of its oil and natural gas production over the term of the Notes. Accordingly, the Company has entered into fixed swap agreements to sell an average of 653 BOPD and 7,033 MMBTUPD at $77.50 per BOE and $3.81 per MMBTU, respectively, until February 29, 2016.

Effective November 17, 2014, the Company, Chet Morrison Contractors, LLC, and the Notes holder entered into a subordination agreement that prohibits payment by the Company of accounts payable, classified as due to related parties on the consolidated balance sheet of the Company, due and owing to Chet Morrison Contractors, LLC, in excess of the amount of $2,717,581.

In connection with the Notes, the Notes holder, the Company and each of the loans payable to related parties (see notes 6(ii), (iii) and (iv)), entered into intercreditor and subordination agreements that prohibit any payments on the related party indebtedness until the Notes are fully satisfied. Additionally, each of the loan or credit agreements between the Company and each related party was amended to extend the maturity date of each of those loans to one year after all obligations under the Notes are satisfied, being February 14, 2017.