Questfire Energy Corp.

Condensed Interim Financial Statements
For the three months ended March 31, 2014

(amounts in Canadian dollars) (unaudited)

Questfire Energy Corp.

Condensed Interim Balance Sheets

(amounts in Canadian dollars) (unaudited)

	Note	**March 31, 2014**	December 31, 2013
		$	$
Assets			
Current assets			
Cash and cash equivalents		**5,476,678**	-
Accounts receivable	4(c)	**10,495,337**	8,256,402
Deposits and prepaid expenses		**574,866**	592,870
Total current assets		**16,546,881**	8,849,272
Non-current assets			
Property and equipment	6	**122,487,639**	122,140,086
Exploration and evaluation assets		**1,564,044**	1,564,044
Deferred tax asset		**-**	623,976
Total assets		**140,598,564**	133,177,378
Liabilities			
Current liabilities			
Bank overdraft		**-**	167,201
Accounts payable and accrued liabilities	8	**14,094,679**	12,247,693
Bank debt	9	**42,000,000**	41,000,000
Current portion of long-term contract obligation	10	**334,769**	-
Risk management contracts	4(e)	**3,325,181**	1,606,257
Convertible debentures	13	**1,408,802**	1,382,604
Total current liabilities		**61,163,431**	56,403,755
Non-current liabilities			
Decommissioning provisions	11	**34,681,952**	34,706,080
Convertible Class B shares	12	**15,484,362**	15,088,437
Long-term contract obligation	10	**14,665,231**	-
Convertible debentures	13	**-**	31,002,508
Deferred tax liabilities		**4,190,087**	-
Total liabilities		**130,185,063**	137,200,780
Shareholders' Equity (Deficiency)			
Share capital		**4,272,595**	4,272,595
Equity component of convertible Class B shares	12	**(2,081,352)**	(2,081,352)
Equity component of convertible debentures	13	**75,805**	75,805
Warrants	13	**28,295**	28,295
Contributed surplus		**350,391**	288,768
Retained earnings (deficit)		**7,767,767**	(6,607,513)
Total earnings (deficiency) attributable to equity holders of the Corporation		**10,413,501**	(4,023,402)
Total liabilities and shareholders' equity		**140,598,564**	133,177,378

Commitments (note 18)
Subsequent events (notes 12 and 19)

(Signed) "Richard Dahl", Director

(Signed) "Roger MacLeod", Director

See accompanying notes to the financial statements.

Questfire Energy Corp.

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

(amounts in Canadian dollars) (unaudited)

	Note	Three months ended March 31, 2014	2013
		$	$
Revenue			
Oil and natural gas sales		**20,955,819**	64,121
Royalties		**(3,171,539)**	(3,467)
		17,784,280	60,654
Realized loss on risk management		**(1,087,983)**	-
Unrealized loss on risk management	4(e)	**(1,800,824)**	-
		14,895,473	60,654
Expenses			
Production and operating		**6,197,474**	31,925
Transportation		**452,914**	1,264
General and administrative		**1,613,135**	291,747
Share-based compensation		**61,623**	12,281
Exploration and evaluation		**112,500**	62,500
Depletion and depreciation	6	**3,007,132**	26,687
Transaction costs	5	**-**	624,465
		11,444,778	1,050,869
Operating Income (Loss)		**3,450,695**	(990,215)
Gain on sale of assets	5(a)	**431,262**	-
Gain on repurchase of convertible debentures	13	**17,722,983**	-
Finance expense	15	**(2,415,597)**	(160,577)
Income (Loss) Before Income Taxes		**19,189,343**	(1,150,792)
Deferred income tax (expense) recovery		**(4,814,063)**	47,849
Income (Loss) and Comprehensive Income (Loss) for the Period		**14,375,280**	(1,102,943)
Income (Loss) per Share			
Basic	14(c)	**1.11**	(0.09)
Diluted	14(c)	**0.32**	(0.09)

See accompanying notes to the financial statements.

	Note	Share capital	Equity component of convertible Class B shares	Equity component of convertible debentures	Warrants	Contributed surplus	Deficit	Total
		$	$	$	$	$	$	$
Balance, January 1, 2013		4,193,633	(2,081,352)	79,767	28,295	134,770	(4,429,039)	(2,073,926)
Share-based compensation		-	-	-	-	12,281	-	12,281
Loss for the period		-	-	-	-	-	(1,102,943)	(1,102,943)
Balance, March 31, 2013		4,193,633	(2,081,352)	79,767	28,295	147,051	(5,531,982)	(3,164,588)
Issued on conversion of convertible debentures	13	78,962	-	(3,962)	-	-	-	75,000
Share-based compensation		-	-	-	-	141,717	-	141,717
Loss for the period		-	-	-	-	-	(1,075,531)	(1,075,531)
Balance, December 31, 2013		4,272,595	(2,081,352)	75,805	28,295	288,768	(6,607,513)	(4,023,402)
Share-based compensation		-	-	-	-	61,623	-	61,623
Income for the period		-	-	-	-	-	14,375,280	14,375,280
Balance, March 31, 2014		**4,272,595**	**(2,081,352)**	**75,805**	**28,295**	**350,391**	**7,767,767**	**10,413,501**

See accompanying notes to the financial statements.

Questfire Energy Corp.

Condensed Interim Statements of Cash Flows

(amounts in Canadian dollars) (unaudited)

	Note	Three months ended March 31, 2014	2013
		$	$
Cash flows related to:			
Operating Activities			
Income (loss)		**14,375,280**	(1,102,943)
Add (deduct) items not involving cash:			
Unrealized loss on risk management	4(e)	**1,800,824**	-
Share-based compensation		**61,623**	12,281
Depletion and depreciation	6	**3,007,132**	26,687
Acquired office lease amortization	16	**69,543**	-
Deferred income tax expense (recovery)		**4,814,063**	(47,849)
Gain on repurchase of convertible debentures	13	**(17,722,983)**	-
Gain on sale of assets	5(a)	**(431,262)**	-
Net finance expense	15	**2,415,597**	160,577
Funds flow from (used in) operations		**8,389,817**	(951,247)
Decommissioning costs incurred	11	**(752,049)**	-
Change in non-cash working capital	16	**1,066,737**	1,065,717
Cash from operating activities		**8,704,505**	114,470
Investing Activities			
Exploration and evaluation expenditures		**-**	(7,002)
Property and equipment expenditures		**(3,176,003)**	(203,513)
Disposal of assets	6	**40,049**	-
Disposal of assets held for sale	5(a)	**431,262**	-
Purchase of risk management contracts	4(e)	**(81,900)**	-
Change in non-cash working capital	16	**(1,664,134)**	(16,152)
Cash used in investing activities		**(4,450,726)**	(226,667)
Financing Activities			
Bank debt draws		**1,000,000**	-
Long-term contract obligation draws	10	**15,000,000**	-
Convertible debenture repurchase	13	**(13,600,000)**	-
Interest and finance costs paid	15	**(1,163,809)**	(145,450)
Change in non-cash working capital	16	**153,909**	-
Cash from (used in) financing activities		**1,390,100**	(145,450)
Increase (decrease) in Cash and Cash Equivalents		**5,643,879**	(257,647)
Cash and Cash Equivalents (Bank Overdraft), Beginning of Period		**(167,201)**	395,288
Cash and Cash Equivalents, End of Period		**5,476,678**	137,641

See accompanying notes to the financial statements.

1. General business description

Questfire Energy Corp. ("Questfire" or the "Corporation") is engaged in the exploration for, and development and production of, oil and natural gas in Alberta and may conduct its activities jointly with others; these condensed interim financial statements reflect only the Corporation's proportionate interest in such activities. The Corporation's Class A shares and Class B shares are listed on the TSX Venture Exchange (TSXV). The address and principal place of business of the Corporation is Suite 500, 400 – 3rd Avenue S.W., Calgary, Alberta, T2P 4H2.

The condensed interim financial statements were approved and authorized for issuance by the Corporation's Board of Directors on May 21, 2014.

2. Basis of preparation

Statement of compliance

These condensed interim financial statements were prepared in accordance with International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board (IASB), interpretations of the International Financial Reporting Interpretations Committee (IFRIC), and Canadian generally accepted accounting principles (GAAP) as applicable to interim financial statements, including International Accounting Standard (IAS) 34, *Interim Financial Reporting*, and should be read in conjunction with the annual financial statements for the year ended December 31, 2013, which were prepared in accordance with IFRS. The disclosure provided is incremental to that included with the annual financial statements. Certain information and disclosures included in the notes to the annual financial statements is condensed or disclosed only on an annual basis.

Basis of measurement

These condensed interim financial statements were prepared on a historical cost basis, except for certain financial instruments and share-based payment transactions, which were measured at fair value.

Use of estimates and judgments

The preparation of financial statements in conformity with IFRS requires management to make estimates and assumptions that affect the reported amount of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amount of income and expenses during the period. These estimates are reviewed periodically and, as adjustments become necessary, are reported in the period in which they become known. By their nature, these estimates and related future cash flows are subject to measurement uncertainty, and the impact on future financial statements could be material.

In preparing these condensed interim financial statements, the significant estimates and judgments made by management in applying the Corporation's accounting policies and the key sources of estimation uncertainty were the same as those that applied to the financial statements for the year ended December 31, 2013, with the exception of changes in estimates that are required in determining the provision for income taxes. Income taxes on income or loss in the interim periods are accrued using the income tax rate that would be applicable to the expected total annual income or loss.

3. Significant accounting policies

The accounting policies followed in these condensed interim financial statements are consistent with those for the year ended December 31, 2013, except as described below:

a) New and amended standards adopted by the Corporation

Questfire adopted the following new and revised standards, along with any amendments, effective January 1, 2014:

(i) IAS 32, *Financial Instruments: Presentation*, clarifies the requirements for offsetting financial assets and liabilities. The amendments clarify that the right to offset must be available on the current date and cannot be contingent on a future event. IAS 32 did not impact the financial statements.

(ii) In December 2013, the IASB issued narrow-scope amendments to a total of nine standards as part of its annual improvement process. Some of the amendments were: clarifying the definition of vesting conditions in IFRS 2, *Share-based Payment*; defining the classification and measurement of contingent consideration; scope exclusion for the formation of joint arrangements in IFRS 3, *Business Combinations*; and modifying the definition of a related party in IAS 24, *Related Party Disclosures*. The adoption of the amendments did not affect the financial statements.

(iii) IFRIC Interpretation 21, *Levies*, pertains to accounting for certain payments to governments. Levies may be any amounts paid to a government that is not income tax, for the acquisition of an asset, nor for the rendering of contractual services by the government. The interpretation of IFRIC 21 continues to evolve. The Corporation believes royalties are outside the scope of IFRIC 21, and that its current accounting treatment is appropriate even were IFRIC 21 applied. Property tax is considered within the scope of IFRIC 21, and is material to the Corporation. Property taxes are generally due in advance on an annual basis for individual properties. Management has assessed its current accounting treatment and considers it appropriate. IFRIC 21 did not impact the financial statements.

These changes were made in accordance with the applicable transitional provisions.

b) New and revised IFRS not yet adopted

There were no new or amended standards issued during the three months ended March 31, 2014 that are applicable to the Corporation in future periods. A description of standards and interpretations that will be adopted by the Corporation in future periods can be found in the notes to the financial statements for the year ended December 31, 2013.

c) Reclassification

Certain information provided for the three months ended March 31, 2013 was reclassified for comparability with the current period's presentation.

4. Financial instruments and risk management

a) Risk management overview

The Corporation's activities expose it to a variety of financial risks including credit risk, liquidity risk and market risk. This note presents information about the Corporation's exposure to each of these risks, its objectives, policies and processes for measuring and managing risk, and its management of capital. Further quantitative disclosure is included throughout this document. Questfire employs risk management strategies and polices to ensure its risk exposure is consistent with its business objectives and risk tolerance. While the Board of Directors has overall responsibility for Questfire's risk management framework, Questfire's management monitors the risks and administers the risk management measures.

b) Fair value of financial instruments

The fair values of cash and cash equivalents or bank overdraft, accounts receivable, accounts payable and accrued liabilities, and bank debt approximate their carrying values due to the short-term maturity of those instruments. The fair value of the bank debt is equal to its carrying value as the facility bears floating-rate interest with credit spreads indicative of market rates. The fair value of the convertible debentures is approximated by their carrying value given interest rates the Corporation believes it would have to pay on an instrument with similar terms.

The fair value of convertible Class B shares at March 31, 2014, based on a discounted cash flow model assuming a 10.44 percent effective interest rate, is approximately $15.5 million (December 31, 2013 – $14.8 million).

The fair value of financial derivatives, including risk management contracts, is determined by discounting the difference between the contracted prices and published forward price curves at the balance sheet date, using the remaining contracted oil and natural gas volumes and a risk-free interest rate adjusted for the Corporation's and the counterparty's non-performance risk (see also note 4(e)).

The significance of inputs used in making fair-value measurements is examined and the inputs are classified according to a fair-value hierarchy with three levels. 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 in which the inputs are derived from quoted indices. Level 3 valuations are based on inputs that are unobservable, but are significant to the overall fair value measurement.

Cash and cash equivalents are measured at fair value based on their Level 1 designation. Derivative financial instruments, including risk management contracts, are measured at fair value based on a Level 2 designation.

c) Credit risk

Credit risk is the risk of financial loss to the Corporation if a customer or counterparty to a financial instrument fails to meet its contractual obligations. The Corporation is exposed to credit risk with respect to accounts receivable, cash and cash equivalents, and risk management contracts if in an unrealized asset position.

Substantially all of the Corporation's accounts receivable are due from purchasers of Questfire's oil and natural gas production, joint interest partners and government agencies and are subject to normal industry credit risk. Receivables from oil and natural gas marketers are normally collected on the 25th day of the month following production. The Corporation mitigates the credit risk associated with the marketing of its oil and natural gas production by establishing marketing relationships with large, credit-worthy purchasers. The Corporation has not experienced any collection issues with its marketers.

Significant changes in industry conditions and risks that weaken partners' ability to generate cash flow will increase collection risk. Questfire's management believes the risk is mitigated by the size and reputation of the companies to which the Corporation extends credit and believes all receivables will be collected.

At March 31, 2014 and December 31, 2013, the Corporation's accounts receivable were comprised of the following:

	March 31, 2014	December 31, 2013
	$	$
Oil and natural gas sales	**7,593,197**	5,789,802
Joint interest billings, GST and other	**2,902,140**	2,466,600
Accounts receivable	**10,495,337**	8,256,402

The Corporation considers all amounts greater than 90 days to be past due. At March 31, 2014, $318,016 is past due (December 31, 2013 – $542,509). The Corporation considers this amount fully collectible. Some of these amounts arose from the acquisition of producing assets from Advantage Oil & Gas Ltd. (Advantage) (note 5(a)), and the subsequent delay in some parties recognizing Questfire's ownership of the assets.

The Corporation manages the credit exposure related to cash and cash equivalents by selecting financial institutions with high credit ratings and monitors all short-term deposits to ensure an adequate rate of return. The Corporation manages the credit exposure related to risk management contracts by ensuring the contracts are entered into with counterparties that are financial institutions with high credit ratings. Given these credit ratings, management does not expect any counterparty to fail to meet its obligations.

d) Liquidity risk

Liquidity risk is the risk that the Corporation will not be able to meet its financial obligations as they are due. The Corporation's goals is to meet its liabilities when due, and its management of liquidity is structured accordingly. The Corporation's liquidity is affected by various external events and conditions, including commodity price fluctuations and global economic instability.

The Corporation expects to repay its financial liabilities in the normal course of operations and to fund future operational, capital and other obligations through future operating cash flow, as well as future equity and debt financings.

The timing of undiscounted cash flows relating to the financial liabilities outstanding at March 31, 2014 is outlined below:

	1 year	2 years	3 years	>3 years	Total
	$	$	$	$	$
Accounts payable and accrued liabilities	14,094,679	-	-	-	14,094,679
Risk management contracts	3,325,181	-	-	-	3,325,181
Bank debt [(1)]	42,000,000	-	-	-	42,000,000
Convertible debentures [(2)]	1,435,000	-	-	-	1,435,000
Long-term contract obligation [(3)]	2,326,300	2,326,300	2,326,300	15,672,439	22,651,339

(1) This amount excludes future interest payable on amounts drawn on the bank credit facility.

(2) The Corporation believes that the current portion of the convertible debentures will be converted into Class A shares but has adequate operating cash flow to repay this amount if required.

(3) This amount includes the payments required if the long-term contract obligation is repaid within 48 months of inception.

The Corporation's credit facility is a demand loan and, as such, the bank could demand repayment at any time. Management has not observed any indications that the bank would demand repayment within the next 12 months. Indications considered include the lack of any breach or default of credit facility covenants during the period by the Corporation, the initiation of the credit facility in 2013, and the renewal of the facility in March 2014. The Corporation further ensures it will have sufficient access to funds to meet short-term obligations by actively monitoring its credit facilities, and coordinating payment cycles with revenue cycles.

The Corporation is also subject to commitments as disclosed in note 18.

e) Market risk

Market risk is the risk that changes in market prices, such as commodity prices, interest rates and foreign exchange rates, will reduce the Corporation's net earnings or the value of financial instruments. These risks are largely outside the Corporation's control. The Corporation's objective is to manage and mitigate market risk exposure within acceptable limits, while maximizing returns. Market risks are as follows:

Foreign currency risk

Crude oil prices are determined in global markets and generally denominated in United States dollars. Natural gas prices obtained by the Corporation are influenced by U.S. and Canadian supply and demand and, to a much lesser degree, the international market for liquefied natural gas. An increase in the value of the Canadian dollar relative to the U.S. dollar will decrease the revenues received from the sale of oil and natural gas. The impact of such exchange rate fluctuations cannot be predicted. At March 31, 2014 and December 31, 2013, the Corporation had no forward exchange rate contracts nor any working capital denominated in foreign currencies.

Interest rate risk

Interest rate risk is the risk that future cash flows will fall as a result of changes in market interest rates. The Corporation has exposure to interest rate cash flow risk as its bank borrowing bears interest at variable rates. For the three months ended March 31, 2014, a 1 percent increase in interest rates would decrease income by approximately $79,000 (three months ended March 31, 2013 – $Nil). The Corporation had no interest rate swaps or contracts in place as at or during the three months ended March 31, 2014 or 2013.

Commodity price risk

The Corporation's operations expose it to fluctuations in commodity prices. Commodity prices for oil and natural gas are affected by global economic events that influence supply and demand. Questfire's management continuously monitors commodity prices and has opted to employ a number of risk-management instruments.

The Corporation's production was historically sold using spot or near-term contracts, with prices fixed at the time of transfer of custody or on the basis of a monthly average market price. The Corporation's policy is to limit swap commodity price contracts to a maximum of 50 percent of forecast production volume. The Corporation has also entered into other derivative financial instruments, being put options, to achieve this objective. Collars (which are generally fee-offsetting put and call options for the same volume and time-frame) ensure that the realized commodity prices will fall into a contracted range for a contracted sale volume based on the monthly index price, while puts ensure the realized price will not fall below a price floor. The purchase of put options creates a floor for the realized price, while maintaining exposure to potential price upside. At March 31, 2014, the Corporation's forward commodity contracts consisted of a mix of fixed-price, fixed-volume oil and natural gas swaps and purchased put options.

I. Summary of risk management positions

At March 31, 2014, Questfire had the following crude oil and natural gas risk management contracts with a total mark-to-market liability of $3,325,181:

Period	Commodity	Type of contract	Notional quantity	Pricing point	Contract price
Apr. 1/14 - Dec. 31/14	Natural gas	Fixed price	8,000 GJ/d	AECO 7A	Cdn$3.3575/GJ
Apr. 1/14 - Dec. 31/14	Natural gas	Purchased put (1)	5,000 GJ/d	AECO 7A	Cdn$3.00/GJ
Apr. 1/14 - Dec. 31/14	Natural gas	Purchased put (2)	10,000 GJ/d	AECO 7A	Cdn$3.00/GJ
Apr. 1/14 - Dec. 31/14	Crude oil	Fixed price	200 bbls/d	WTI Nymex	Cdn$94.80/bbl

(1) The put contracts require the Corporation to pay a monthly premium of approximately $28,000 over the term for a total premium of $332,150, of which $250,250 remains to be paid.

(2) The put contracts required the Corporation to pay total premiums of $424,313 at inception.

Reconciliation of unrealized risk management contracts during the three months ended March 31, 2014:

	Fair value	Total unrealized loss
	$	$
Fair value of contracts, beginning of period	(1,606,257)	-
Contracts entered into	81,900	-
Change in fair value of contracts	(1,800,824)	(1,800,824)
Fair value of contracts, end of period	**(3,325,181)**	**(1,800,824)**

II. Commodity price sensitivities – risk management positions

The following table summarizes the sensitivity of the fair value of Questfire's risk management contracts to fluctuations in commodity prices, with all other variables held constant. Management believes the price fluctuations identified in the table below are a reasonable measure of volatility. The impact of fluctuating commodity prices on the Corporation's risk management contracts at March 31, 2014 could have resulted in unrealized gains or losses affecting profit or loss for the three months ended March 31, 2014 as follows:

Commodity	**Sensitivity range**	**Increase**	**Decrease**
		$	**$**
Natural gas commodity price	± $0.10 per Mcf – AECO 7A contracts	(180,684)	182,295
Crude oil commodity price	± $1.00 per bbl – WTI Canadian contracts	(45,756)	45,756

f) Capital management

The Corporation maintains a flexible capital structure to maximize its ability to pursue oil and natural gas exploration and asset acquisition opportunities and to sustain future development of the business. The Corporation monitors risks for each capital project to balance the proportion of debt and equity in its capital structure. Its officers are responsible for managing its capital and do so through quarterly meetings and regular reviews of financial information, including budgets and forecasts. The Corporation's Board of Directors is responsible for overseeing this process. The Corporation considers its capital structure to include shareholders' equity or deficiency, the convertible Class B share liability, convertible debentures, long-term contract obligation and bank debt.

The Corporation monitors capital based on its current working capital, projected cash flow from operations and anticipated capital expenditures. In order to manage its capital structure, the Corporation prepares annual capital expenditure and operating budgets, which are updated throughout the year as necessary. The annual and updated budgets are prepared by management and approved by the Board of Directors. Results are regularly reviewed and updated as required.

In order to maintain or adjust its current and projected capital structure, the Corporation may issue shares, seek debt financing and adjust its capital spending. The Corporation's ability to raise additional debt or equity is affected by external conditions, including future commodity prices, particularly of natural gas, and by global economic conditions. The Corporation continually monitors business conditions, including: changes in economic conditions, the risks encountered in its drilling programs, forecast commodity prices, and potential corporate or asset acquisitions.

The Corporation has no externally imposed capital requirements other than its working capital covenants related to its bank debt (note 9) and any debt or equity to be raised is subject to approval by the Corporation's priority lender (note 9). The Corporation has not paid or declared any dividends since incorporation. There were no changes to the Corporation's approach to capital management during the three months ended March 31, 2014 other than entering into the long-term contract obligation (note 10) and the repurchase of the 2013 Debentures (note 13).

5. Acquisitions

a) On April 30, 2013, the Corporation completed its acquisition of producing assets in Alberta from Advantage Oil & Gas Ltd. (Advantage). The producing assets are all located in Alberta.

The acquisition has been accounted for using the purchase method, with the results of the acquired assets included in the Corporation's financial statements commencing on the day of closing.

The acquisition-date fair value of consideration transferred and net assets acquired was as follows:

	Recognized as of acquisition date $
Fair value of net assets acquired	
Risk management contracts	(2,782,639)
Office lease	312,944
Assets held for sale	281,000
Property and equipment	116,918,361
Decommissioning provisions	(33,636,218)
Total net assets acquired	81,093,448
Consideration	
Cash	40,608,830
Accrued liabilities assumed	200,000
Convertible senior secured debentures	30,284,618
Class B shares (note 12)	10,000,000
Total purchase price	81,093,448

The assets were acquired with full tax pools.

The Corporation funded the cash portion of the purchase price by entering into an agreement for a credit facility with National Bank of Canada and the Alberta Treasury Branches that provides a revolving operating demand loan of $60.0 million (note 9). Questfire paid National Bank Financial Inc. a success fee on closing of the asset purchase and credit facility.

The assets held for sale were disposed of prior to December 31, 2013. The current period's gain on sale of assets of $431,262 relates to assets acquired from Advantage that were assigned a value of $Nil at the time of acquisition.

b) On July 31, 2013, the Corporation purchased a working interest in certain Alberta producing assets for $1,506,310, which was allocated to property and equipment. The acquisition was accounted for using the purchase method, with the results of the operations of the acquired assets included in the Corporation's financial statements commencing on the acquisition date. The allocation of fair values to the net assets acquired is based on the best available information at this time and could be subject to further change.

During the three months ended March 31, 2014, the Corporation incurred $Nil (three months ended March 31, 2013 – $624,465) of costs related to acquisitions that are recorded as transaction costs in the statement of income (loss).

The revenues and profit or loss since the closing date of the acquisitions, and pro-forma revenues and profit or loss giving effect to the acquisitions as if they had occurred on January 1, 2013, are not practical to determine. The operations of the acquired assets are not managed as a separate business units, and the Corporation's general business overhead and other costs are not allocated or identified on a specific property basis. Such allocation would, accordingly, be arbitrary and would require significant assumptions and estimates concerning management's intentions and decision-making.

6. Property and equipment (P&E)

	Oil and natural gas interests	Corporate and other	Total
Cost	$	$	$
Balance, December 31, 2013	131,058,561	146,349	131,204,910
Additions	3,172,446	3,557	3,176,003
Disposals	(40,049)	-	(40,049)
Decommissioning provision	218,731	-	218,731
Balance, March 31, 2014	**134,409,689**	**149,906**	**134,559,595**
Accumulated depletion, depreciation and impairment			
Balance, December 31, 2013	9,023,824	41,000	9,064,824
Depletion and depreciation	2,999,411	7,721	3,007,132
Balance, March 31, 2014	**12,023,235**	**48,721**	**12,071,956**
Balance, December 31, 2013	122,034,737	105,349	122,140,086
Balance, March 31, 2014	**122,386,454**	**101,185**	**122,487,639**

To date, the Corporation has not capitalized any interest nor general and administrative expenses to P&E.

7. Impairment

At March 31, 2014, the Corporation assessed its P&E cash-generating units (CGUs) and exploration and evaluation (E&E) assets for indicators of impairment and noted none. There were no impairment reversals for either P&E or E&E during the three months ended March 31, 2014 or 2013.

8. Accounts payable and accrued liabilities

As at	March 31, 2014	December 31, 2013
	$	$
Accruals	**5,171,358**	6,944,491
Trade	**8,752,102**	5,222,409
Other	**171,219**	80,793
	14,094,679	12,247,693

9. Bank debt

On April 30, 2013, the Corporation entered into a $60.0 million demand revolving credit facility with a syndicate of Canadian banks (the “Credit Facility”). The Credit Facility provided that advances may be made by way of direct advances, bankers’ acceptances or standby letters of credit.

The Corporation negotiated with a syndicate of Canadian banks for the provision, effective March 26, 2014, of a revised revolving credit facility in the amount of $55.0 million (replacing the $60.0 million revolving credit facility as described above) and a new $5.0 million non-revolving development demand line (together, the “Revolving Credit Facility”). The $55.0 million revolving credit facility will be reduced to $52.5 million on September 30, 2014, and $50.0 million on December 31, 2014.

The Corporation is subject to certain reporting and financial covenants on its Revolving Credit Facility. The financial covenant requires the Corporation to maintain an adjusted working capital ratio of at least 1:1 (for purposes of the covenant, bank debt, the current portion of any subordinated convertible debentures, and the fair value of any risk management contracts are excluded and the undrawn portion of the revolving credit facility is added to current assets). The covenant was met at March 31, 2014 at 2.10:1. The Corporation is limited to hedging no greater than 60 percent of its production (not including put options). The Corporation is also required to enter into hedging contracts for at least 50 percent of its forecast natural gas production for 2015 and 2016, at a price equal to or above $3.00 per GJ, before July 1, 2014 (see note 4(e)).

At March 31, 2014, $42.0 million of the Revolving Credit Facility was drawn. It bears interest at a floating rate based on the applicable Canadian prime rate, plus between 1.00 percent and 3.00 percent depending on the Corporation’s net debt to cash flow ratio. For the three months ended March 31, 2014, the average effective interest rate was 4.4 percent. The Revised Credit Facility is secured by all assets of the Corporation, except as described in note 10.

At March 31, 2014, the Corporation had letters of credit of $350,000, which reduces the borrowing capacity under the Revolving Credit Facility.

10. Long-term contract obligation

On March 26, 2014, the Corporation entered into a facilities joint venture agreement with a third party (the “Partner”). The Corporation received $15.0 million, which was used to fund the repurchase of the 2013 Debentures (note 13), in exchange for beneficial ownership of Questfire’s natural gas processing facilities at Lookout Butte and Medicine Hat, Alberta. Questfire will operate the facilities and continue to process its Lookout Butte and Medicine Hat natural gas production through the facilities. The Corporation will pay an annual facility fee of $2,326,300 for 17.5 years, after which beneficial ownership will revert to Questfire.

Questfire has the option to terminate the joint venture agreement on payment of an amount which will provide the Partner with a compound annual yield on its investment of 13.25 percent to the later of 48 months or until the option is exercised. Upon the payment of aggregate processing fees to the Partner of a minimum of $19,500,000, the Partner has the option to sell back to Questfire its interest in the facilities for the sum equal to the total remaining scheduled processing payments, discounted at 17.5 percent back to the time of exercise. The long-term contract obligation is secured

by Questfire's Lookout Butte and Medicine Hat natural gas processing facilities. Questfire has also indemnified the Partner for all costs and expenses that may arise out of the operation of the facilities.

This transaction effectively leaves substantially all of the economic risks and rewards of ownership with Questfire and will be accounted for similarly to a sale and leaseback transaction, whereby Questfire will continue to record the facility as property and equipment on its balance sheet and will account for the $15.0 million proceeds as a long-term contract obligation and the annual facility fee payments as blended repayments of principal and interest expense.

11. Decommissioning provisions

The Corporation's decommissioning provisions result from its ownership interest in oil and natural gas assets, including well sites, facilities and gathering systems. The total decommissioning provision is estimated based on the Corporation's net ownership interest, estimated costs to reclaim and abandon its wells, facilities and gathering systems and the estimated timing of the costs to be incurred in future years. The estimated cash flows required to settle the provisions, excluding salvage, are approximately $91.8 million at March 31, 2014 (December 31, 2013 – $91.2 million). This was inflated using a weighted-average rate of 2.0 percent (December 31, 2013 – 2.0 percent), to arrive at undiscounted future cash flows of approximately $173.3 million at March 31, 2014 (December 31, 2013 – $173.1 million), and then discounted using a weighted-average credit-adjusted risk-free rate of 6.48 percent at March 31, 2014 (December 31, 2013 – 6.48 percent) to arrive at the present value of the decommissioning provision as disclosed in the table below. The weighted-average credit-adjusted risk-free rate is based on a combination of Government of Canada benchmark bond rates and an adjustment for Questfire's estimated credit risk. These obligations are to be settled based on the estimated economic lives of the underlying assets, which currently extend up to 50 years into the future, and will be funded from general corporate resources at the time of abandonment.

The following table reconciles the decommissioning provisions for the three months ended March 31, 2014:

As at	**March 31, 2014**
	$
Balance, beginning of period	34,706,080
Additions	60,688
Costs incurred	(752,049)
Accretion (note 15)	509,190
Change in estimated future cash flows	-
Change in discount rate	158,043
Balance, end of period	34,681,952

Sensitivities

Changes to the risk-free discount rate or the inflation rate would have had the following impact on the decommissioning provisions:

As at	**March 31, 2014**	
	Credit-adjusted risk-free discount rate	Inflation rate
	$	$
1 percent increase	(3,739,827)	5,355,053
1 percent decrease	5,037,715	(3,999,382)

12. Convertible Class B shares

Class B shares are convertible (at Questfire's option) into Class A shares any time after September 30, 2014 and on or before November 30, 2016. The number of Class A shares to be issued upon conversion of one Class B share is calculated by dividing $10 by the greater of $1 and the 30 day weighted average market price of the Class A shares. If conversion has not occurred by the close of business on November 30, 2016, the Class B shares become convertible (at the option of the shareholder) into Class A shares on the same basis. Effective at the close of business on December 31, 2016, all remaining Class B shares will be automatically converted into Class A shares. The Class B shares are listed and posted for trading on the TSXV under the symbol "Q.B".

The Class B shares were determined to be compound financial instruments. As the Class B shares are convertible into Class A shares, based on the conversion formula above, the number of Class A shares is unknown and, therefore, they are presented as a liability.

The Class B share liability related to the Class B shares issued in 2011 ("2011 Class B shares"), estimated at issuance to be $3,576,932, based on the present value of discounted cash flows using a discount rate of 9 percent, is accreted using the effective interest rate method over the term of the 2011 Class B shares, such that the carrying amount of the financial liability will be equal to the principal of $5,558,400 at maturity. Upon issuance of the 2011 Class B shares, the Corporation recognized the equity component of the convertible 2011 Class B shares as a conversion option of $1,585,985, with a further $495,367 related to the deferred income tax effect of the 2011 Class B shares, for a total of $2,081,352.

The Class B share liability related to the shares issued in 2013 ("2013 Class B shares"), estimated at issuance to be $10.0 million, based on the present value of discounted cash flows using a discount rate of 11.69 percent, is accreted using the effective interest rate method over the term of the 2013 Class B shares, such that the carrying amount of the financial liability will be equal to the principal of $15.0 million at maturity. Upon issuance of the 2013 Class B shares, the Corporation estimated the equity component to be $Nil.

On March 26, 2014, the Corporation executed an agreement with Advantage whereby Questfire agreed that it would make an offer to purchase, by way of Issuer Bid, all of its 2,055,840 issued and outstanding Class B shares at a purchase price of $2.60 per share, which was mailed to shareholders. Advantage agreed to tender all of its 1,500,000 Class B shares to the Issuer Bid. The Issuer Bid was open for acceptance until May 5, 2014. Subsequent to the end of the quarter, 1,505,400 Class B shares were tendered through the Issuer Bid, and were repurchased by the Corporation for $3,914,040.

The Corporation has authorized an unlimited number of Class B shares. The following table is a continuity of the convertible Class B shares liability:

As at	**March 31, 2014**	
	Number of shares	Amount $
Balance, beginning of period	2,055,840	15,088,437
Accretion of convertible Class B shares liability (note 15)	-	395,925
Balance, end of period	**2,055,840**	**15,484,362**

13. Convertible debentures

On June 28, 2012, the Corporation completed the issuance of unsecured senior convertible debentures (the "2012 Debentures") for gross proceeds of $1,510,000 ($1,444,497 net), of which $750,000 was raised from officers and directors of the Corporation. The Corporation issued 302 units at a price of $5,000 per unit, with each unit being comprised of one $5,000 debenture and 5,000 Class A share purchase warrants. The 2012 Debentures bear interest at a rate of 12 percent per annum, payable quarterly in arrears commencing on September 30, 2012, mature on June 30, 2014 and can be converted into Class A shares of Questfire any time at the option of the holders at a conversion price of $0.50 per Class A share. In aggregate the Corporation issued 1,510,000 share purchase warrants and each warrant entitles the holder to acquire one Class A share at a price of $0.75 until June 30, 2014. These warrants are all outstanding at March 31, 2014.

During the year ended December 31, 2013, $75,000 of the 2012 Debentures were converted into 150,000 Class A shares by officers and directors of the Corporation.

The 2012 Debentures are classified as debt, net of issuance costs and of the fair value of the conversion feature and the warrants (the "Conversion Features") at the date of issuance, which have been classified in shareholders' equity. The issuance costs will be amortized over the term of the debentures and the debt portion will accrete up to the original face value at maturity. The accretion, amortization of issuance costs and interest paid are expensed to profit or loss. The fair value of the Conversion Features was determined at the time of issuance as the difference between the face value of the debentures and the discounted cash flows assuming an 18 percent effective interest rate, the estimated rate for debt with similar terms but without convertibility. If the debentures or the warrants are converted to Class A shares, a portion of the value of the Conversion Features under shareholders' equity will be reclassified to share capital along with the conversion price paid.

On April 30, 2013, the Corporation issued convertible debentures in association with the acquisition discussed in note 5 (the "2013 Debentures"). The 2013 Debentures have a face value of $32,585,000, and the Corporation incurred $62,875 of issuance costs. The 2013 Debentures bear interest at a rate of 6 percent per annum until April 30, 2014, 7 percent per annum from May 1, 2014 to April 30, 2015, and 9 percent per annum from May 1, 2015 until maturity on April 30, 2016. Interest on the 2013 Debentures is payable quarterly in arrears, and commenced on June 30, 2013. They mature on April 30, 2016 and can be converted into Class A shares of Questfire at a conversion price equal to the trailing 20-day volume-weighted average trading price of Class A shares at the time of exercise for a 30-day period following certain events listed below:

i) If the Corporation chooses to pay interest by delivering Class A shares to the debenture trustee;
ii) Any event of default;
iii) Any conversion by the Corporation of Class B shares into Class A shares;
iv) The date 30 months from closing;
v) The date one month before maturity;
vi) Upon a change of control; or
vii) Upon an equity financing by the Corporation whereby the holder of a Debenture has the option of conversion (at the financing price), up to a maximum of 50 percent of the total shares issued in the financing, unless mutually agreed to otherwise.

The 2013 Debentures were classified as debt, net of issuance costs. The debt portion was accreting up to the original face value at maturity, with the accretion and interest paid expensed to profit or loss. The fair value of the 2013 Debentures was determined at the time of issuance based on the discounted cash flows assuming a 10 percent effective interest rate, the estimated rate for debt with similar terms but without convertibility. The conversion feature of the 2013 Debenture was recorded as a liability as it converted at market prices, and as such its fair value was nominal.

On March 26, 2014, the Corporation executed an agreement with Advantage to repurchase all of the 2013 Debentures. These debentures were repurchased for $13.6 million, resulting in a gain of approximately $17.7 million.

The following table is a continuity of the 2012 and 2013 Debentures for the three months ended March 31, 2014:

	Liability component	**Warrants**	**Equity conversion feature**	**Total**
	$	**$**	**$**	**$**
Balance, December 31, 2013	32,385,112	28,295	75,805	32,489,212
Repurchases	(31,322,983)	-	-	(31,322,983)
Accretion of discount (note 15)	346,673	-	-	346,673
Balance, March 31, 2014	**1,408,802**	**28,295**	**75,805**	**1,512,902**

As the 2012 Debentures mature on June 30, 2014, the liability component has been classified as a current liability.

14. Share capital

a) Authorized – Unlimited number of Class A and Class B common shares with no par value.

b) Issued - Class A shares

	Number of shares	Amount $
Balance, December 31, 2013 and March 31, 2014	**12,963,001**	**4,272,595**

c) Income (loss) per share

The following table sets forth the computation of per share amounts:

Three months ended March 31,	2014 $	2013 $
Numerator		
Income (loss) attributable to Class A shares	**14,375,280**	(1,102,943)
Adjustment for dilutive effect of convertible debentures, net of tax	**633,766**	-
Adjustment for dilutive effect of Class B shares, net of tax	**296,943**	-
Numerator for diluted per share amounts	**15,305,989**	(1,102,943)
	Number of shares	
	#	**#**
Denominator		
Weighted-average number of shares outstanding for basic per share calculation	**12,963,001**	12,813,001
Stock options	**1,127,968**	-
Warrants	**735,362**	-
Convertible debentures	**21,424,086**	-
Class B shares	**12,093,177**	-
Denominator for diluted per share amounts	**48,343,594**	12,813,001
	$	$
Basic income (loss) per share attributable to Class A shares	**1.11**	(0.09)
Diluted income (loss) per share attributable to Class A shares	**0.32**	(0.09)

For the three months ended March 31, 2014, the Corporation excluded the following securities from the calculation of diluted income (loss) per share as they would be anti-dilutive:

i. Stock options – 345,000 (three months ended March 31, 2013 – 1,281,000), with a weighted-average exercise price of $1.11 (three months ended March 31, 2013 – $0.20)
ii. Warrants – Nil (three months ended March 31, 2013 – 1,510,000)
iii. Class B shares – Nil (three months ended March 31, 2013 – 555,840)
iv. Face value of convertible debentures – $Nil (three months ended March 31, 2013 – $1,510,000)

d) Shares in escrow

At March 31, 2014 a total of 2,458,500 Class A shares (December 31, 2013 – 2,458,500) were held in escrow pursuant to TSXV requirements. Of the remaining shares, 1,229,250 were released from escrow on April 25, 2014. The remaining 1,229,250 will be released on October 25, 2014. The above escrow release schedule is subject to acceleration in accordance with National Policy 46-201, *Escrow for Initial Public Offerings,* and the policies of the TSXV in the event that the Corporation meets certain listing requirements.

e) Share-based compensation

The Corporation has a stock option plan under which it is authorized to issue stock options to employees, officers, directors and consultants for up to 20 percent of the total issued and outstanding number of Class A and Class B shares. Options under the stock option plan cannot have an exercise price less than the closing market price on the day immediately preceding grant and expire a maximum of ten years from grant. It is the Corporation's intention for the options it grants generally to vest as to one-third on each of the first, second and third anniversaries of grant and expire ten years from grant.

During the three months ended March 31, 2014, the Corporation granted 160,000 options (three months ended March 31, 2013 – nil) to acquire Class A shares. The options vest one-third on each of the first, second and third anniversaries of grant and expire ten years from grant. The fair value of the options granted during the three months ended March 31, 2014 was estimated at $89,078, using the Black-Scholes option pricing model with the following weighted-average assumptions: an exercise price of $0.95, market price of Class A shares of $0.95, a risk-free interest rate of 2.00 percent, volatility of 73 percent, an expected life of six years, a forfeiture rate of 10 percent and no dividend yield.

The following table provides information with respect to stock option transactions:

	March 31, 2014	
	Number of options	**Weighted-average exercise price $**
Outstanding, beginning of period	1,971,000	0.48
Granted	160,000	0.95
Forfeited	(75,000)	0.65
Outstanding, end of period	**2,056,000**	**0.51**

The following provides information about stock options outstanding at March 31, 2014:

Range of exercise prices ($)	Number outstanding	Weighted-average remaining contractual life (years)	Options outstanding – weighted-average exercise price ($)	Number exercisable	Options exercisable – weighted-average exercise price ($)
0.20 - 0.65	1,326,000	7.62	0.22	854,000	0.20
0.95 - 1.25	730,000	9.45	1.04	-	-
	2,056,000	**8.27**	**0.51**	**854,000**	**0.20**

15. Finance expense

Three months ended March 31,	**2014**	2013
	$	$
Finance expense		
Interest on convertible debentures	**(498,348)**	(45,450)
Interest on bank debt	**(446,367)**	-
Interest on long-term contract obligation	**(32,445)**	
Financing costs	**(186,649)**	-
Accretion on decommissioning provisions (note 11)	**(509,190)**	(2,537)
Accretion on convertible Class B share liability (note 12)	**(395,925)**	(86,392)
Accretion on convertible debentures (note 13)	**(346,673)**	(26,198)
Total finance expense	**(2,415,597)**	(160,577)

16. Supplemental cash flow information

Changes in non-cash working capital are comprised of:

Three months ended March 31,	**2014**	2013
	$	$
Cash flows related to:		
Accounts receivable	**(2,238,935)**	130,351
Deposits and prepaid expenses	**18,004**	(43,050)
Accounts payable and accrued liabilities	**1,846,986**	962,264
	(373,945)	1,049,565
Acquired non-cash working capital items:		
Office lease amortization	**(69,543)**	-
Changes in non-cash working capital	**(443,488)**	1,049,565
Relating to:		
Operating activities	**1,066,737**	1,065,717
Investing activities	**(1,664,134)**	(16,152)
Financing activities	**153,909**	-
	(443,488)	1,049,565

17. Related-party transactions

A director of Questfire is a partner of a law firm that provides legal services to Questfire. Legal fees of $147,193 were incurred by Questfire to the law firm in the three months ended March 31, 2014 (three months ended March 31, 2013 – $150,000), of which $19,816 (three months ended March 31, 2013 – $Nil) was charged to general and administrative expenses, $Nil to transaction costs (three months ended March 31, 2013 – $150,000) and $127,377 (three months ended March 31, 2013 – $Nil) to financing expense. At March 31, 2014, $143,642 (December 31, 2013 – $21,230) related to these amounts was included in accounts payable and accrued liabilities and was due under normal credit terms.

18. Commitments

As part of its normal operations, Questfire has committed to paying certain amounts over the next five years and thereafter as follows:

	2014	2015	2016	2017	2018	Thereafter
	$	$	$	$	$	$
Office leases	311,577	401,616	401,616	401,616	401,616	234,276

Questfire's commitments related to its risk management program are disclosed in note 4(e).

19. Subsequent events

Subsequent to March 31, 2014, the Corporation granted a total of 615,000 stock options to employees, officers, directors and consultants, of which 320,000 were granted to directors and officers, at an exercise price of $2.05 per Class A share, based on the closing market price on the day of the grant. The options will vest as to one-third on each of the first, second, and third anniversaries of grant and expire ten years from grant.

On May 5, 2014, the Issuer Bid described in note 12 closed. A total of 1,505,400 Class B shares were tendered through the Issuer Bid, and were repurchased by the Corporation for $3,914,040. This transaction will result in a repurchase gain in the amount of approximately $7.3 million that will be recognized during the three and six months ending June 30, 2014.