ANNUAL REPORT
AS AT AND FOR THE YEAR ENDED
DECEMBER 31, 2014

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FINANCIAL AND OPERATIONAL HIGHLIGHTS	Three months ended December 31			Year ended December 31		
(CA$ thousands, except as otherwise indicated)	**2014**	2013	%	**2014**	2013	%
FINANCIAL						
Revenue, before royalties and financial instruments	**54,396**	18,543	193%	**214,691**	46,656	360%
Funds from operations[(1)]	**29,664**	9,396	216%	**115,503**	23,656	388%
Basic ($/ common share)[(1)]	**0.23**	0.09	156%	**0.95**	0.32	197%
Diluted ($/ common share)[(1)]	**0.23**	0.09	156%	**0.93**	0.32	191%
Profit (loss) and comprehensive income (loss)	**1,256**	(1,838)	-	**10,628**	(5,115)	-
Basic ($/ common share)	**0.01**	(0.02)	-	**0.09**	(0.07)	-
Diluted ($/ common share)	**0.01**	(0.02)	-	**0.09**	(0.07)	-
Total capital expenditures, net of dispositions	**99,466**	231,329	-57%	**423,900**	329,143	29%
Total assets	**908,709**	485,201	87%	**908,709**	485,201	87%
Bank debt	**46,929**	-	-	**46,929**	-	-
Working capital deficiency (surplus)	**57,501**	(20,500)	-	**57,501**	(20,500)	-
Shareholders' equity	**619,639**	392,872	58%	**619,639**	392,872	58%
Weighted average shares outstanding (000's)						
Basic	**126,760**	99,244	28%	**121,779**	74,554	63%
Diluted	**128,512**	100,242	28%	**124,296**	75,093	66%
OPERATIONS						
Average daily production						
Oil (bbls/d)	**4,691**	809	480%	**3,413**	516	561%
NGLs (bbls/d)	**1,037**	487	113%	**924**	297	211%
Gas (mcf/d)	**58,984**	26,660	121%	**50,516**	18,888	167%
Combined (BOE/d)	**15,559**	5,739	171%	**12,756**	3,961	222%
Production per million common shares (BOE/d)[(1)]	**123**	58	112%	**105**	53	98%
Average realized prices, after financial instruments						
Oil ($/bbl)	**74.11**	81.35	-9%	**85.53**	86.77	-1%
NGLs ($/bbl)	**47.48**	57.00	-17%	**59.73**	52.76	13%
Gas ($/mcf)	**3.81**	3.97	-4%	**4.75**	3.51	35%
Operating netbacks[(1)] ($/BOE)						
Oil and gas revenue	**38.00**	35.12	8%	**46.11**	32.27	43%
Cash premium on financial instruments	**-**	-	-	**-**	0.16	-100%
Realized gain (loss) on financial instruments	**1.96**	(0.38)	-	**(0.08)**	(0.40)	-80%
Average realized price, after financial instruments	**39.96**	34.74	15%	**46.03**	32.03	44%
Royalties	**(4.55)**	(4.71)	-3%	**(6.11)**	(4.37)	40%
Production and transportation expense	**(13.86)**	(11.36)	22%	**(14.30)**	(10.69)	34%
Operating netback[(1)]	**21.55**	18.67	15%	**25.62**	16.97	51%
Drilling activity						
Total wells	**9**	6	50%	**36**	19	89%
Working interest wells	**5.4**	4.2	29%	**27.1**	12.2	122%
Success rate on working interest wells	**100%**	100%	0%	**100%**	100%	0%
Undeveloped land						
Gross acres	**494,361**	299,142	65%	**494,361**	299,142	65%
Net acres	**318,743**	184,082	73%	**318,743**	184,082	73%
Reserves – proved plus probable						
Oil (mbbls)	**23,474**	11,808	99%	**23,474**	11,808	99%
NGLs (mbbls)	**10,800**	5,002	116%	**10,800**	5,002	116%
Gas (mmcf)	**389,014**	254,329	53%	**389,014**	254,329	53%
Combined (mBOE)	**99,110**	59,198	67%	**99,110**	59,198	67%

(1) Refer to advisory regarding non-GAAP measures.

MESSAGE TO SHAREHOLDERS

Kelt Exploration Ltd. ("Kelt" or the "Company") is pleased to report its fourth quarter interim results and full year results to shareholders for the three months and twelve months ended December 31, 2014.

Kelt achieved record production levels in the fourth quarter of 2014. Average production for the three months ended December 31, 2014 was 15,559 BOE per day, up 171% from the average production of 5,739 BOE per day during the fourth quarter of 2013. On a production per share basis, the fourth quarter of 2014 was up 112% compared to the fourth quarter of 2013. Daily average production in the fourth quarter of 2014 was 12% higher than the average production of 13,872 BOE per day in the third quarter of 2014.

For the three months ended December 31, 2014, revenue was $54.4 million, funds from operations was $29.7 million ($0.23 per share, diluted) and profit was $1.3 million ($0.01 per share, diluted). For the year ended December 31, 2014, revenue was $214.7 million, funds from operations was $115.5 million ($0.93 per share, diluted) and profit was $10.6 million ($0.09 per share, diluted). At December 31, 2014, bank debt, net of working capital was $104.4 million.

During the three months ended December 31, 2014, Kelt drilled 9 gross (5.4 net) oil and gas wells, with a 100% success rate. During the year ended December 31, 2014, Kelt drilled 36 gross (27.1 net) oil and gas wells, with a 100% success rate.

Net capital expenditures incurred during the year were $423.9 million of which $256.3 million was exploration and development expenditures and $167.6 million was for the acquisition of Capio Exploration Ltd. Exploration and development expenditures of $99.5 million in the fourth quarter of 2014 are expected to contribute to 2015 production additions as the wells are brought on-stream.

In February 2015, Kelt announced that it had entered into an agreement with Artek Exploration Ltd. ("Artek"), pursuant to which Kelt will acquire all of the issued and outstanding common shares of Artek on the basis of 0.34 of a Kelt common share for each Artek common share. The acquisition will be effected by way of a statutory plan of arrangement (the "Artek Arrangement"). Based on the volume-weighted average trading price of the Kelt common shares for the five trading days ended February 20, 2015 of $8.10 on the Toronto Stock Exchange ("TSX"), the deemed acquisition price is approximately $307 million, comprised of the issuance of approximately 26.9 million Kelt common shares and the assumption of an estimated $89.5 million of net debt as of February 20, 2015, which includes estimated associated transaction costs of approximately $5.6 million.

Completion of the Artek Arrangement is anticipated to occur on or around April 16, 2015. The acquisition of Artek consolidates the majority of Kelt's land acreage in its Inga-Fireweed-Stoddart, British Columbia core area to 100% and is consistent with the Company's strategy to operate and control all of its major core exploration and development prospects. In addition, Kelt's acquisition of Artek will result in 100% ownership by Kelt in key infrastructure including compression facilities and pipelines in the area. The net present value of Artek's Inga-Fireweed-Stoddart reserves at December 31, 2014 represented approximately 90% of Artek's total corporate reserves value.

Key attributes of Kelt's acquisition of Artek include:

- Accretion to existing Kelt shareholders on a reserves per share, production per share, funds from operations per share and net asset value per share basis;
- Artek's reserves at December 31, 2014 consist of 24.0 million BOE of proved reserves and 46.4 million BOE of proved plus probable reserves;
- Acquisition cost, including future development capital costs and estimated associated transaction costs, is $20.46 per BOE for proved reserves and $12.89 per BOE for proved plus probable reserves;
- Artek's January 2015 production is estimated to be approximately 5,400 BOE per day; and
- Artek's land holdings at December 31, 2014 were 262,254 net acres of which 202,967 net acres were undeveloped.

In March 2015, Kelt announced that it had increased its previously announced non-brokered private placement of common shares, issued on a "flow-through" basis in respect of Canadian development expenses at a price of $8.60 per share, from $28.4 million to $33.4 million (the "Private Placement"). Proceeds from the Private Placement will be used to partially finance the Company's drilling and completion expenditures during the remainder of 2015. Pursuant to the Private

Placement, the Company has issued 3.3 million flow-through common shares for gross proceeds of $28.4 million and has received commitments from subscribers to purchase an additional 581,400 flow-through common shares for aggregate gross proceeds of $5.0 million, which is expected to close on or about March 16, 2015.

Certain directors, officers and employees of the Company have been issued an aggregate of 1.7 million flow-through common shares for gross proceeds of $14.7 million representing approximately 44% of the aggregate issue.

After giving effect to the Artek Arrangement and after giving effect to the Private Placement, Kelt's pro-forma bank debt, net of working capital at December 31, 2015 is estimated to be $198.0 million or 1.7 times estimated pro-forma 2015 funds from operations.

In light of the current energy business environment with much lower oil and gas prices compared to 2014, Kelt has taken steps to take advantage of acquisition opportunities and has positioned itself financially to create sufficient financial flexibility to carry out its operations during the remainder of the year. Management is excited about the Company's prospects and looks forward to updating shareholders with 2015 first quarter results on or about May 15, 2015.

On behalf of the Board of Directors,

[signed]

David J. Wilson
President and Chief Executive Officer
March 9, 2015

MANAGEMENT'S DISCUSSION & ANALYSIS

INTRODUCTION

Kelt Exploration Ltd. ("Kelt" or the "Company") is an oil and gas company based in Calgary, Alberta, focused on the exploration, development and production of crude oil and natural gas resources, primarily in west central Alberta and northeastern British Columbia. The Company was incorporated under the *Business Corporations Act* (Alberta) on October 11, 2012 as 1705972 Alberta Ltd. and was inactive until February 26, 2013. On October 19, 2012, Articles of Amendment were filed to change the name of the Company to Kelt Exploration Ltd. Common shares of the Company are listed and posted for trading on the Toronto Stock Exchange ("TSX") under the symbol "KEL". The head office of Kelt is located at Suite 300, 311 – 6th Avenue S.W., Calgary, Alberta T2P 3H2.

Additional information relating to Kelt can be found on SEDAR at www.sedar.com.

This Management's Discussion and Analysis ("MD&A") is dated March 9, 2015 and should be read in conjunction with the Company's audited annual financial statements and related notes as at and for the year ended December 31, 2014. The accompanying financial statements have been prepared in accordance with Canadian generally accepted accounting principles ("GAAP") as set out in the *CPA Canada Handbook – Accounting* ("CPA Handbook"). The CPA Handbook incorporates International Financial Reporting Standards ("IFRS") and publicly accountable enterprises, such as Kelt, are required to apply such standards. The Company's Board of Directors approved and authorized the financial statements for issue on March 9, 2015.

The Company was incorporated as a wholly owned subsidiary of Celtic Exploration Ltd. ("Celtic"), for the purposes of participating in a Plan of Arrangement (the "Arrangement") between ExxonMobil Canada Ltd. ("ExxonMobil Canada"), ExxonMobil Celtic ULC (formerly 1690731 Alberta ULC) (the "Purchaser"), Celtic and Kelt. Pursuant to the Arrangement, the Purchaser purchased all of Celtic's outstanding common shares ("Celtic Shares"), including Celtic Shares issued upon conversion of Celtic's 5% convertible debentures, at a cash price of $24.50 per Celtic Share. Additionally, Celtic shareholders received one-half (1/2) of a share of Kelt for each Celtic Share.

Pursuant to the Arrangement and a conveyance agreement (the "Conveyance Agreement") entered into by Celtic and Kelt upon closing of the Arrangement on February 26, 2013, Celtic transferred certain petroleum and natural gas assets (the "Celtic Assets") to Kelt in exchange for $142.0 million of common share consideration (the "Common Control Transaction"). The Celtic Assets transferred pursuant to the Common Control Transaction included all of Celtic's rights, title, estate and interest in the petroleum, natural gas and related hydrocarbon rights and related personal property interests within, upon or under the lands and leases, including: a liquids-rich gas property in the Inga area of northeastern British Columbia; a gas property in the Grande Cache area of Alberta; and an oil prospect in the Karr area of west central Alberta.

Kelt commenced active operations on February 27, 2013 following completion of the Arrangement and the Common Control Transaction. Prior to completion of the Arrangement on February 26, 2013, the Company did not have any assets, liabilities, or operations.

ADVISORY REGARDING FORWARD-LOOKING STATEMENTS

This MD&A contains forward-looking statements and forward-looking information within the meaning of applicable securities laws. The use of any of the words "expect", "anticipate", "continue", "estimate", "objective", "ongoing", "may", "will", "project", "should", "believe", "plans", "intends" and similar expressions are intended to identify forward-looking information or statements. In particular, this MD&A contains forward-looking statements pertaining to the following: the Company's expected future financial position, operating results and its planned 2015 capital expenditure budget; the amount and timing of future development capital expenditures; the extent of Kelt's reserves and resources; the expected extension of the Company's Credit Facility (defined herein); the pro-forma effect of the 2015 Private Placement (defined herein); the expected closing of the Artek Arrangement (defined herein) and the pro-forma effect of the Artek Arrangement on the Company's financial position and average daily production, as well as the anticipated accretive impact of the Artek Arrangement on reserves per share, production per share, funds from operations per share, and net asset value per share. Statements relating to "reserves" or "resources" are deemed to be forward looking statements, as they involve the implied assessment, based on certain estimates and assumptions, that the reserves described exist in the quantities predicted or estimated and that the reserves can be profitably

produced in the future. Actual reserves may be greater than or less than the estimates provided herein.

Although Kelt believes that the expectations and assumptions on which the forward-looking statements are based are reasonable, undue reliance should not be placed on the forward-looking statements because Kelt cannot give any assurance that they will prove to be correct. Since forward-looking statements address future events and conditions, by their very nature they involve inherent risks and uncertainties. Actual results could differ materially from those currently anticipated due to a number of factors and risks. These include, but are not limited to, the risks associated with the oil and gas industry in general (e.g., operational risks in development, exploration and production; delays or changes in plans with respect to exploration or development projects or capital expenditures; the uncertainty of reserve estimates; the uncertainty of estimates and projections relating to production, costs and expenses; failure to obtain necessary regulatory approvals for planned operations; health, safety and environmental risks; uncertainties resulting from potential delays or changes in plans with respect to exploration or development projects or capital expenditures; volatility of commodity prices, currency exchange rate fluctuations; imprecision of reserve estimates; and competition from other explorers) as well as general economic conditions, stock market volatility; and the ability to access sufficient capital. We caution that the foregoing list of risks and uncertainties is not exhaustive.

In addition, the reader is cautioned that historical results are not necessarily indicative of future performance. The forward-looking statements contained herein are made as of the date hereof and the Company does not intend, and does not assume any obligation, to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise unless expressly required by applicable securities laws.

Certain information set out herein may be considered as "financial outlook" within the meaning of applicable securities laws. The purpose of this financial outlook is to provide readers with disclosure regarding Kelt's reasonable expectations as to the anticipated results of its proposed business activities for the periods indicated. Readers are cautioned that the financial outlook may not be appropriate for other purposes.

NON-GAAP MEASURES

This document contains certain financial measures, as described below, which do not have standardized meanings prescribed by GAAP. As these measures are commonly used in the oil and gas industry, the Company believes that their inclusion is useful to investors. The reader is cautioned that these amounts may not be directly comparable to measures for other companies where similar terminology is used.

"Operating income" is calculated by deducting royalties, production expenses and transportation expenses from oil and gas revenue, after realized gains or losses on financial instruments. The Company refers to operating income expressed per unit of production as an "Operating netback". "Funds from operations" is calculated by adding back settlement of decommissioning obligations and change in non-cash operating working capital to cash provided by operating activities. Funds from operations per common share is calculated on a consistent basis with profit (loss) per common share, using basic and diluted weighted average common shares as determined in accordance with GAAP. Funds from operations and operating income or netbacks are used by Kelt as key measures of performance and are not intended to represent operating profits nor should they be viewed as an alternative to cash provided by operating activities, profit or other measures of financial performance calculated in accordance with GAAP.

The following table reconciles cash provided by operating activities to funds from operations:

	Three months ended December 31			Year ended December 31		
(CA$ thousands, except as otherwise indicated)	**2014**	2013	%	**2014**	2013	%
Cash provided by operating activities	**28,300**	13,866	104%	**112,391**	26,891	318%
Settlement of decommissioning obligations	**83**	-	-	**229**	-	-
Change in non-cash working capital	**1,281**	(4,470)	-	**2,883**	(3,235)	-
Funds from operations	**29,664**	9,396	216%	**115,503**	23,656	388%

The following table demonstrates the calculation of operating income derived from the individual financial statement line items in accordance with GAAP:

	Three months ended December 31			Year ended December 31		
(CA$ thousands, except as otherwise indicated)	**2014**	2013	%	**2014**	2013	%
Oil and gas sales	**54,396**	18,543	193%	**214,691**	46,656	360%
Cash premium on financial instruments	**-**	-	-	**-**	228	-100%
Realized gain (loss) on financial instruments	**2,808**	(201)	-	**(388)**	(579)	-33%
Royalties	**(6,514)**	(2,486)	162%	**(28,433)**	(6,321)	350%
Production expenses	**(16,788)**	(4,988)	237%	**(55,901)**	(11,358)	392%
Transportation expenses	**(3,038)**	(1,005)	202%	**(10,719)**	(4,090)	162%
Operating income	**30,864**	9,863	213%	**119,250**	24,536	386%
Production (mBOE)	**1,431**	528	171%	**4,656**	1,446	222%
Operating netback ($/BOE)	**21.55**	18.67	15%	**25.62**	16.97	51%

"Production per common share" is calculated by dividing total production by the basic weighted average number of common shares outstanding, as determined in accordance with GAAP.

"Finding, development and acquisition" ("FD&A") cost is the sum of capital expenditures incurred in the period and the change in future development capital ("FDC") required to develop reserves. FD&A cost per BOE is determined by dividing current period net reserve additions into the corresponding period's FD&A cost. Readers are cautioned that the aggregate of capital expenditures incurred in the year, comprised of exploration and development costs and acquisition costs, and the change in estimated FDC generally will not reflect total FD&A costs related to reserves additions in the year.

"Recycle ratio" is a measure for evaluating the effectiveness of a company's re-investment program. The ratio measures the efficiency of capital investment by comparing the operating netback per BOE to FD&A cost per BOE.

"Net asset value per common share" is calculated by adding the present value of petroleum and natural gas reserves, undeveloped land value and proceeds from exercise of stock options, less the present value of decommissioning obligations and bank debt, net of working capital, and dividing by the diluted number of common shares outstanding. The calculation of proceeds from exercise of stock options and the diluted number of common shares outstanding only include stock options that are "in-the-money" based on the closing price of KEL common shares as at the calculation date.

OTHER MEASUREMENTS

All dollar amounts are referenced in thousands of Canadian dollars, except when noted otherwise. Where amounts are expressed on a barrel of oil equivalent ("BOE") basis, natural gas volumes have been converted to oil equivalence at six thousand cubic feet per barrel and sulphur volumes have been converted to oil equivalence at 0.6 long tons per barrel. The term BOE may be misleading, particularly if used in isolation. A BOE conversion ratio of six thousand cubic feet per barrel is based on an energy equivalency conversion method primarily applicable at the burner tip and does not represent a value equivalency at the wellhead. References to oil in this discussion include crude oil and field condensate. References to natural gas liquids ("NGLs") include, pentane, butane, propane, and ethane. References to gas in this discussion include natural gas and sulphur.

SIGNIFICANT JUDGMENTS AND ESTIMATES

The significant accounting policies used by the Company are disclosed in note 2 of the audited annual financial statements as at and for the year ended December 31, 2014. Certain accounting policies require that management make judgments regarding the selection and application of such policies, and to make appropriate decisions with respect to formulation of estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses. Actual results may differ materially from these estimates. The following discussion identifies the critical accounting policies and practices of the Company and helps assess the likelihood of materially different results being reported.

Common control transaction

In connection with the Arrangement and pursuant to the terms of the Conveyance Agreement, the Celtic Assets were transferred from Celtic to Kelt and Kelt assumed certain obligations and liabilities of Celtic. Kelt was a wholly owned subsidiary of Celtic immediately preceding closing of the Arrangement and immediately subsequent to closing, Kelt was controlled by the same shareholders as Celtic; consequently, the entities were under common control at the time the Celtic Assets were transferred. Business combinations involving entities under common control are outside the scope of IFRS 3 *Business Combinations*. IFRS provides no guidance on the accounting for these types of transactions and an entity is required to develop an accounting policy. The three most common methods utilized are the purchase method, the predecessor values since inception method, and the predecessor values from date of transaction method. A business combination involving entities under common control is a business combination in which all of the combining entities are ultimately controlled by the same party, both before and after the business combination, and control is not transitory. Management has determined the predecessor values from date of transaction method to be most appropriate. This method requires the financial statements to be prepared using the predecessor carrying values without any step up to fair value. The difference between any consideration and the aggregate carrying value of the assets and liabilities is recorded as a reserve from common control transaction in shareholders' equity.

Assets held for sale

The decision to classify a non-current asset or disposal group as held for sale requires judgment to determine if the carrying amount will be recovered through a sale transaction rather than through continuing use. In order to draw this conclusion, management must assert that the asset or disposal group is available for immediate sale in its present condition and believe that it is highly probable that a sale transaction will be completed within one year of designating the asset as held for sale. As more particularly described in note 6 of the financial statements, estimates and assumptions are also required to measure the assets held for sale at their fair value less costs of disposal.

Depletion, depreciation and reserves

The Company calculates depletion based on total proved reserves as determined in accordance with the Canadian Oil and Gas Evaluation Handbook ("COGEH"). The process of determining reserves is complex. Significant judgments are based on available geological, geophysical, engineering, and economic data. These judgments are based on estimates and assumptions that may change substantially as additional data from ongoing development activities and production performance becomes available and as economic conditions impacting oil and gas prices and costs change. The reserve estimates are based on current production forecasts, prices and economic conditions. As circumstances change and additional data becomes available, reserve estimates also change. Estimates made are reviewed and revised, either upward or downward, as warranted by the new information. Revisions are often required due to changes in well performance, prices, economic conditions and governmental restrictions.

Although every reasonable effort is made to ensure that reserve estimates are accurate, reserve estimation can be impacted by subjective decisions, new geological or production information and a changing environment. In addition, revisions to reserve estimates can arise from changes in forecast oil and gas prices and reservoir performance. Such revisions can be either positive or negative.

Changes in reserve estimates impact the financial results of the Company as reserves and estimated future development costs are used to calculate depletion. Reserves are used in measuring the fair value less costs of disposal ("FVLCD") of property, plant and equipment ("PP&E") for impairment calculations and for determining the fair value of PP&E acquired in a business combination. Reserves also impact the Company's assessment of the commercial viability and technical feasibility of an exploration project and the decision to transfer exploration and evaluation ("E&E") assets to PP&E.

Determination of Cash Generating Units ("CGUs")

The determination of CGUs requires judgment in defining a group of assets that generate cash inflows that are largely independent of the cash inflows from other assets or groups of assets. CGUs are determined by similar geological structure, shared infrastructure, geographical proximity, commodity type, similar exposure to market risks and materiality.

Impairment of non-financial assets

Significant judgment is required to assess the Company's non-financial assets, namely PP&E, E&E and goodwill, for impairment. Management must first determine whether indicators of impairment exist that suggest the carrying value may not be recoverable through the asset's continued use or sale. As a result of a significant decline in current and forecast oil and natural gas prices, an indication of potential impairment was identified and the Company was required to perform a formal impairment test and calculate the recoverable amount as at December 31, 2014.

Significant judgment and estimates are required to calculate the recoverable amount in an impairment test. Management calculated the recoverable amount of each CGU based on its FVLCD, using an after-tax discounted cash flow analysis derived from proved plus probable reserves. Reserve estimates and expected future cash flows from production of reserves are subject to measurement uncertainty as discussed above and are subject to variability due to changes in forecasted commodity prices. In addition, the present value of forecast future cash flows is highly sensitive to the discount rate. Judgment is required to determine an appropriate discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. Refer to note 8 of the financial statements for a discussion of the specific estimates and assumptions applied in the calculation of the recoverable amount. For the purpose of impairment testing, goodwill is allocated to the CGU expected to benefit from the business combination.

Exploration and evaluation assets

The decision to transfer assets from E&E to PP&E requires judgment as it is based on estimated proved reserves, which are used, in part, to determine a project's technical feasibility and commercial viability. Judgment is also required to determine the level at which E&E is assessed for impairment; for Kelt, the recoverable amount of E&E assets is assessed at the operating segment level.

Decommissioning obligations

The Company estimates the decommissioning obligations for oil and gas wells and their associated production facilities and infrastructure. In most instances, dismantling of assets and remediation occurs many years into the future. The value of the ultimate decommissioning obligation can fluctuate in response to many factors including changes to relevant legal requirements, the emergence of new restoration techniques, experience at other production sites, and changes to the risk-free discount rate. The expected timing and amount of expenditure can also change, for example, in response to changes in reserves or changes in laws and regulations or their interpretation. Judgments include the most appropriate discount rate to use, which management has determined to be a risk-free rate.

Kelt estimates abandonment and reclamation costs based on a combination of publically available industry benchmarks and internal site specific information. For producing wells and facilities, the expected timing of settlement is estimated based on the proved plus probable period to abandonment for each field, as per the independent reserve report. For non-producing wells, the expected timing of settlement is estimated to be half of the period applied to producing wells in that field, unless the timing to abandon and reclaim a specific well site or facility is known based on budgeted expenditures.

Business combinations

Business combinations are accounted for using the acquisition method of accounting. The determination of fair value often requires management to make assumptions and estimates about future events. The assumptions and estimates with respect to determining the fair value of exploration and evaluation assets and property, plant and equipment acquired generally require the most judgment and include estimates of reserves acquired, forecast benchmark commodity prices and discount rates. Assumptions are also required to determine the fair value of decommissioning obligations associated with the properties. Changes in any of these assumptions or estimates used in determining the fair value of acquired assets and liabilities could impact the amounts assigned to assets, liabilities and goodwill (or gain from a bargain purchase) in the acquisition equation. Future profit (loss) can be affected as a result of changes in future depletion and depreciation or impairment.

Deferred income taxes

The Company follows the liability method for calculating deferred income taxes. Tax interpretations, regulations and legislation in the jurisdictions in which the Company operates are subject to change. As such, deferred income taxes

are subject to measurement uncertainty. Deferred income tax assets are assessed by management at the end of the reporting period to determine the likelihood that they will be realized from future taxable earnings. Given the Company had a net deferred income tax liability as at December 31, 2014, judgment with respect to the recoverability of deferred income tax assets was not required in the current reporting period. The provision for deferred income taxes also includes the following significant judgments of management:

- Classification of intangible drilling and completion costs as Canadian exploration expenses ("CEE") or Canadian development expenses ("CDE") – CEE is deductible at a rate of 100% per year, whereas CDE may be deducted on a declining basis at 30% per year. Accordingly, the allocation of resource deductions will impact the period in which Kelt may become taxable in the future. In addition, the designation of certain expenditures as CEE and/or CDE impacts the Company's ability to satisfy its flow-through share obligations; and
- Recognition of unrecognized deferred income tax asset – per IAS 12, deferred income taxes are not initially recognized on transactions that are not business combinations. The unrecognized deferred income tax asset that arose on the Common Control Transaction is being amortized based on the corporate weighted average depletion factor for the period.

Share based compensation

The Company uses the fair value method of accounting for its long-term incentive plans, which include an Incentive Stock Option Plan and a Restricted Share Unit Plan. Judgments include which valuation model is most appropriate for the grant of the award to estimate its fair value. Estimates and assumptions are then used in the valuation model to determine fair value.

For stock options, the Company uses the Black-Scholes option pricing model which requires that management make assumptions for the expected life of the option, the anticipated volatility of the share price over the life of the option, the risk-free interest rate for the life of the option, and the number of options that will ultimately vest. The assumptions used by the Company are discussed in note 12 of the financial statements.

The fair value of restricted share units is estimated based on the volume weighted average trading price on the TSX over three trading days immediately prior to the date of grant. Judgment is also required to estimate the number of restricted share units that will ultimately vest. The assumptions used by the Company are discussed in note 12 of the financial statements.

Flow-through shares

There is no IFRS guidance that specifically addresses accounting for flow-through shares, therefore the Company is required to develop an accounting policy. The two most common methods are the residual method and the relative fair value method. The Company has applied the residual method to appropriately reflect the substance transaction. Under the residual method, the proceeds from the issuance are allocated between i) the proceeds of the offering of shares, and ii) the renunciation of tax deductions. At the time the flow-through shares are issued: i) shareholders' capital is credited based on the fair value of ordinary common shares, and ii) the tax deductions to be renounced are deferred and presented as a liability in the Statement of Financial Position, at an amount equal to the residual difference between the fair value of the Company's ordinary common shares relative to the amount the investor pays for the flow-through shares.

Determination of the fair value of ordinary shares requires judgment. Typically, it is based on the share price at the time the parties agree to the transaction, which is generally at a date earlier than closing. If there are significant changes in the share price between the date the parties agree to the offering and closing, additional judgment may be required.

Judgment is also required to determine when the Company has fulfilled its obligation to pass on the tax deduction to investors, at which time, the premium on flow-through shares is recognized in income. The Company deems the obligation to have been fulfilled in the period that eligible expenditures are incurred, regardless of the period in which the tax deductions are legally renounced. This is based on the view that the renunciation is perfunctory and that the accounting should be reflected when the expenditure is made.

DISCLOSURE CONTROLS AND PROCEDURES

The Chief Executive Officer ("CEO") and the Chief Financial Officer ("CFO") have designed, or caused to be designed under their supervision, disclosure controls and procedures as defined in National Instrument 52-109 of the Canadian Securities Administrators, to provide reasonable assurance that: (i) material information relating to the Company is made known to the CEO and the CFO by others, particularly during the period in which the annual and interim filings are being prepared; and (ii) information required to be disclosed by the Company in its annual filings, interim filings or other reports filed or submitted by it under securities legislation is recorded, processed, summarized and reported within the time periods specified in securities legislation.

The CEO and the CFO have evaluated the effectiveness of Kelt's disclosure controls and procedures as at December 31, 2014 and have concluded that such disclosure controls and procedures are effective. The assessment was based on the framework in Internal Control – Integrated Framework (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission.

INTERNAL CONTROLS OVER FINANCIAL REPORTING

The CEO and the CFO have designed, or caused to be designed under their supervision, internal controls over financial reporting as defined in National Instrument 52-109 of the Canadian Securities Administrators, in order to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with IFRS.

There were no material changes to the Company's internal controls over financial reporting during the interim period from October 1, 2014 to December 31, 2014. The CEO and the CFO have evaluated the effectiveness of Kelt's internal controls over financial reporting as at December 31, 2014 and have concluded that such internal controls over financial reporting are effective. The assessment was based on the framework in Internal Control – Integrated Framework (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission.

Due to its inherent limitations, internal controls over financial reporting may not prevent or detect misstatements. In addition, projections of any evaluation relating to the effectiveness in future periods are subject to the risk that controls may become inadequate as a result of changes in conditions, or that the degree of compliance with policies and procedures may deteriorate.

GROWTH STRATEGY

The business plan of Kelt is to create sustainable and profitable growth as a participant in the oil and gas industry in Canada. Kelt seeks to identify and acquire strategic oil and gas properties where it believes further exploitation, development and exploration opportunities exist. From time to time, Kelt may acquire a corporate entity in order to accomplish its oil and gas property acquisition strategy. In addition, Kelt has implemented a full cycle exploration program, resulting in exploration and development drilling based on opportunities generated internally.

Kelt is optimistic about its future prospects. The Company is opportunity driven and is confident that it can grow its production base by building on its current inventory of development projects and by adding new exploration prospects. Kelt will endeavor to maintain a high quality product stream that on a historical basis receives a superior price with reasonably low production and transportation costs. In addition, the Company will focus its exploration efforts in areas of multi-zone hydrocarbon potential, primarily in west central Alberta and northeastern British Columbia. Kelt will continue to seek optimization of its asset base by building on its core properties and monetizing non-core assets.

RESULTS OF OPERATIONS

FINANCIAL AND OPERATING HIGHLIGHTS

- During the fourth quarter of 2014, the Company achieved record production of 15,559 BOE per day, up 171% from 5,739 BOE per day in the same quarter 2013 and up 12% from 13,872 BOE per day during the third quarter of 2014. Production for the year ended December 31, 2014, averaged 12,756 BOE per day, an increase of 222% compared to average production of 3,961 BOE per day during the previous year ended December 31, 2013;
- The Company generated funds from operations in the amount of $29.7 million ($0.23 per common share, basic and diluted) during the fourth quarter of 2014, up 216% from $9.4 million ($0.09 per common share, basic and

diluted) in the same quarter of 2013. During the year ended December 31, 2014, the Company generated funds from operations of $115.5 million ($0.95 per common share, basic and $0.93 per common share, diluted) compared to $23.7 million ($0.32 per common share, basic and diluted) during the previous year ended December 31, 2013. This equates to an absolute increase of 388% year over year, or a 191% increase in funds from operations per common share, diluted;

- During the fourth quarter of 2014, corporate royalty rates averaged 12.0% of revenue; production and transportation expense, combined, averaged $13.86 per BOE; and G&A expense averaged $0.54 per BOE. On an annual basis, corporate royalty rates averaged 13.2% of revenue; production and transportation expense, combined, averaged $14.30 per BOE; and G&A expense averaged $0.78 per BOE in 2014;
- During 2014, the Company raised gross proceeds of $149.0 million through private placement equity offerings, by issuing a total of 12.6 million common shares (of which, 2.8 million common shares were issued on a "flow-through" basis) at an average issue price of $11.83 per common share. Certain officers, directors and employees of the Company purchased 1.1 million of the 12.6 million common shares issued during the year. As at December 31, 2014, insiders owned or controlled 24.6 million common shares, or 19.4% of the total shares outstanding;
- The Company's total capital expenditures amounted to $423.9 million in 2014, up 29% from $329.1 million in 2013. Of this total, $188.6 million was spent drilling and completing wells, $46.1 million was spent on infrastructure, $16.5 million was spent on land to expand the Company's inventory of drilling prospects, and $172.7 million was spent on acquisitions, net of proceeds from dispositions. The Company's exploration and development capital program was back weighted to the second half of 2014 and capital expenditures during the fourth quarter were $99.5 million;
- Kelt drilled 36 (27.1 net working interest) wells during 2014 resulting in 15 (9.9 net) gas wells, 20 (16.2 net) oil wells and 1 (1.0 net) service well, for an overall success rate of 100%. Of the wells drilled in the year, 9 (5.4 net) were drilled during the fourth quarter;
- On July 2, 2014, the Company completed the acquisition of Capio Exploration Ltd. ("Capio"), a private Canadian oil and gas company, which held crude oil and natural gas assets located at Valhalla/La Glace, adjacent to the Kelt's core producing areas at Pouce Coupe/Spirit River in west central Alberta. The consideration paid by Kelt, after closing adjustments, consisted of $72.1 million in cash and the issuance of 4.3 million common shares. In addition, Kelt assumed Capio's working capital deficit of $37.4 million which included $32.5 million of bank indebtedness that was repaid by Kelt at closing;
- On December 18, 2014, the Company acquired petroleum and natural gas assets located at Stoddart, British Columbia, for cash consideration of approximately $10.4 million. The assets acquired are adjacent to the Company's core producing area at Inga/Fireweed in northeastern British Columbia and include a significant infrastructure component which is expected to reduce production and transportation expenses and improve liquids recoveries at Inga;
- The Company reported significant growth in reserves as at December 31, 2014:
    - Proved developed producing reserves increased 47% to 26.8 million BOE;
    - Total proved reserves increased 73% to 61.1 million BOE; and
    - Total proved plus probable reserves increased 67% to 99.1 million BOE;
- Compared to the previous year, the Company's reserve volumes weighting to oil and NGLs increased. At December 31, 2014, the weighting of proved plus probable reserves was 24% oil, 11% NGLs and 65% gas (2013 – 20% oil, 8% NGLs and 72% gas);
- Reported finding, development and acquisition costs, including future development capital expenditures, of $13.42 per BOE (2013 – $13.23 per BOE) resulting in a recycle ratio of 1.9 times based on proved plus probable reserves (2013 – 1.3 times);
- Reported net asset value at December 31, 2014 of $8.20 per common share, up 46% from $5.61 per common share per common share at December 31, 2013; and
- As at December 31, 2014, bank debt, net of working capital was $104.4 million. The Company has $235.0 million revolving credit facility, providing the Company with sufficient financial flexibility to fund ongoing operations and to execute its 2015 capital expenditure program.

REVENUE

	Three months ended December 31			Year ended December 31		
(CA$ thousands, except as otherwise indicated)	**2014**	2013	%	**2014**	2013	%
Average daily production:						
Oil (bbls/d)	**4,691**	809	480%	**3,413**	516	561%
NGLs (bbls/d)	**1,037**	487	113%	**924**	297	211%
Gas (mcf/d)	**58,984**	26,660	121%	**50,516**	18,888	167%
Combined (BOE/d)	**15,559**	5,739	171%	**12,756**	3,961	222%
Average realized prices, before financial instruments:						
Oil ($/bbl)	**68.16**	84.02	-19%	**85.91**	88.62	-3%
NGLs ($/bbl)	**44.98**	57.00	-21%	**59.47**	52.76	13%
Gas ($/mcf)	**3.81**	3.97	-4%	**4.75**	3.51	35%
Combined ($/BOE)	**38.00**	35.12	8%	**46.11**	32.27	43%
Average realized prices, after financial instruments:						
Oil ($/bbl)	**74.11**	81.35	-9%	**85.53**	86.77	-1%
NGLs ($/bbl)	**47.48**	57.00	-17%	**59.73**	52.76	13%
Gas ($/mcf)	**3.81**	3.97	-4%	**4.75**	3.51	35%
Combined ($/BOE)	**39.96**	34.74	15%	**46.03**	32.03	44%
Revenue, before royalties and financial instruments:						
Oil	**29,414**	6,252	370%	**107,020**	16,687	541%
NGLs	**4,293**	2,554	68%	**20,062**	5,721	251%
Gas	**20,689**	9,737	112%	**87,609**	24,248	261%
Total revenue, before royalties and financial instruments	**54,396**	18,543	193%	**214,691**	46,656	360%

The Company commenced active operations on February 27, 2013 following the completion of the Arrangement and conveyance of the Celtic Assets from Celtic to Kelt on February 26, 2013, at which time, production from the Celtic assets was approximately 3,500 BOE per day. Since commencing active operations, Kelt has increased production by 345% to an average of 15,559 BOE per day during the fourth quarter of 2014, through a combination of strategic acquisitions and an active drilling program, as outlined further below:

- On December 18, 2014, the Company acquired petroleum and natural gas assets located at Stoddart, British Columbia. At the time of the acquisition, production from the acquired assets was approximately 450 BOE per day.
- On July 2, 2014, the Company completed a corporate acquisition of a private company with the majority of crude oil and natural gas assets located at Valhalla/La Glace in west central Alberta. Production from these assets was approximately 2,300 BOE per day at the time of the acquisition.
- On December 20, 2013, the Company completed a property acquisition in the Pouce Coupe/Spirit River area of west central Alberta. The acquired assets contributed to daily average production of approximately 4,800 BOE per day at the time of the acquisition. Approximately 210 BOE per day of the acquired non-core oil production was subsequently disposed on February 10, 2014, but was offset by approximately 250 BOE per day of oil and gas production from a minor property acquisition in the Spirit River area which was completed on March 7, 2014.
- On August 9, 2013, the Company acquired petroleum and natural gas assets at Fireweed, British Columbia. Production on the acquisition date was approximately 600 BOE per day.
- The Company also has an active drilling program in its core areas at Inga/Fireweed, Karr, La Glace and Pouce Coupe/Spirit River. In 2014, Kelt drilled 15 (9.9 net) gas wells and 20 (16.2 net) oil wells. The remaining increase in daily average production is a result of incremental production from new wells drilled that more than offset corporate production declines.

During the three month period ended December 31, 2014, the Company earned revenue before royalties and financial instruments of $54.4 million, an increase of 193% compared to $18.5 million in the same quarter of the previous year. The increase in sales revenue is a result of higher production volumes combined with an increase in the proportion of oil and NGLs production. Specifically, oil and NGLs accounted for 37% of total production during the fourth quarter of 2014 compared to 22% during the fourth quarter of 2013. As a result, although realized prices for each product type decreased in the current quarter, the Company's combined average sales price increased 8% to $38.00 per BOE ($39.96 after financial instruments) from $35.12 per BOE ($34.74 after financial instruments) during the fourth quarter of 2013.

During the year ended December 31, 2014, revenue before royalties and financial instruments increased by 360% to $214.7 million compared to $46.7 million during the previous year ended December 31, 2013. The increase in sales revenue is primarily due to higher production volumes combined with a significant increase in natural gas prices and appreciation of the US dollar. The Company realized a combined average sales price of $46.11 per BOE ($46.03 after financial instruments) during 2014, a 43% increase from $32.27 per BOE ($32.03 after financial instruments) during the previous year. The increase in the combined average realized sales price is also due to an increase in the proportion of oil and NGLs production. Oil and NGLs accounted for 34% of total production in 2014 compared to 20% in 2013.

BENCHMARK COMMODITY PRICES

The following table summarizes average historical benchmark commodity prices for the periods indicated, which represent the periods over which Kelt had active operations:

	Q4 2014	Q4 2013	% change	**YTD 2014**	Mar-Dec[6] 2013	% change
WTI Cushing Oklahoma (US$/bbl)[1]	**73.15**	97.46	-25%	**92.99**	98.60	-6%
Average FX rate (CA$/US$)[1]	**1.1361**	1.0495	8%	**1.1045**	1.0357	7%
WTI Cushing Oklahoma (CA$/bbl)[2]	**82.97**	102.29	-19%	**102.49**	102.16	0%
Canadian Light Sweet (CA$/bbl)[1][3]	**75.11**	86.26	-13%	**94.18**	94.26	0%
As a % of CA$ WTI	**91%**	84%	7%	**92%**	92%	0%
Edmonton Pentane (CA$/bbl)[1]	**80.11**	98.77	-19%	**102.33**	103.97	-2%
As a % of CA$ WTI	**97%**	97%	0%	**100%**	102%	-2%
Edmonton Butane (CA$/bbl)[1]	**62.67**	70.40	-11%	**68.02**	70.13	-3%
As a % of CA$ WTI	**76%**	69%	10%	**66%**	69%	-3%
Edmonton Propane (CA$/bbl)[1]	**27.16**	57.65	-53%	**44.42**	40.58	9%
As a % of CA$ WTI	**33%**	56%	-42%	**43%**	40%	8%
NYMEX Henry Hub (US$/mmbtu)[4]	**3.94**	3.63	9%	**4.37**	3.73	17%
AECO 5A (CA$/GJ)[5]	**3.41**	3.35	2%	**4.27**	3.03	41%

(1) Source: Sproule Associates Limited

(2) Source: Sproule Associates Limited, Canadian dollar equivalent price WTI price is calculated based on monthly average US$WTI price and the monthly average CA$/US$ exchange rate

(3) The Edmonton Light Par price was discontinued as of May 1, 2014, and replaced by the Canadian Light Sweet crude blend which is traded daily on the Net Energy Index. Historical information is not available for the Canadian Light Sweet index for 2013.

(4) Source: Canadian Gas Price Reporter (Henry Hub 3-Day Average Close)

(5) Source: Canadian Gas Price Reporter (NGX AB-NIT Same Day Index 5A)

(6) Represents period over which Kelt had active operations following completion of the Arrangement

OIL OPERATIONS

	Three months ended December 31			Year ended December 31		
(CA$/bbl)	**2014**	2013	%	**2014**	2013	%
Oil sales	**68.16**	84.02	-19%	**85.91**	88.62	-3%
Cash premium on financial instruments	**-**	-	-	**-**	1.21	-100%
Realized gain (loss) on financial instruments	**5.95**	(2.67)	-	**(0.38)**	(3.06)	-88%
Average realized price, after financial instruments	**74.11**	81.35	-9%	**85.53**	86.77	-1%
Royalties	**(11.77)**	(20.63)	-43%	**(15.67)**	(19.92)	-21%
Production and transportation expense	**(16.36)**	(12.87)	27%	**(16.41)**	(14.63)	12%
Operating netback	**45.98**	47.85	-4%	**53.45**	52.22	2%

During the fourth quarter of 2014, the Company realized an average price for oil sales of $68.16 per barrel ($74.11 after financial instruments), a decrease of 19% compared to the same quarter of the previous year. By comparison, the WTI index oil price decreased 25% from US$97.46 per barrel in the fourth quarter of 2013 to US$73.15 per barrel in the fourth quarter of 2014. Appreciation of the US dollar during 2014 softened the impact of falling oil prices on the average oil price realized by the Company in Canadian dollars.

The Company realized an average price of $85.91 per barrel ($85.53 after financial instruments) for oil sales during the year ended December 31, 2014, a decrease of 3% compared to the previous year ended December 31, 2013. By comparison, the WTI index oil price decreased 6% from US$98.60 per barrel in 2013 to US$92.99 per barrel in 2014. Appreciation of the US dollar during 2014 softened the impact of falling oil prices on the average oil price realized by the Company in Canadian dollars. The average price realized by the Company for oil sales in 2014 reflects a discount of 16.8% relative to the Canadian dollar equivalent WTI price, compared to a discount of 13.2% in the previous year. The widening of the discount is primarily due to new oil production added at Valhalla/La Glace which has a higher sour content compared to the Company's other oil production.

Oil royalties averaged 17.3% and 18.2%, respectively, during the quarter and year ended December 31, 2014. During the corresponding periods of the previous year, oil royalties averaged 24.6% and 22.5%. The decrease in the Company's average oil royalty rate compared to the previous year is primarily due to oil production from new drills which qualify for a minimum 5% royalty pursuant to various Alberta royalty incentive programs.

Oil production and transportation expenses, combined, averaged $16.36 per barrel and $16.41 per barrel during the quarter and year ended December 31, 2014, respectively. The increase in per unit costs compared to the same periods of the previous year is due to acquired properties that carry higher costs than Kelt's historical average.

NGL OPERATIONS

	Three months ended December 31			Year ended December 31		
(CA$/bbl)	**2014**	2013	%	**2014**	2013	%
NGLs sales	**44.98**	57.00	-21%	**59.47**	52.76	13%
Realized gain on financial instruments	**2.50**	-	-	**0.26**	-	-
Average realized price, after financial instruments	**47.48**	57.00	-17%	**59.73**	52.76	13%
Royalties	**(4.79)**	(9.14)	-48%	**(8.04)**	(8.40)	-4%
Production and transportation expense	**(12.10)**	(11.59)	4%	**(12.05)**	(12.17)	-1%
Operating netback	**30.59**	36.27	-16%	**39.64**	32.19	23%

During the fourth quarter of 2014, the Company realized an average price for NGL sales of $44.98 per barrel ($47.48 after financial instruments), a decrease of 21% compared to an average price of $57.00 per barrel during the fourth quarter of 2013. The decrease in the Company's realized price is due a decline market prices for all NGL products, most notably propane prices which fell 53% quarter over quarter. The impact of the decrease in propane prices was partially mitigated by a financial derivative contract which fixed the price of OPIS-Conway propane at US$48.09 per barrel on 150 barrels per day.

The Company realized an average price of $59.47 per barrel ($59.73 after financial instruments) for NGL sales during the year ended December 31, 2014, an increase of 13% compared to the previous year ended December 31, 2013. Although market prices for NGLs were relatively flat year over year, the Company's average realized price increased due to a higher weighting of pentane and butane sales. During 2014, pentane and butane sales represented 65% of the Company's total NGL sales volumes compared to 55% in the previous year.

NGL royalties averaged 10.6% and 13.5%, respectively, during the quarter and year ended December 31, 2014. During the corresponding periods of the previous year, NGL royalties averaged 16.0% and 15.9%. The decrease in average NGL royalties is a result of production from new drills which qualify for a minimum 5% royalty pursuant to various Alberta and BC royalty incentive programs, as well as gas cost allowance credits allocated to NGLs production, which do not fluctuate with NGL prices.

Per unit production and transportation expenses for NGLs were relatively flat compared to the corresponding periods of the previous year.

GAS OPERATIONS

	Three months ended December 31			Year ended December 31		
(CA$/mcf)	**2014**	2013	%	**2014**	2013	%
Gas sales	**3.81**	3.97	-4%	**4.75**	3.51	35%
Royalties	**(0.18)**	(0.22)	-18%	**(0.34)**	(0.24)	42%
Production and transportation expense	**(2.14)**	(1.84)	16%	**(2.28)**	(1.65)	38%
Operating netback	**1.49**	1.91	-22%	**2.13**	1.62	31%
Barrel of oil equivalent netback ($/BOE)	**8.94**	11.46	-22%	**12.78**	9.72	31%

During the three month period ended December 31, 2014, the Company realized an average price of $3.81 per MCF for gas sales, a decrease of 4% compared to $3.97 per MCF during same three month period of the previous year. By comparison, the AECO 5A index gas price increased 2% from $3.35 per MCF in the fourth quarter of 2013 to $3.41 per MCF in the fourth quarter of 2014. The Company's realized price for gas sales was impacted by pipeline capacity constraints during November and December 2014, which resulted in a reduction of net revenue paid by the purchasers of the Company's natural gas, as higher third party pipeline tariffs were passed on to Kelt.

The Company realized an average price of $4.75 per MCF for gas sales during the year ended December 31, 2014, an increase of 35% compared to the previous year ended December 31, 2013. The AECO 5A gas index price averaged $4.27 per MCF during 2014. The average gas price realized by the Company includes a heating value premium, earned primarily from gas produced at Inga/Fireweed in northeastern British Columbia.

Gas royalties averaged 4.7% and 7.1%, respectively, during the quarter and year ended December 31, 2014. During the corresponding periods of the previous year, gas royalties averaged 5.5% and 6.8%. The decrease in the average gas royalty rate during the fourth quarter of 2014 is a result of production from new drills which qualify for a minimum 5% royalty pursuant to various royalty incentive programs in Alberta and BC, as well as gas cost allowance credits which do not fluctuate with gas prices. The increase in gas royalties on an annual basis is due to higher natural gas prices.

Per unit production and transportation expenses, combined, averaged $2.14 per MCF and $2.28 per MCF during the quarter and year ended December 31, 2014, respectively. The increase in per unit costs compared to the corresponding periods of the previous year is primarily due to gas production from acquired properties that carry higher costs than Kelt's historical average.

FINANCING EXPENSES

	Three months ended December 31			Year ended December 31		
(CA$ thousands, unless otherwise indicated)	**2014**	2013	%	**2014**	2013	%
Interest and fees on bank debt	**426**	31	1274%	**820**	82	900%
Accretion of decommissioning obligations	**469**	96	389%	**1,701**	247	589%
Financing expense	**895**	127	605%	**2,521**	329	666%
Average bank debt outstanding	**11,635**	-	-	**2,933**	-	-
Average interest rate on indebtedness	**4.0%**	-	-	**4.0%**	-	-
Interest and fees on bank debt ($/BOE)	**0.30**	0.06	400%	**0.18**	0.06	200%

The Company has a $235.0 million committed term credit facility (the "Credit Facility"). The Company did not begin drawing on the Credit Facility until the fourth quarter of 2014 resulting in interest expense in the current quarter. Fees on bank debt include commitment fees and standby charges on the undrawn facility. Commitment fees and standby charges increased in 2014 as a result of an increase in the authorized borrowing amount (previously $100.0 million).

Accretion expense is a measure of the increase in the present value of the decommissioning obligation due to the passage of time. The increase in accretion expense is due to a significant increase in the carrying value of decommissioning obligations resulting from acquisitions and drilling activity.

GENERAL AND ADMINISTRATIVE ("G&A") EXPENSES

The following table summarizes significant components of the Company's G&A expenses:

	Three months ended December 31			Year ended December 31		
(CA$ thousands, unless otherwise indicated)	**2014**	2013	%	**2014**	2013	%
Salaries and benefits	**1,513**	408	271%	**4,360**	1,254	248%
Other G&A expenses	**901**	602	50%	**3,052**	1,365	124%
Gross G&A expenses	**2,414**	1,010	139%	**7,412**	2,619	183%
Recovery pursuant to the Arrangement	**-**	(1)	-100%	**-**	(133)	-100%
Overhead recoveries	**(1,636)**	(352)	365%	**(3,781)**	(826)	358%
Total G&A expenses, net of recoveries	**778**	657	18%	**3,631**	1,660	119%
Net G&A ($ per BOE)	**0.54**	1.24	-56%	**0.78**	1.15	-32%

In conjunction with the Company's significant growth, Kelt hired several new employees resulting in an increase in salaries, benefits and other overhead costs, including the cost of additional office space to accommodate new staff. The impact of the increase in gross G&A expenses is partially offset by higher overhead recoveries primarily due to higher capital spending (excluding acquisitions) on operated assets in the current year.

On a per unit basis, net G&A expenses decreased by 56% to $0.54 per BOE during the fourth quarter of 2014 and decreased by 32% to $0.78 per BOE for the year ended December 31, 2014, compared to the corresponding periods of the previous year. The decrease in per unit G&A expenses reflects the significant increase in production period over period and the Company's continued efforts to maintain a low cost structure.

SHARE BASED COMPENSATION

	Three months ended December 31			Year ended December 31		
(CA$ thousands, unless otherwise indicated)	**2014**	2013	%	**2014**	2013	%
Stock options	**1,181**	824	43%	**4,116**	2,593	59%
Restricted share units ("RSUs")	**1,345**	1,011	33%	**4,917**	3,186	54%
Total share based compensation expense	**2,526**	1,835	38%	**9,033**	5,779	56%
$ per BOE	**1.76**	3.48	-49%	**1.94**	4.00	-52%

The increase in share based compensation expenses in 2014 reflects the amortization of expense related to additional stock options and RSUs granted in the year. The decrease in per unit costs reflects the significant increase in production period over period which more than offset the increase in expenses.

DEPLETION AND DEPRECIATION

	Three months ended December 31			Year ended December 31		
(CA$ thousands, unless otherwise indicated)	**2014**	2013	%	**2014**	2013	%
Depletion of development and production assets	**26,148**	8,216	218%	**84,006**	23,232	262%
Depreciation of corporate assets	**152**	55	176%	**412**	105	292%
Total depletion and depreciation	**26,300**	8,271	218%	**84,418**	23,337	262%
$ per BOE	**18.37**	15.66	17%	**18.13**	16.14	12%

The Company calculates depletion of development and production assets based on production relative to total proved reserves, for each property. The increase in the absolute level of depletion expense is due to an increase in the carrying value of assets subject to depletion, resulting from capital expenditures and acquisitions. The increase in depletion and depreciation expenses per unit of production reflects the addition of proved reserves at higher than historical capital costs, primarily due to the acquisition of oil weighted assets that received higher operating netbacks than gas weighted assets in 2014.

EXPLORATION AND EVALUATION

	Three months ended December 31			Year ended December 31		
(CA$ thousands, unless otherwise indicated)	**2014**	2013	%	**2014**	2013	%
Expired mineral leases	**129**	-	-	**377**	114	231%
$ per BOE	**0.09**	-	-	**0.08**	0.08	0%

During the quarter and year ended December 31, 2014, the Company recognized $0.1 million and $0.4 million, respectively, of costs related to the expiry of non-core land holdings.

OTHER INCOME AND EXPENSES

Interest income

	Three months ended December 31			Year ended December 31		
(CA$ thousands, unless otherwise indicated)	**2014**	2013	%	**2014**	2013	%
Interest income	**8**	454	-98%	**938**	1,095	-14%
$ per BOE	**0.01**	0.86	-99%	**0.20**	0.76	-74%

The Company earns interest on cash held on deposit with a Canadian chartered bank. Interest income decreased in the current year due to a lower average cash balance, as the majority of the Company's cash on hand was used to partially fund the acquisition of Capio on July 2, 2014.

Transaction costs

	Three months ended December 31			Year ended December 31		
(CA$ thousands, unless otherwise indicated)	**2014**	2013	%	**2014**	2013	%
Transaction costs	**4**	233	-98%	**234**	233	0%
$ per BOE	**0.00**	0.44	-100%	**0.05**	0.16	-69%

In accordance with IFRS 3, transactions costs incurred pursuant to acquisitions are recognized as an expense. Transaction costs of approximately $0.2 million incurred during 2014 relate primarily to the acquisition of Capio.

Premium on flow-through shares

On December 18, 2014, the Company issued 0.182 million flow-through shares at a price of $11.00 per flow-through share. The implied premium on the flow-through shares was determined to be $0.7 million or $3.80 per flow-through share. As of December 31, 2014, the Company had not incurred any qualifying expenditures, leaving $2.0 million of Canadian exploration expenses to be incurred in 2015. Accordingly, the deferred premium is presented as a current liability in the Statement of Financial Position as at December 31, 2014, and will be recognized as income when the qualifying expenditures are incurred in 2015.

On March 25, 2014, the Company issued 2.635 million flow-through shares at a price of $12.75 per flow-through share. The implied premium on the flow-through shares was determined to be $3.0 million or $1.15 per flow-through share, in context of Kelt's concurrent private placement of common shares which was completed at a price of $11.60 per ordinary common share. As of December 31, 2014, the Company had incurred the full commitment of $33.6 million of qualifying Canadian development expenses and the deferred premium of $3.0 million was recognized as income in 2014.

On August 27, 2013, the Company issued 2.0 million flow-through shares at a price of $9.80 per flow-through share. The implied premium on the flow-through shares was determined to be $3.6 million or $1.80 per flow-through share, in context of Kelt's concurrent private placement of common shares which was completed at a price of $8.00 per ordinary common share. During the previous year ended December 31, 2013, the Company incurred $13.2 million of qualifying expenditures and the deferred premium was drawn down proportionately by $2.4 million. As of February 28, 2014, the Company had incurred the full commitment of $19.6 million of qualifying Canadian exploration expenses and the remaining deferred premium of $1.2 million in respect of the August 27, 2013 flow-through share financing was recognized as income in the first quarter of 2014.

Gains and losses on derivative financial instruments

The table below summarizes realized and unrealized gains (losses) on risk management contracts:

	Three months ended December 31			Year ended December 31		
(CA$ thousands, unless otherwise indicated)	**2014**	2013	%	**2014**	2013	%
Realized gain (loss)	**2,808**	(201)	-	**(388)**	(579)	-33%
Unrealized gain (loss)	**1,655**	(277)	-	**2,277**	(304)	-
Gain (loss) on derivative financial instruments	**4,463**	(478)	-	**1,889**	(883)	-
$ per BOE	**3.12**	(0.91)	-	**0.41**	(0.61)	-

During the year ended December 31, 2014, the Company had risk management contracts in place that fixed the price of crude oil at an average price of WTI CA$101.50 per barrel on approximately 1,500 barrels of oil per day. The Canadian dollar equivalent WTI price averaged $102.49 during 2014, resulting in a cumulative realized loss for the year of $0.5 million. The significant decrease in oil prices during the fourth quarter of 2014 contributed to a realized gain of approximately $2.6 million on these contracts in the current quarter.

In addition, the Company had a financial derivative contract which fixed the price of OPIS-Conway propane at US$48.09 per barrel on 150 barrels per day throughout 2014. The contract resulted in a realized gain of $0.2 million for the quarter and a cumulative realized gain of $0.1 million for the year ended December 31, 2014.

Fair value accounting for derivative financial instruments may cause significant fluctuations in the reported amounts of derivative financial instrument assets and liabilities as at the Statement of Financial Position date and the resultant magnitude of unrealized gains and losses. Additional information with respect to the Company's risk management contracts that give rise to gains or losses on financial instruments is provided under the heading of *Derivative Financial Instruments*.

INCOME TAXES

The Company recognized deferred tax expense of $0.6 million during the fourth quarter of 2014, compared to $3.2 million in the same quarter of 2013. For the year ended December 31, 2014, the Company reported deferred tax expense of $15.8 million compared to $1.2 million in previous year. An analysis of the provision for deferred income taxes is included in note 13 of the financial statements. Deferred tax expense reported differs from the expected expense (recovery) of income taxes calculated based on the statutory tax rate due to non-deductible share based compensation expense, recognition of the unrecognized deferred income tax asset resulting from the Common Control Transaction, and the impact of flow-through shares. Pursuant to the Company's flow-through share obligations, Kelt renounced tax pools in the amount $40.0 million during the year ended December 31, 2014. During the previous year ended December 31, 2013, the Company renounced $13.2 million of tax pools to the subscribers of flow-through shares.

Deferred income tax recoveries in the amounts of $1.6 million and $3.1 million were charged directly to equity in respect of share issue costs incurred in 2014 and 2013, respectively.

Kelt was not required to pay income taxes in the current or prior year as the Company had sufficient income tax deductions available to shelter taxable income. Tax deductions available as of December 31, 2014 are estimated to be approximately $599.8 million, up 34% from $447.0 million as at December 31, 2013.

(CA$ thousands, unless otherwise indicated)	Rate	**2014**	2013	change
Canadian oil and gas property expenses (COGPE)	10%	**250,377**	259,625	-4%
Canadian development expenses (CDE)	30%	**106,719**	33,339	220%
Canadian exploration expenses (CEE)	100%	**45,043**	18,399	145%
Undepreciated capital cost[(1)] (UCC)	25%	**135,929**	98,424	38%
Share and debt issue costs (SIC/ DIC)	5 years	**13,353**	10,575	26%
Non-capital losses[(2)] (NCL)	100%	**48,353**	26,630	82%
Estimated tax deductions available, end of year		**599,774**	446,992	34%

(1) The majority of the Company's undepreciated capital cost deductions relate to Class 41 assets, which are deductible at a rate of 25% per year.

(2) The Company's non-capital losses will expire in 15-20 years.

PROFIT (LOSS) AND COMPREHENSIVE INCOME (LOSS)

	Three months ended December 31			Year ended December 31		
(CA$ thousands, unless otherwise indicated)	**2014**	2013	%	**2014**	2013	%
Profit (loss) and comprehensive income (loss)	**1,256**	(1,838)	-	**10,628**	(5,115)	-
Weighted avg. shares outstanding, basic (000's)	**126,760**	99,244	28%	**121,779**	74,554	63%
Weighted avg. shares outstanding, diluted (000's)	**128,512**	99,244	29%	**124,296**	74,554	67%
$ per common share, basic	**0.01**	(0.02)	-	**0.09**	(0.07)	-
$ per common share, diluted	**0.01**	(0.02)	-	**0.09**	(0.07)	-
$ per BOE	**0.88**	(3.48)	-	**2.28**	(3.54)	-

The increase in profit during the current year is primarily due to a significant increase in production coupled with strong commodity prices. In addition, the integration of strategic acquisitions at Valhalla/La Glace and Pouce Coupe/Spirit River contributed to a higher average operating netback as the assets are more oil weighted. Profit (loss) reported by the Company, as determined in accordance with GAAP, includes the provision for significant non-cash items such as deferred income tax, depletion and depreciation, and share based compensation expense.

FUNDS FROM OPERATIONS

	Three months ended December 31			Year ended December 31		
(CA$ thousands, unless otherwise indicated)	**2014**	2013	%	**2014**	2013	%
Funds from operations[(1)]	**29,664**	9,396	216%	**115,503**	23,656	388%
Weighted avg. shares outstanding, basic (000's)	**126,760**	99,244	28%	**121,779**	74,554	63%
Weighted avg. shares outstanding, diluted (000's)	**128,512**	100,242	28%	**124,296**	75,093	66%
$ per common share, basic[(2)]	**0.23**	0.09	156%	**0.95**	0.32	197%
$ per common share, diluted[(2)]	**0.23**	0.09	156%	**0.93**	0.32	191%
$ per BOE	**20.72**	17.80	16%	**24.81**	16.36	52%

(1) Funds from operations is a non-GAAP measure which is calculated as cash provided by operating activities, before settlement of decommissioning obligations and change in non-cash operating working capital.

(2) Funds from operations per common share is calculated on a consistent basis with profit (loss) per common share, using basic and diluted weighted average common shares as determined in accordance with GAAP.

The Company generated funds from operations in the amount of $29.7 million ($0.23 per common share, basic and diluted) during the fourth quarter of 2014, up 216% from $9.4 million ($0.09 per common share, basic and diluted) in the same quarter of the previous year. During the year ended December 31, 2014, the Company generated funds from operations of $115.5 million ($0.95 per common share, basic and $0.93 per common share, diluted) compared to $23.7 million ($0.32 per common share, basic and diluted) during the previous year ended December 31, 2013. This equates to an absolute increase of 388% year over year, or a 191% increase in funds from operations per common share, diluted. The increase in funds from operations year over year is primarily due to increased production, an increase in natural gas prices and the addition of new higher netback oil production at Karr, La Glace and Pouce Coupe/Spirit River. The previous year only includes 308 days of active operations following completion of the Arrangement on February 26, 2013.

INVESTMENT AND INVESTMENT EFFICIENCIES

CAPITAL EXPENDITURES

Kelt is committed to future growth through its strategy to implement a full-cycle exploration and development program. In addition, Kelt seeks to identify and acquire strategic oil and gas properties where it believes further exploitation, development and exploration opportunities exist.

The Company's capital expenditures, including acquisitions and dispositions, are summarized in the following table:

	Year ended December 31, 2014		Year ended December 31, 2013[(1)]		
	Amount	**% of total**	Amount	% of total	change
Capital expenditures:					
Lease acquisition and retention	**15,086**	**4%**	12,947	4%	17%
Geological and geophysical	**1,434**	**0%**	3,033	1%	-53%
Drilling and completion of wells	**188,615**	**44%**	84,251	26%	124%
Facilities, pipeline and well equipment	**45,476**	**11%**	19,054	6%	139%
Corporate assets	**636**	**0%**	414	0%	54%
	251,247	**59%**	119,699	37%	110%
Property acquisitions	**24,714**	**6%**	209,444	63%	
Property dispositions	**(19,635)**	**-5%**	-	0%	
Corporate acquisition[(2)]	**167,574**	**40%**	-	0%	
Capital expenditures, net of dispositions	**423,900**	**100%**	329,143	100%	29%

(1) Of the $329.1 million of total capital expenditures incurred during 2013, approximately $23.2 million was incurred prior to completion of the Arrangement on February 26, 2013, as described under the heading of *Common Control Transaction* below.

(2) The total cost of the corporate acquisition, as reported above, includes $72.1 million of cash consideration, $58.0 million of common share consideration valued based on the negotiated price of $13.58 per common share of Kelt, and the $37.4 million working capital deficit assumed.

Corporate acquisition

On July 2, 2014, the Company closed the acquisition of Capio Exploration Ltd. ("Capio"), a private Canadian oil and gas company, by acquiring all of the issued and outstanding common shares of Capio, which held crude oil and natural gas assets located at Valhalla/La Glace, adjacent to Kelt's core producing areas at Pouce Coupe/Spirit River in west central Alberta. Pursuant to the terms of the acquisition, which had an effective date of May 1, 2014, the consideration paid by Kelt, after closing adjustments, consisted of $72.1 million in cash and the issuance of 4,270,956 common shares of Kelt. In addition, Kelt assumed a working capital deficit of $37.4 million, including $32.5 million of bank indebtedness which was repaid at closing and Capio's demand loan credit facility was terminated. Immediately following closing of the acquisition, all of the property, assets and liabilities of Capio were assigned to Kelt and Capio was subsequently dissolved.

Key attributes of the assets acquired:

- At the time of the acquisition, net production was approximately 2,300 BOE per day (70% oil/NGLs and 30% gas) from Triassic horizons, primarily from the Montney formation and also including production from the Halfway and Charlie Lake formations;
- Petroleum and natural gas reserves were evaluated independently by Sproule effective December 31, 2014:
    - Total proved reserves were 8.2 million BOE, with $41.7 million in associated future development capital;
    - Total proved plus probable reserves were 11.9 million BOE, with $41.7 million in associated future development capital;
- Infrastructure component with interests in major oil and gas facilities including a 100% ownership interest in an oil battery, recently upgraded to handle 3,500 barrels of oil per day and 20.0 mmcf of gas per day and 100% ownership interests in gas compressors and oil and gas gathering pipelines;
- Extensive land position that is a complementary fit geographically to Kelt's existing core areas at Pouce Coupe/Spirit River and is located approximately 18 miles south of Pouce Coupe/Spirit River and approximately 15 miles northwest of Grande Prairie. The acquisition included 38,400 gross acres (60 gross sections) and 32,981 net acres (51.5 net sections) of land; and
- The Valhalla/La Glace assets are now operated from Kelt's established field office located in Grande Prairie, Alberta.

The table below summarizes the allocation of the purchase price:

Cash consideration, after closing adjustments	72,136
Issuance of common shares[(1)]	66,243
Total consideration	**138,379**
Net working capital deficit[(2)]	(37,439)
Exploration and evaluation assets	10,832
Property, plant and equipment	184,757
Goodwill	18,206
Decommissioning obligations	(399)
Deferred income tax liability	(37,578)
Fair value of net assets acquired	**138,379**

(1) The number of common shares issued pursuant to the acquisition was negotiated based on a total value of $58.0 million divided by the five day volume weighted average price of Kelt common shares that traded on the Toronto Stock Exchange from June 9th to 13th of $13.58 per common share. Under IFRS 3 *Business Combinations*, the value of common share consideration must be recognized based on acquisition date fair value. Accordingly, the value of common share consideration of $66.2 million reported above is based on the closing price of Kelt common shares on July 2, 2014 of $15.51 per common share.

(2) The net working capital deficit includes $32.5 million of bank indebtedness which was repaid by Kelt at closing pursuant to the change in control provisions under Capio's credit agreement.

The Statement of Profit (Loss) and Comprehensive Income (Loss) includes the results of operations for the period following closing of the transaction on July 2, 2014. Specifically, Kelt's profit for the year ended December 31, 2014 includes approximately $17.4 million of revenue and $8.2 million of operating income generated from the acquired properties subsequent to closing. If the acquisition had occurred on January 1, 2014, pro-forma revenue and operating income for the assets acquired is estimated to be approximately $44.1 million and $22.1 million, respectively, for the year ended December 31, 2014. Operating income is defined as revenue, net of royalties, less production and transportation expenses. This pro-forma information is not necessarily indicative of the results of operations that would have resulted had the acquisition been effected on the dates indicated, or the results that may be obtained in the future.

Stoddart property acquisition

On December 18, 2014, the Company acquired petroleum and natural gas assets located at Stoddart, British Columbia, for cash consideration of $10.4 million. The acquired assets are a strategic and complimentary fit with the Company's core producing assets at Inga. In addition to the low decline liquids rich natural gas production and drilling upside, the assets include a significant infrastructure component. The Company expects that production expense on existing Inga production will be reduced and as more volumes are redirected through the infrastructure in the future, the Company expects a reduction in transportation expense for natural gas and NGLs. Furthermore, the infrastructure allows for significant natural gas volumes to flow into a medium cut third party facility at Stoddart which is expected to result in greater liquids yield from its liquids rich natural gas and incremental liquids volumes to be processed through its own terminal which will result in higher liquids netbacks than previously realized.

Pouce Coupe/Spirit River property acquisition

On December 20, 2013, the Company acquired certain crude oil and natural gas assets located at Pouce Coupe/Spirit River, for cash consideration of $192.0 million, before closing adjustments. The acquisition included an established field office located in the city of Grande Prairie, Alberta which has now become Kelt's main field operating base for all of the Company's operated properties in the newly acquired Pouce Coupe/Spirit River area and in the Company's existing areas at Karr and Grande Cache. The Pouce Coupe/Spirit River assets included an extensive land position that is a complementary fit geographically to Kelt's existing core areas at Karr and Grande Cache and are located 20 and 40 miles north of Karr and Grande Cache, respectively. The acquisition included 256,345 gross acres (400 gross sections) and 103,303 net acres (161 net sections) of land. The acquisition also included a major infrastructure component with interests in major oil and gas facilities including a 20.2% ownership interest in a 140 MMCF per day gas processing plant, varying ownership interests in gas compressors and oil batteries, as well as an extensive network of oil and gas gathering pipelines that is accessible for transportation of current and future oil and gas production.

Fireweed property acquisition

On August 9, 2013, the Company acquired natural gas assets at Fireweed, adjacent to the Company's core producing area at Inga, in northeastern British Columbia, for cash consideration of $15.5 million, before closing adjustments. Kelt acquired a 50% working interest in the Fireweed assets and its partner and the operator at Inga, also acquired a 50% working interest in the assets. The assets acquired include a compression and dehydration facility with approximately 16 MMCF per day of gross natural gas capacity and 25 kilometres of pipeline that adds to the Company's infrastructure in the area. The Fireweed assets are a complementary fit with a contiguous land position adjacent to Kelt's Inga exploration and development core area, including 11,227 net acres (15.8 net sections) of land (6,299 net acres with Doig mineral rights and 7,097 net acres with Montney mineral rights).

Common control transaction

Pursuant to the Arrangement and the Conveyance Agreement, Celtic transferred certain petroleum and natural gas assets to Kelt in exchange for $142.0 million of common share consideration on February 26, 2013. Celtic incurred approximately $23.2 million of capital costs on behalf of Kelt prior to closing of the Arrangement, which were incremental to the value of common share consideration. Accordingly, the additional costs are included in the Company's total capital expenditures for the year ended December 31, 2013.

Non-core property disposition

On February 10, 2014, Kelt completed the disposition of certain non-core and non-operated assets in northwestern Alberta. These assets were part of the assets included in the Pouce Coupe/Spirit River acquisition that was completed on December 20, 2013. The Company received proceeds of $20.0 million, before closing adjustments. Net production from these assets was approximately 210 barrels per day of oil at the time of the disposition. The disposition did not result in a reduction of the authorized borrowing amount available under the Credit Facility.

LAND HOLDINGS

As at December 31, 2014, the Company owned 318,743 net acres of undeveloped land. Based on an internal evaluation of the fair market value of the Company's land holdings at December 31, 2014, Kelt estimates the fair market value of its undeveloped land at $103.2 million. This implies an average fair value of $324 per acre.

Kelt continued to expand its prospect inventory in its core areas. In 2014, the Company expended approximately $14.2 million at Crown land sales acquiring 68,598 net acres (107.2 net sections) of petroleum and natural gas rights at an average bonus cost of $208 per acre, compared to an industry average of $289 per acre (being the combined average of Alberta and British Columbia land sales during 2014, for conventional petroleum and natural gas rights).

Kelt's ongoing land acquisition strategy is focused on building a significant land base of high working interest, internally generated prospects, complemented by third party farm-in arrangements in core exploration areas. The Company will continue building a significant base of high working interest operated prospects, ensuring that the Company is in a position to control its capital expenditure program.

The following table summarizes the Company's land holdings:

LAND HOLDINGS	**As at December 31, 2014**		As at December 31, 2013		Percentage Change	
(Acres)	**Gross**	**Net**	Gross	Net	Gross	Net
Developed	**299,818**	**142,445**	255,320	113,273	17%	26%
Undeveloped	**494,361**	**318,743**	299,142	184,082	65%	73%
Total	**794,179**	**461,188**	554,462	297,355	43%	55%
Average working interest		**58%**		54%		

DRILLING

During the year ended December 31, 2014, the Company drilled 36 (27.1 net) wells, with an overall success rate of 100% on net wells drilled. The Company's average working interest in wells drilled during 2014 was 75% (2013 – 64%). In 2014, Kelt's active horizontal drilling program resulted in an average measured depth of net wells drilled of 3,871 metres (2013 – 3,725 meters). The Company drilled a total of 104,955 net metres during the year (2013 – 45,255 net metres).

DRILLING ACTIVITY	**Three months ended December 31, 2014**		**Year ended December 31, 2014**	
	Gross	**Net**	**Gross**	**Net**
Oil	**5**	**3.1**	**20**	**16.2**
Gas	**4**	**2.3**	**15**	**9.9**
Service	**-**	**-**	**1**	**1.0**
Dry	**-**	**-**	**-**	**-**
Total wells	**9**	**5.4**	**36**	**27.1**
Success rate		**100%**		**100%**

The following table summarizes the Company's drilling activity during the previous year ended December 31, 2013:

DRILLING ACTIVITY	Three months ended December 31, 2013		Year ended December 31, 2013	
	Gross	Net	Gross	Net
Oil	2	2.0	6	5.8
Gas	4	2.2	13	6.4
Dry	-	-	-	-
Total wells	6	4.2	19	12.2
Success rate		100%		100%

RESERVES

Kelt retained Sproule Associates Limited ("Sproule"), an independent qualified reserve evaluator to prepare a report on 100% of its oil and gas reserves (the "Sproule Report"). The Company has a Reserves Committee which oversees the selection, qualifications and reporting procedures of the independent engineering consultants. Reserves as at December 31, 2014 were determined using the guidelines and definitions set out under National Instrument 51-101 ("NI 51-101").

At December 31, 2014, Kelt's proved plus probable reserves were 99.1 million BOE. The Company's net present value of proved plus probable reserves at December 31, 2014, discounted at 10% before tax, was $1.1 billion up 92% from $557.4 million at December 31, 2013. Sproule's forecasted commodity prices for 2015 used to determine the present value of the Company's reserves at December 31, 2014, were US$65.00 per barrel for WTI oil and CA$3.15 per GJ for AECO-C gas.

Proved developed producing reserves at December 31, 2014 were 26.8 million BOE, an increase of 47% from 18.2 million BOE at December 31, 2013. Total proved reserves at December 31, 2014 were 61.1 million BOE, up 73% from 35.3 million BOE at December 31, 2013. Proved plus probable reserves at December 31, 2014 were 99.1 million BOE, an increase of 67% from 59.2 million BOE at December 31, 2013.

At December 31, 2014, the weighting of proved plus probable reserves was 24% oil, 11% NGLs and 65% gas. At December 31, 2013, the weighting of proved plus probable reserves was 20% oil, 8% NGLs and 72% gas.

The following table outlines a summary of the Company's reserves at December 31, 2014:

SUMMARY OF RESERVE VOLUMES (1)	Oil (mbbls)	NGLs (mbbls)	Gas (mmcf)	Combined (mBOE)	FDC Costs ($ thousands)
Proved developed producing	6,713	2,430	105,940	26,800	100
Proved developed non-producing	678	192	5,054	1,712	2,600
Proved undeveloped	7,548	3,687	128,111	32,587	380,100
Total Proved	**14,939**	**6,309**	**239,105**	**61,099**	**382,800**
Probable additional	8,535	4,491	149,909	38,011	122,500
Total Proved plus Probable	**23,474**	**10,800**	**389,014**	**99,110**	**505,300**

(1) Reserve volumes include Company gross working interest share of remaining reserves, as determined in accordance with NI 51-101, plus reserve volumes in which the Company has a royalty interest. The inclusion of royalty interests resulted in an increase in the amount reported for proved plus probable reserves by approximately 100 mBOE or 0.1% of total proved plus probable reserves.

Future development capital ("FDC") expenditures of $382.8 million are included in the reserve evaluation for total proved reserves and are expected to be spent as follows: $119.1 million in 2015, $121.7 million in 2016, $65.6 million in 2017 and $76.4 million thereafter. FDC expenditures of $505.3 million are included for proved plus probable reserves and are expected to be spent as follows: $133.8 million in 2015, $166.7 million in 2016, $114.5 million in 2017 and $90.3 million thereafter.

The following table outlines FDC expenditures by major prospect included in the December 31, 2014 reserve evaluation, for proved ("1P") and proved plus probable ("2P") reserves:

FDC EXPENDITURES	1P FDC ($M)	1P Gross/ (Net) Wells	2P FDC ($M)	2P Gross/ (Net) Wells
Inga/Fireweed/Stoddart	120,900	40 (17.4)	190,600	64 (28.0)
Grande Prairie	229,900	41 (36.9)	260,800	46 (40.7)
Karr	32,000	5 (5.0)	53,900	8 (8.0)
Total FDC Expenditures	**382,800**	**86 (59.3)**	**505,300**	**118 (76.7)**

The following table reconciles the change in total proved reserves during the year:

RESERVES RECONCILIATION **TOTAL PROVED**	Oil (mbbls)	NGLs (mbbls)	Gas (mmcf)	Combined (mBOE)
Balance, December 31, 2013	6,670	2,641	155,696	35,260
Extensions	3,411	883	45,354	11,853
Infill drilling	633	375	5,416	1,911
Technical revisions	1,395	1,384	21,515	6,365
Economic factors	(20)	(8)	(848)	(169)
Acquisitions	4,593	1,371	30,410	11,032
Dispositions	(497)	-	-	(497)
Net additions	9,515	4,005	101,847	30,495
2014 Production	(1,246)	(337)	(18,438)	(4,656)
Balance, December 31, 2014	**14,939**	**6,309**	**239,105**	**61,099**

The following table reconciles the change in total proved plus probable reserves during the year:

RESERVES RECONCILIATION **TOTAL PROVED PLUS PROBABLE**	Oil (mbbls)	NGLs (mbbls)	Gas (mmcf)	Combined (mBOE)
Balance, December 31, 2013	11,808	5,002	254,329	59,198
Extensions	5,268	1,625	90,348	21,951
Infill drilling	615	258	2,975	1,369
Technical revisions	1,125	2,015	14,824	5,611
Economic factors	(18)	(6)	(1,188)	(222)
Acquisitions	6,554	2,243	46,164	16,491
Dispositions	(632)	-	-	(632)
Net additions	12,912	6,135	153,123	44,568
2014 Production	(1,246)	(337)	(18,438)	(4,656)
Balance, December 31, 2014	**23,474**	**10,800**	**389,014**	**99,110**

The WTI oil price during the years 2012 to 2014 was range bound averaging between US$93.00 and US$97.98 per barrel. After a precipitous decline since December 2014, Sproule is forecasting an average WTI oil price of US$65.00 per barrel in 2015. Natural gas prices were much more volatile during the 2012 to 2014 period, during which AECO-C prices averaged between $2.30 and $4.27 per GJ. Sproule is forecasting an average AECO-C gas price of $3.15 per GJ in 2015.

In the Company's December 31, 2014 reserve evaluation, Sproule is forecasting WTI oil prices to average US$83.81 per barrel over the next five years from 2015 to 2019, 10% lower than the average price of US$92.70 per barrel used in the December 31, 2013 evaluation, over the same five year period. For natural gas, AECO-C natural gas prices are forecasted to average $3.88 per GJ over the 2015 to 2019 period, a decrease of 11% from the average price of $4.36 per GJ used in the December 31, 2013 evaluation, over the same five year period.

The following table outlines forecasted future prices that Sproule has used in their evaluation of the Company's reserves at December 31, 2014:

FUTURE COMMODITY PRICE FORECAST	WTI Cushing Oklahoma US$/bbl	Canadian Light Sweet CA$/bbl	NYMEX Henry Hub US$/mmbtu	AECO-C Spot CA$/GJ	USD/CAD Exchange US$/CA$
2015	65.00	70.35	3.25	3.15	0.85
2016	80.00	87.36	3.75	3.52	0.87
2017	90.00	98.28	4.00	3.70	0.87
2018	91.35	99.75	4.50	4.24	0.87
2019	92.72	101.25	5.00	4.79	0.87
Five year average	**83.81**	**91.40**	**4.10**	**3.88**	**0.87**

The Company's net present value of proved plus probable reserves, discounted at 10% before tax, was $1.1 billion as at December 31, 2014, up 92% from $557.4 million as of December 31, 2013. The undiscounted future net cash flow, before tax, was $2.3 billion as of December 31, 2014, an increase of 107% from $1.1 billion as of December 31, 2013. The following table summarizes the net present value of the Company's reserves (before tax) as at December 31, 2014:

NET PRESENT VALUE (BEFORE TAX)

(CA$ millions)	Undiscounted	NPV 5% BT	NPV 8% BT	NPV 10% BT
Proved developed producing	622.9	487.4	432.9	403.6
Proved developed non-producing	47.1	37.8	34.0	31.8
Proved undeveloped	568.3	357.1	276.2	234.0
Total Proved	**1,238.3**	**882.3**	**743.1**	**669.4**
Probable additional	1,032.6	599.0	466.2	402.9
Total Proved plus Probable	**2,270.9**	**1,481.3**	**1,209.3**	**1,072.3**

The Company's net present value of proved plus probable reserves, discounted at 10% after tax, was $885.4 million as of December 31, 2014, up 103% from $437.2 million as of December 31, 2013. The undiscounted future net cash flow, after tax, was $1.8 billion as of December 31, 2014, an increase of 115% from $860.3 million as of December 31, 2013. The following table summarizes the net present value of the Company's reserves (after tax) as at December 31, 2014:

NET PRESENT VALUE (AFTER TAX)

(CA$ millions)	Undiscounted	NPV 5% AT	NPV 8% AT	NPV 10% AT
Proved developed producing	614.0	482.2	429.2	400.5
Proved developed non-producing	35.4	29.8	27.3	26.0
Proved undeveloped	426.3	259.3	195.6	162.4
Total Proved	**1,075.7**	**771.3**	**652.1**	**588.9**
Probable additional	772.0	444.6	344.3	296.5
Total Proved plus Probable	**1,847.7**	**1,215.9**	**996.4**	**885.4**

During 2014, the Company's capital expenditures, net of dispositions, resulted in proved plus probable reserve additions of 44.6 million BOE, resulting in 2P finding, development and acquisition ("FD&A") costs of $13.42 per BOE, including FDC costs. Proved reserve additions in 2014 were 30.5 million BOE, resulting in 1P FD&A costs of $19.25 per BOE, including FDC costs.

The recycle ratio is a measure for evaluating the effectiveness of a company's re-investment program. The ratio measures the efficiency of capital investment. It accomplishes this by comparing the operating netback per BOE to that years' reserve FD&A cost per BOE. Since inception, Kelt has successfully added high quality reserves at an all-in

2P FD&A cost of $13.31 per BOE. Since inception, corporate operating netbacks have averaged $23.56 per BOE, giving the Company an inception to date recycle ratio of 1.8 times. This has been primarily a result of the Company's successful exploration and development drilling programs combined with strategic acquisitions.

The following table provides detailed calculations relating to FD&A costs and recycle ratios:

FINDING, DEVELOPMENT & ACQUISITION COSTS	Year ended December 31		Cumulative since
(CA$ thousands, except as otherwise noted)	**2014**	2013	Incorporation
Proved (1P) reserves:			
Capital expenditures	**423,900**	329,143	753,043
Value of assets conveyed from Celtic Exploration Ltd.	**-**	141,961	141,961
Change in FDC costs required to develop 1P reserves	**163,200**	219,600	382,800
Total capital costs	**587,100**	690,704	1,277,804
1P Reserve additions, net (mBOE)	**30,495**	36,705	67,200
FD&A cost, before FDC ($/BOE)	**13.90**	8.97	11.21
1P FD&A cost, including FDC ($/BOE)	**19.25**	18.82	19.02
Operating netback ($/BOE)[(1)]	**25.62**	16.97	23.56
1P Recycle ratio	**1.3 x**	0.9 x	1.2 x
Proved plus probable (2P) reserves:			
Capital expenditures	**423,900**	329,143	753,043
Value of assets conveyed from Celtic Exploration Ltd.	**-**	141,961	141,961
Change in FDC costs required to develop 2P reserves	**174,000**	331,300	505,300
Total capital costs	**597,900**	802,404	1,400,304
2P Reserve additions, net (mBOE)	**44,568**	60,643	105,211
FD&A cost, before FDC ($/BOE)	**9.51**	5.43	7.16
2P FD&A cost, including FDC ($/BOE)	**13.42**	13.23	13.31
Operating netback ($/BOE)[(1)]	**25.62**	16.97	23.56
2P Recycle ratio	**1.9 x**	1.3 x	1.8 x

In calculating finding and development ("F&D") costs, NI 51-101 requires that exploration and development costs incurred in the year and the change in FDC be aggregated and divided by reserve additions in the year. Under NI 51-101, the F&D calculation expressly excludes acquisitions. The Company believes that by excluding the effect of acquisitions, the provisions of NI 51-101 do not fully reflect Kelt's ongoing reserve replacement costs. Since acquisitions can have a significant impact on annual reserve replacement costs, the Company believes that excluding acquisitions could result in an inaccurate representation of Kelt's cost structure. It is further noted that, for the year ended December 31, 2013, the assets conveyed from Celtic to Kelt pursuant to the Arrangement are reflected as an acquisition in the Sproule Report, therefore it is impracticable to calculate F&D for the previous year and the cumulative F&D cost since incorporation. Accordingly, the Company presents its finding and development costs, inclusive of acquisitions, as shown in the table above.

Excluding the acquisition of Capio, the Company's 2014 capital expenditures resulted in proved plus probable reserve additions of 32.4 million BOE, resulting in 2P F&D costs of $12.01 per BOE, including FDC costs. Proved reserve additions were 22.0 million BOE, resulting in 1P F&D costs of $17.21 per BOE, including FDC costs.

Kelt's 2014 capital investment program resulted in net reserve additions that replaced 2014 production by a factor of 6.5 times on a proved basis (2013 – 25.4 times) and 9.6 times on a proved plus probable basis (2013 – 42.0 times).

The tables below summarize production replacement for 2014:

PRODUCTION REPLACEMENT **TOTAL PROVED RESERVES**	Oil (mbbls)	NGLs (mbbls)	Gas (mmcf)	Combined (mBOE)
Reserve additions, including revisions	9,515	4,005	101,847	30,495
2014 Production	1,246	337	18,438	4,656
Production replacement ratio – 1P	**7.6 x**	**11.9 x**	**5.5 x**	**6.5 x**

PRODUCTION REPLACEMENT **TOTAL PROVED PLUS PROBABLE RESERVES**	Oil (mbbls)	NGLs (mbbls)	Gas (mmcf)	Combined (mBOE)
Reserve additions, including revisions	12,912	6,135	153,123	44,568
2014 Production	1,246	337	18,438	4,656
Production replacement ratio – 2P	**10.4 x**	**18.2 x**	**8.3 x**	**9.6 x**

NET ASSET VALUE

Kelt's net asset value increased to $1.1 billion at December 31, 2014, up 67% from $639.9 million at December 31, 2013. On a per share basis, net asset value increased by 46% to $8.20 per common share at December 31, 2014, compared to $5.61 per common share at December 31, 2013. The present value of petroleum and natural gas ("P&NG") reserves was determined by Sproule in their year-end evaluation report.

The components of net asset value are summarized in the table below. The present value of P&NG reserves is determined using proved plus probable reserves discounted at 8% and 10% before tax. Undeveloped land at December 31, 2014 was internally valued at an average price of $324 per acre. Decommissioning obligations as presented in the financial statements as at December 31, 2014, were revalued using discount rates of 8% and 10% to match the discount rate applied to value P&NG reserves.

NET ASSET VALUE *(CA$ thousands, except per share amounts)*	NPV discounted @ 8% BT	NPV discounted @ 10% BT
Present value of P&NG reserves, before tax	1,209,300	1,072,300
Undeveloped land	103,212	103,212
Present value of decommissioning obligations	(19,555)	(12,758)
Bank debt, net of working capital	(104,430)	(104,430)
Proceeds from exercise of stock options[(1)]	13,102	13,102
Net asset value	1,201,629	1,071,426
Fully diluted common shares outstanding (000's)[(1)]	130,721	130,721
Net asset value ($ per common share)	**9.19**	**8.20**

(1) The calculation of proceeds from exercise of stock options and the fully diluted number of common shares outstanding only include stock options that are "in-the-money" based on the closing price of KEL of $7.00 per common share as at December 31, 2014.

CAPITAL RESOURCES AND LIQUIDITY

MARKET CAPITALIZATION

The Company's total capitalization was $1.1 billion as of December 31, 2014. The market value of common shares, based on the closing share price on the TSX, represented 78% of the total capitalization.

The following table summarizes the Company's capitalization:

CAPITALIZATION	**As at December 31, 2014**		As at December 31, 2013		
(CA$ thousands, except per share amounts)	**Amount**	**% of total**	Amount	% of total	change
Common shares outstanding (000's)	**126,934**		110,026		15%
Share price (last price traded at in the year)	**$7.00**		$9.40		-26%
Market capitalization	**888,538**	**78%**	1,034,244	98%	-14%
Bank debt	**46,929**	**4%**	-	0%	-
Working capital deficiency (surplus)	**57,501**	**5%**	(20,500)	-2%	-
Decommissioning obligations	**94,033**	**8%**	46,857	4%	101%
Deferred income tax liability (asset)	**49,882**	**5%**	(1,957)	0%	-
Total capitalization	**1,136,883**	**100%**	1,058,644	100%	7%

As at December 31, 2014, the Company had $46.9 million of bank debt outstanding on its $235.0 million Credit Facility. Total debt, which is comprised of bank debt and net working capital, was $104.4 million, representing 0.9 times 2014 funds from operations and 1.2 times forecasted 2015 funds from operations.

KEY DEBT RATIOS	**As at December 31, 2014**	
(CA$ thousands, except as otherwise indicated)	**Amount**	**Ratio**
Debt to funds from operations ratio:		
Total debt	**104,430**	
Funds from operations – actual	**115,503**	
Funds from operations – next year forecast	**88,000**	
Debt to funds from operations – trailing		**0.9 x**
Debt to funds from operations – forward		**1.2 x**
Asset coverage ratio:		
Total assets	**908,709**	
Total debt	**104,430**	
Asset coverage		**8.7 x**
Debt to equity ratio:		
Total debt	**104,430**	
Shareholders' equity	**619,639**	
Debt to equity		**0.2 x**

Note that information in the table above is only provided for the current year ended December 31, 2014. As at the previous year ended December 31, 2013, the Company did not have any bank debt outstanding and had a working capital surplus of $20.5 million. Accordingly, the key debt ratios are not applicable for the prior year.

SOURCE OF FUNDS

During the year ended December 31, 2014, the Company generated $112.4 million in cash provided by operating activities. The Company's 2014 capital expenditures were funded by cash on hand, cash provided by operating activities, the issuance of common shares, a minor non-core asset disposition, and bank debt.

During the year ended December 31, 2014, the Company raised gross proceeds of $149.0 million pursuant to private placements, by issuing a total of 12.6 million common shares at an average issue price of $11.83 per common share. In addition, Kelt issued 4.3 million common shares of Kelt to the shareholders of Capio in order to partially fund the corporate acquisition. During the previous year ended December 31, 2013, the Company completed four private placement equity offerings, issuing a total of 48.9 million common shares at an average issue price of $6.56 per common share resulting in aggregate gross proceeds of $320.9 million. Details of the foregoing are set out in note 12 of the financial statements.

The Company has a $235.0 million committed term credit facility (the "Credit Facility") with a syndicate of financial institutions. As at December 31, 2014, Kelt had drawn $46.9 million, leaving sufficient unused credit lines to fund working capital, ongoing operations and capital expenditures. The Credit Facility is available for a revolving period of 364 days, maturing on May 1, 2015, and may be extended for an additional 364 days at the discretion of the lenders, with a term-out to April 29, 2016 if not renewed.

Kelt expects to fund future capital expenditures through the use of a combination of cash provided by operating activities and bank debt, supplemented by new equity or debt offerings, as necessary. Refer to additional information under the heading of *Subsequent Events*.

WORKING CAPITAL

The capital intensive nature of Kelt's operations may create a working capital deficiency position during periods with high levels of capital investment. However, during such periods, the Company maintains sufficient unused bank credit lines to satisfy such working capital deficiencies. As at December 31, 2014, the Company's working capital deficit of $57.5 million combined with outstanding bank debt of $46.9 million, represented 44% of the Company's authorized borrowing amount available under the Credit Facility.

The Company's accounts receivable consists primarily of accrued revenue and joint venture receivables. The oil and gas industry has a pre-arranged monthly clearing day for payment of revenues from all buyers of oil and natural gas. This occurs on the 25th day following the month of sale. As a result, the Company's production revenues are collected in an orderly fashion. Kelt monitors its counterparty credit positions to mitigate any potential credit losses. To the extent that the Company has joint venture partners in its activities, it must collect the partners' share of capital expenditures and operating expenses on a monthly basis. Exceptions are in the event that the partners' share of a capital project is a significant amount. In this case, Kelt will collect such amounts from its partners in advance of expenditures taking place in accordance with standard industry operating procedures. At December 31, 2014, approximately 89% of accounts receivable are current. The balance of accounts receivable outstanding for more than 90 days is approximately $1.3 million and relates primarily to receivables from joint venture partners. Management has reviewed past due accounts and expects the balances to be fully collectible.

Accounts payable and accrued liabilities total $96.8 million as at December 31, 2014, of which approximately $25.9 million is payable and $70.9 million is accrued. Accrued liabilities include approximately $49.5 million of estimated capital expenditures related to the Company's active fourth quarter capital program. Invoices are processed within the Company's normal payment period, which is typically 30 to 60 days.

LIQUIDITY

Liquidity risk is the risk the Company will encounter difficulties in meeting its financial obligations. The Company's financial liabilities are comprised of accounts payable and bank debt. The Company manages liquidity risk through prudent use of bank debt and an actively managed production and capital expenditure budgeting process. In addition, risk management contracts such as derivative financial instruments may be used from time to time. Kelt targets a debt to trailing funds from operations ratio of less than 2.0 times. To manage this, the Board of Directors approves an annual capital expenditure budget, which is regularly monitored and updated as necessary in response to changing capital requirements. Kelt actively manages the pace of its capital spending program by monitoring forecasted

production and commodity prices and resulting cash flows. Should circumstances affect cash flow in a detrimental way, the Company is capable of reducing capital investment levels. In addition, the Company utilizes a control system with respect to authorizations for expenditures on both operated and non-operated projects to further manage capital expenditures.

As at December 31, 2014, the Company had drawn $46.9 million on its $235.0 million Credit Facility, which is structured as a committed term loan. The Credit Facility is available for a revolving period of 364 days, maturing on May 1, 2015, and may be extended for an additional 364 days at the discretion of the lenders, with a term-out to April 29, 2016 if not renewed. Repayments of principal are not required provided that the borrowings under the Credit Facility do not exceed the authorized borrowing amount and the Company is in compliance with all covenants, representations and warranties. The Company is not subject to any financial covenants under the Credit Facility and as at December 31, 2014, Kelt is in compliance with all other covenants. As a result of the precipitous decline in commodity prices, many oil and gas companies, including Kelt, are facing a number of uncertainties. Although management expects that the lenders will extend the Credit Facility in 2015, there is no assurance that the financial institutions will choose to do so. Should the financial institutions not extend the loan, the Company would need to seek alternative sources of debt or equity financing.

SHARE INFORMATION

The Company is authorized to issue an unlimited number of common shares and an unlimited number of preferred shares. As at December 31, 2014 there were 126.9 million common shares issued and outstanding (as at March 9, 2015, there were 130.2 million common shares outstanding). There are no preferred shares issued or outstanding.

As at December 31, 2014, officers, directors, and employees have been granted options to purchase 4.9 million common shares of the Company at an average exercise price of $8.38 per common share. In addition, there are 1.8 million RSUs outstanding. Options and RSUs outstanding at December 31, 2014 represented 5.3% of total common shares outstanding. Additional information regarding the Company's stock options and RSUs is included in note 12 to the financial statements.

The Company's common shares trade on the TSX under the symbol "KEL". During the period from January 1, 2014 to December 31, 2014, 153.1 million common shares traded on the TSX at a weighted average price of $11.78 per common share. The following table outlines Kelt's common share trading activity by quarter:

SHARE TRADING ACTIVITY (KEL)	**Q1 2014**	**Q2 2014**	**Q3 2014**	**Q4 2014**	**YTD 2014**
High ($)	**13.08**	**15.60**	**15.61**	**12.17**	**15.61**
Low ($)	**9.38**	**12.49**	**11.84**	**6.64**	**6.64**
Close ($)	**12.85**	**15.23**	**12.00**	**7.00**	**7.00**
Volume traded (thousands)	**36,504**	**30,916**	**39,918**	**45,750**	**153,088**
Value traded ($ thousands)	**418,714**	**427,382**	**535,633**	**421,097**	**1,802,826**
Weighted average trading price ($)	**11.47**	**13.82**	**13.42**	**9.20**	**11.78**

	Q1 2013	Q2 2013	Q3 2013	Q4 2013	YTD 2013
High ($)	7.45	7.60	8.57	9.74	9.74
Low ($)	5.30	6.10	7.17	8.07	5.30
Close ($)	6.65	7.40	8.39	9.40	9.40
Volume traded (thousands)	57,809	17,154	14,283	16,592	105,838
Value traded ($ thousands)	336,364	120,161	115,978	147,402	719,905
Weighted average trading price ($)	5.82	7.00	8.12	8.88	6.80

DERIVATIVE FINANCIAL INSTRUMENTS

The Company may, from time to time, enter into fixed price contracts and derivative financial instruments with respect to oil and gas sales, currency exchange and interest rates in order to secure a certain amount of cash flow to protect a desired level of capital spending.

The following table summarizes the Company's financial derivative risk management contracts outstanding as of December 31, 2014:

Commodity	Notional volume	Pricing point	Contract Price	Remaining term	Fair value Asset (Liability)
Propane	250 bbls/d	OPIS-Conway	US$ 40.95/bbl	Mar 1 to Dec 31, 2015	**1,745**
Net derivative financial instrument asset					**1,745**

The fair value of the derivative financial instruments is sensitive to changes in commodity prices. If the Canadian dollar equivalent OPIS-Conway propane price increases (decreases) by $1.00 per barrel, the fair market value of the contract would decrease (increase) by approximately $0.1 million.

Subsequent to December 31, 2014, the Company unwound the OPIS-Conway propane contract for cash proceeds of US$1.5 million (CA$1.8 million). In addition, the Company entered into a new forward foreign exchange contract fixing the US/Canadian dollar exchange rate at US$0.7949 on a notional US$3.0 million per month from March to December 2015. This represents approximately 40% of the Company's budgeted oil revenue currency exposure for the same period. The contract will settle monthly, based on the difference between the fixed rate and the average noon exchange rate for the month per the Bank of Canada.

CONTRACTUAL OBLIGATIONS

As of December 31, 2014, the Company is committed to future payments under the following agreements:

(CA$ thousands)	2015	2016	2017	2018	2019	Thereafter
Operating lease – office buildings	1,095	1,229	1,253	495	114	19
Operating lease – vehicles	219	157	69	1	-	-
Flow-through shares	2,002	-	-	-	-	-
Firm transportation commitments	2,967	1,173	14	-	-	-
Total annual commitments	**6,283**	**2,559**	**1,336**	**496**	**114**	**19**

Payments under the office building operating leases relate to the Company's head office in Calgary, Alberta, and the field office in Grande Prairie, Alberta. The head office and field office leases expire on April 30, 2018 and February 28, 2020, respectively, if not extended.

On December 18, 2014, the Company issued 0.182 million flow-through shares at a price of $11.00 per flow-through share. Pursuant to the provisions in the *Income Tax Act* (Canada), the Company shall incur Canadian exploration expenses (the "Qualifying Expenditures") after December 18, 2014 and prior to December 31, 2015 in the aggregate amount of not less than $2.0 million. As of December 31, 2014, the Company had not incurred any Qualifying Expenditures, leaving $2.0 million of Qualifying Expenditures to be incurred in 2015. Kelt shall renounce the Qualifying Expenditures so incurred to the subscriber of the flow-through shares such that $11.00 per flow-through share shall be deductible against the subscriber's income for the fiscal year ended December 31, 2014.

RELATED PARTY TRANSACTIONS

A director of the Company is also a partner at a law firm which Kelt has engaged to provide legal services. During the year ended December 31, 2014, the Company incurred $0.4 million (2013 – $0.6 million) in legal fees and disbursements, of which, less than $0.1 million is payable at December 31, 2014 (2013 – $0.2 million). The Company expects to continue using the services of this law firm from time to time.

Key management personnel are those persons having authority and responsibility for planning, directing and controlling the activities of the Company. The following table summarizes compensation paid or payable to officers and directors of the Company:

	Year ended December 31	
	2014	2013
Salaries, bonuses and other benefits	**715**	485
Share based compensation	**4,096**	3,392
Total compensation	**4,811**	3,877

During the year ended December 31, 2014, key management personnel were granted an aggregate of 970,000 stock options with an average exercise price of $9.34 per share. During the previous year ended December 31, 2013, key management personnel were granted an aggregate of 789,000 restricted share units and 1,250,000 stock options with an exercise price of $6.47 per share.

The Common Control Transaction is considered to be a related party transaction because Kelt was a wholly owned subsidiary of Celtic immediately prior to closing of the Arrangement. Refer to note 4 of the financial statements for additional information regarding accounting for the transaction.

OFF-BALANCE SHEET TRANSACTIONS

The Company did not engage in any off-balance sheet transactions during the years ended December 31, 2014 and 2013.

SUBSEQUENT EVENTS

Acquisition of Artek Exploration Ltd.

On February 20, 2015, Kelt entered into an agreement with Artek Exploration Ltd. (“Artek”), pursuant to which Kelt will acquire all of the issued and outstanding common shares of Artek on the basis of 0.34 of a Kelt common share for each Artek common share. The acquisition will be effected by way of a statutory plan of arrangement (the “Artek Arrangement”).

Based on the volume-weighted average trading price of the Kelt common shares for the five trading days ended February 20, 2015 of $8.10 on the TSX, the total consideration is approximately $307 million, comprised of the issuance of approximately 26.9 million Kelt common shares and the assumption of an estimated $89.5 million of bank debt, net of working capital, as at February 20, 2015, which includes estimated associated transaction costs of approximately $5.6 million.

Completion of the Artek Arrangement, which is anticipated to occur on or around April 16, 2015, is subject to, among other things, the approval of at least 66⅔% of votes cast by Artek shareholders voting at a special meeting of shareholders to be held on or around April 16, 2015, the approval of the Court of Queen’s Bench of Alberta, receipt of all necessary regulatory and stock exchange approvals and certain closing conditions that are customary for a transaction of this nature.

The Board of Directors of Artek has unanimously approved the Artek Arrangement and, based in part on a fairness opinion from Artek’s financial advisor, determined that the Artek Arrangement is in the best interests of Artek and the holders of its common shares, and is fair to Artek’s shareholders. Based on the recommendation of the independent committee of the Board of Directors of Artek, the Artek Board of Directors has also resolved to recommend that Artek shareholders vote their common shares in favour of the Artek Arrangement. All of the directors and officers of Artek representing an aggregate of 21.9% of the issued and outstanding Artek common shares, have entered into support agreements pursuant to which they have agreed to vote their Artek common shares in favour of the Artek Arrangement. Artek has agreed not to solicit or initiate any discussion regarding any other business combination or sale of material assets. Artek has also granted Kelt a right to match any superior proposal and has agreed to pay a termination fee of $8.5 million to Kelt in certain events, including if Artek recommends, approves or enters into an agreement with respect to a superior proposal.

The acquisition of Artek will consolidate the majority of Kelt's land acreage in its Inga-Fireweed-Stoddart, British Columbia core area to 100% and is consistent with the Company's strategy to operate and control all of its major core exploration and development prospects. In addition, Kelt's acquisition of Artek will result in 100% ownership by Kelt in key infrastructure including compression facilities and pipelines in the area. The net present value of Artek's Inga-Fireweed-Stoddart reserves at December 31, 2014 represented approximately 90% of Artek's total corporate reserves value.

Key attributes of Kelt's acquisition of Artek include:

- The Artek acquisition is expected to be accretive to existing shareholders of Kelt on a reserves per share, production per share, funds from operations per share and net asset value per share basis;
- Artek's reserves at December 31, 2014 consist of 24.0 million BOE of proved reserves and 46.4 million BOE of proved plus probable reserves;
- Acquisition cost, including future development capital costs and estimated associated transaction costs, is $20.46 per BOE for proved reserves and $12.89 per BOE for proved plus probable reserves;
- Artek's January 2015 production is estimated to be approximately 5,400 BOE per day; and
- Artek's land holdings at December 31, 2014 were 262,254 net acres of which 202,967 net acres were undeveloped.

The anticipated pro-forma impact of the Artek Arrangement on Kelt's forecasted operating results and financial position is discussed under the heading of *2015 Guidance*.

Equity Private Placement

In February 2015, the Company agreed to issue by way of private placement, on a non-brokered basis, 3,881,400 common shares on a "flow-through" basis in respect of Canadian development expenses at a price of $8.60 per flow-through common share (the "2015 Private Placement"), resulting in gross proceeds of $33.4 million. Certain directors and officers of the Company have subscribed to purchase 1,714,500 flow-through common shares for gross proceeds of $14.9 million, representing approximately 44% of the aggregate issue. The 2015 Private Placement will be completed in three tranches. The first tranche of 1,000,000 flow-through common shares closed on February 27, 2015. The second tranche of 2,300,000 flow-through common shares closed on March 6, 2015. The remaining tranche of 581,400 flow-through common shares is expected to close on or about March 16, 2015. Net proceeds of the offering will be used to partially finance drilling and completion expenditures during the remainder of 2015.

Kelt shall, pursuant to the provisions of the *Income Tax Act* (Canada), incur eligible Canadian development expenses, (the "Qualifying Expenditures") after the closing date and prior to December 31, 2015 in the aggregate amount of not less than the total amount of the gross proceeds raised from the issue of flow-through common shares. Kelt shall renounce the Qualifying Expenditures so incurred to the purchasers of the flow-through common shares in an amount equal to $8.60 per flow-through common share on or prior to December 31, 2015.

The Kelt common shares issued and to be issued in connection with the 2015 Private Placement are subject to a statutory hold period of four months plus one day from the respective dates of completion of the offering, in accordance with applicable securities legislation.

SUMMARY OF QUARTERLY RESULTS

Comparative quarterly information is presented in the table below. The Company was incorporated on October 11, 2012 and commenced active operations on February 27, 2013, following completion of the Arrangement.

(CA$ thousands, except as otherwise indicated)	**Q4 2014**	Q3 2014	Q2 2014	Q1 2014
Revenue, before royalties and financial instruments	**54,396**	61,136	51,366	47,793
Funds from operations	**29,664**	31,799	27,956	26,084
Per share – basic ($/common share)	**0.23**	0.25	0.23	0.24
Per share – diluted ($/common share)	**0.23**	0.25	0.22	0.23
Profit (loss) and comprehensive income (loss)	**1,256**	1,185	3,336	4,851
Per share – basic ($/common share)	**0.01**	0.01	0.03	0.04
Per share – diluted ($/common share)	**0.01**	0.01	0.03	0.04
Total assets	**908,709**	820,241	669,098	666,257
Bank debt	**46,929**	-	-	-
Working capital deficiency (surplus)	**57,501**	37,219	(116,488)	(123,150)
Shareholders' equity	**619,639**	614,384	544,735	539,410
Average daily production (BOE/d)	**15,559**	13,872	11,381	10,143
Average realized price, after financial instruments ($/BOE)	**39.96**	47.49	48.23	50.99
Operating netback ($/BOE)	**21.55**	25.81	27.63	29.40
Netback as a percentage of revenue	**54%**	54%	57%	58%

	Q4 2013	Q3 2013	Q2 2013	Q1 2013
Revenue, before royalties and financial instruments	18,543	12,388	11,860	3,865
Funds from operations	9,396	5,473	6,608	2,179
Per share – basic ($/common share)	0.09	0.06	0.08	0.09
Per share – diluted ($/common share)	0.09	0.06	0.08	0.09
Profit (loss) and comprehensive income (loss)	(1,838)	(2,400)	(737)	(140)
Per share – basic ($/common share)	(0.02)	(0.03)	(0.01)	(0.01)
Per share – diluted ($/common share)	(0.02)	(0.03)	(0.01)	(0.01)
Total assets	485,201	333,832	229,370	141,834
Bank debt	-	-	-	-
Working capital deficiency (surplus)	(20,500)	(123,774)	(58,058)	24,471
Shareholders' equity	392,872	294,820	191,256	98,138
Average daily production (BOE/d)	5,739	4,636	4,097	1,316
Average realized price, after financial instruments ($/BOE)	34.74	28.17	32.42	32.64
Operating netback ($/BOE)	18.67	12.94	18.42	19.28
Netback as a percentage of revenue	54%	46%	57%	59%

Since commencing active operations on February 27, 2013, the Company has significantly grown its asset and production base through a combination of robust drilling program and accretive acquisitions. In addition to cash provided by operating activities, the Company's capital expenditures were funded primarily through equity financings, and supplemented by bank debt starting in the fourth quarter of 2014. Increased production and higher average realized prices combined with the maintenance of a low cost structure resulted in a significant improvement in profit and funds from operations per common share and operating netbacks during 2014.

Inherent to the nature of the oil and gas industry, fluctuations can be expected quarter over quarter in the amount of revenue, funds from operations and/or profit (loss) generated by the Company. These fluctuations may be caused by, among other things, variations in production volumes, realized commodity prices and the related impact on royalties, changes in per unit expenses and provisions for deferred income taxes. Refer to the *Results of Operations* section of this MD&A for an explanation of changes.

SELECTED ANNUAL INFORMATION

The following table summarizes key annual financial and operating information over the most recently completed financial years. The Company was incorporated on October 11, 2012 and did not have any assets, liabilities or active operations until February 27, 2013, following completion of the Arrangement on February 26, 2013.

(CA$ thousands, except as otherwise indicated)	**2014**	2013	2012
Revenue, before royalties and financial instruments	**214,691**	46,656	-
Funds from operations	**115,503**	23,656	-
Per share – basic ($/common share)	**0.95**	0.32	-
Per share – diluted ($/common share)	**0.93**	0.32	-
Profit (loss) and comprehensive income (loss)	**10,628**	(5,115)	-
Per share – basic ($/common share)	**0.09**	(0.07)	-
Per share – diluted ($/common share)	**0.09**	(0.07)	-
Total assets	**908,709**	485,201	-
Bank debt	**46,929**	-	-
Working capital deficiency (surplus)	**57,501**	(20,500)	-
Shareholders' equity	**619,639**	392,872	-
Average daily production (BOE/d)	**12,756**	3,961	-
Average realized price, after financial instruments ($/BOE)	**46.03**	32.03	-
Operating netback ($/BOE)	**25.62**	16.97	-
Netback as a percentage of revenue	**56%**	53%	-

BUSINESS RISKS

The business of exploring for, developing and producing oil and natural gas reserves is inherently risky. The following information is a summary only of certain risk factors relating to the Company and should be read in conjunction with the Company's Annual Information Form dated March 28, 2014. In addition, the Company's Annual Information Form as at December 31, 2014, will be filed on or about March 11, 2015. The risks set out below are not an exhaustive list, nor should be taken as a complete summary or description of all the risks associated with the Company's business and the oil and natural gas business generally.

Exploration, Development and Production Risks

Oil and natural gas operations involve many risks that even a combination of experience, knowledge and careful evaluation may not be able to overcome. There is no assurance that expenditures made on exploration by the Company will result in new discoveries of oil or natural gas in commercial quantities. It is difficult to project the costs of implementing an exploratory drilling program due to the inherent uncertainties of drilling in unknown formations, the costs associated with encountering various drilling conditions such as over pressured zones and tools lost in the hole, and changes in drilling plans and locations as a result of prior exploratory wells or additional seismic data and interpretations thereof. The long-term commercial success of the Company depends on its ability to find, acquire, develop and commercially produce oil and natural gas reserves. Without the continual addition of new reserves, the Company's existing reserves, and the production from them, will decline over time as the Company produces from such reserves. A future increase in the Company's reserves will depend on both the ability of the Company to explore and develop its existing properties and on its ability to select and acquire suitable producing properties or prospects. There is no assurance that the Company will be able continue to find satisfactory properties to acquire or participate in. Moreover, management of the Company may determine that current markets, terms of acquisition, participation or pricing conditions make potential acquisitions or participations uneconomic. There is also no assurance that the Company will discover or acquire further commercial quantities of oil and natural gas.

Future oil and gas exploration may involve unprofitable efforts, not only from dry wells but from wells that are productive but do not produce sufficient net revenues to return a profit after drilling, completing, operating and other costs. Completion of a well does not ensure a profit on the investment or recovery of drilling, completion and operating costs.

Drilling hazards or environmental damage could greatly increase the cost of operations and various field operating conditions may adversely affect the production from successful wells. These conditions include, but are not limited to, delays in obtaining governmental approvals or consents, shut-ins of connected wells resulting from extreme weather conditions, insufficient storage or transportation capacity or other geological and mechanical conditions.

While diligent well supervision and effective maintenance operations can contribute to maximizing production rates over time, it is not possible to eliminate production delays and declines from normal field operating conditions, which can negatively affect revenue and cash flow levels to varying degrees.

Oil and natural gas exploration, development and production operations are subject to all the risks and hazards typically associated with such operations, including, but not limited to, fire, explosion, blowouts, cratering and spills or other environmental hazards. These typical risks and hazards could result in substantial damage to oil and natural gas wells, production facilities, other property, the environment and personal injury.

Oil and natural gas production operations are also subject to all the risks typically associated with such operations, including encountering unexpected formations or pressures, premature decline of reservoirs and the invasion of water into producing formations. Losses resulting from the occurrence of any of these risks may have a material adverse effect on the Company's business, financial condition, results of operations and prospects.

As is standard industry practice, the Company is not fully insured against all risks, nor are all risks insurable. Although the Company maintains liability insurance in an amount that it considers consistent with industry practice, liabilities associated with certain risks could exceed policy limits or not be covered. In either event the Company could incur significant costs. See additional information under the heading of *Insurance* below.

Prices, Markets and Marketing of Crude Oil and Natural Gas

Oil and natural gas are commodities whose prices are determined based on world demand, supply and other factors, all of which are beyond the control of Kelt. World prices for oil and natural gas have fluctuated widely in recent years. Any material decline in prices will result in a reduction of net production revenue. Certain wells or other projects may become uneconomic as a result of a decline in world oil prices and natural gas prices, leading to a reduction in the future volume of Kelt's oil and gas production. Kelt might also elect not to produce from certain wells at lower prices. All these factors could result in a material decrease in Kelt's future net production revenue, causing a reduction in its oil and gas acquisition and development activities. In addition, bank borrowings available to Kelt will be in part determined by the borrowing base of Kelt. A sustained material decline in prices from historical average prices could reduce Kelt's future borrowing base, therefore reducing the bank credit available to Kelt, and could require that a portion of any existing bank debt of Kelt be repaid.

In addition to establishing markets for its oil and natural gas, Kelt must also successfully market its oil and natural gas to prospective buyers. The marketability and price of oil and natural gas which may be acquired or discovered by Kelt will be affected by numerous factors beyond its control. Kelt will be affected by the differential between the price paid by refiners for light quality oil and the grades of oil produced by Kelt. The ability of Kelt to market natural gas may depend upon its ability to acquire space on pipelines which deliver natural gas to commercial markets. Kelt will also likely be affected by deliverability uncertainties related to the proximity of its reserves to pipelines and processing facilities and related to operational problems with such pipelines and facilities and extensive government regulation relating to price, taxes, royalties, land tenure, allowable production, the export of oil and natural gas and the management of other aspects of the oil and natural gas business. Kelt has limited direct experience in the marketing of oil and natural gas.

Seasonality

The level of activity in the Canadian oil and gas industry is influenced by seasonal weather patterns. Wet weather and spring thaw may make the ground unstable. Consequently, municipalities and provincial transportation departments enforce road bans that restrict the movement of rigs and other heavy equipment, thereby reducing activity levels. Also, certain oil and gas producing areas are located in areas that are inaccessible other than during the winter months because the ground surrounding the sites in these areas consists of swampy terrain. There can be no assurance that these seasonal factors will not adversely affect the timing and scope of Kelt's exploration and development activities, which could in turn have a material adverse impact on Kelt's business, operations and prospects.

Possible Failure to Realize Anticipated Benefits of Acquisitions and Dispositions

As part of its ongoing strategy, the Company may complete acquisitions of assets or other entities in the future. Achieving the benefits of completed and future acquisitions depends in part on successfully consolidating functions and integrating operations, procedures and personnel in a timely and efficient manner, as well as the Company's ability to realize the anticipated growth opportunities and synergies from combining the acquired businesses and operations with those of the Company. The integration of acquired businesses and entities requires the dedication of substantial management effort, time and resources which may divert management's focus and resources from other strategic opportunities and from operational matters during this process. The integration process may result in the loss of key employees and the disruption of ongoing business, customer and employee relationships that may adversely affect the Company's ability to achieve the anticipated benefits of any acquisitions. In addition, noncore assets may be periodically disposed of so the Company can focus its efforts and resources more efficiently. Depending on the state of the market for such non-core assets, certain non-core assets of the Company, if disposed of, may realize less than their carrying value on the financial statements of the Company.

Capital Markets

Notwithstanding the on-going recovery in the global economic situation, Kelt, along with all other oil and gas entities, may have restricted access to capital, bank debt and equity. The lending capacity of all financial institutions has diminished and risk premiums have increased. As future capital expenditures will be financed out of funds generated from operations, non-core property dispositions, borrowings and possible future equity sales, Kelt's ability to do so is dependent on, among other factors, the overall state of capital markets and investor appetite for investments in the energy industry and Kelt's securities in particular.

To the extent that external sources of capital become limited or unavailable or available on onerous terms, Kelt's ability to make capital investments and maintain existing assets may be impaired, and its assets, liabilities, business, financial condition and results of operations may be materially and adversely affected as a result.

Based on current funds available and expected funds generated from operations, Kelt believes it has sufficient funds available to fund its projected capital expenditures. However, if funds generated from operations are lower than expected or capital costs for these projects exceed current estimates, or if Kelt incurs major unanticipated expense related to development or maintenance of its existing properties, it may be required to seek additional capital to maintain its capital expenditures at planned levels. Failure to obtain any financing necessary for Kelt's capital expenditure plans may result in a delay in development or production on Kelt's properties.

Regulatory

Various levels of governments impose extensive controls and regulations on oil and natural gas operations (exploration, production, pricing, marketing and transportation). Governments may regulate or intervene with respect to exploration and production activities, prices, taxes, royalties and the exportation of oil and natural gas. Amendments to these controls and regulations may occur from time to time in response to economic or political conditions. The implementation of new regulations or the modification of existing regulations affecting the oil and natural gas industry could reduce demand for crude oil and natural gas and increase the Company's costs, either of which may have a material adverse effect on the Company's business, financial condition, results of operations and prospects.

In addition to regulatory requirements pertaining to the production, marketing and sale of oil and natural gas mentioned above, the Company's business and financial condition could be influenced by federal legislation affecting, in particular, foreign investment, through legislation such as the *Competition Act* (Canada) and the *Investment Canada Act* (Canada).

Royalty Regimes

There can be no assurance that the federal government and the provincial governments of the western provinces will not adopt a new or modify the royalty regime which may have an impact on the economics of the Company's projects. An increase in royalties would reduce the Company's earnings and could make future capital investments, or the Company's operations, less economic.

Insurance

Kelt's involvement in the exploration for and development of oil and gas properties may result in Kelt becoming subject to liability for pollution, blow-outs, property damage, personal injury and other hazards. Although Kelt has obtained insurance in accordance with industry standards to address such risks, such insurance has limitations on liability that may not be sufficient to cover the full extent of such liabilities. In addition, such risks may not, in all circumstances be insurable or, in certain circumstances, Kelt may elect not to obtain insurance to deal with specific risks due to the high premiums associated with such insurance or for other reasons. The payment of such uninsured liabilities would reduce the funds available to Kelt. The occurrence of a significant event that Kelt is not fully insured against, or the insolvency of the insurer of such event, could have a material adverse effect on Kelt's financial position, results of operations or prospects.

Operational Dependence

Other companies operate some of the assets in which Kelt has an interest. As a result, Kelt will have limited ability to exercise influence over the operation of those assets or their associated costs, which could adversely affect Kelt's financial performance. Kelt's return on assets operated by others will therefore depend upon a number of factors that may be outside of Kelt's control, including the timing and amount of capital expenditures, the operator's expertise and financial resources, the approval of other participants, the selection of technology and risk management practices.

Competition

The oil and gas industry is highly competitive. Kelt actively competes for reserve acquisitions, exploration leases, licenses and concessions and skilled industry personnel with a substantial number of other oil and gas entities, many of which have significantly greater financial resources, staff and facilities than Kelt. Kelt's competitors include integrated oil and natural gas companies and numerous other independent oil and natural gas companies and individual producers and operators. Certain of Kelt's customers and potential customers may themselves explore for oil and natural gas and the results of such exploration efforts could affect Kelt's ability to sell or supply oil or gas to these customers in the future. Kelt's ability to successfully bid on and acquire additional property rights, to discover reserves to participate in drilling opportunities and to identify and enter into commercial arrangements with customers will be dependent upon developing and maintaining close working relationships with its future industry partners and joint operators and its ability to select and evaluate suitable properties and to consummate transactions in a highly competitive environment. Competitive factors in the distribution and marketing of oil and natural gas include price and methods and reliability of delivery and storage. Competition may also be presented by alternate fuel sources.

Environmental Risks

All phases of the oil and natural gas business present environmental risks and hazards and are subject to environmental regulation pursuant to a variety of international conventions and federal, provincial and municipal laws and regulations. Environmental legislation provides for, among other things, restrictions and prohibitions on spills, releases or emissions of various substances produced in association with oil and gas operations. The legislation also requires that wells and facility sites be operated, maintained, abandoned and reclaimed to the satisfaction of applicable regulatory authorities. Compliance with such legislation can require significant expenditures and a breach may result in the imposition of fines and penalties, some of which may be material.

Environmental legislation is evolving in a manner expected to result in stricter standards and enforcement, larger fines and liability and potentially increased capital expenditures and operating costs. The discharge of oil, natural gas or other pollutants into the air, soil or water may give rise to liabilities to foreign governments and third parties and may require Kelt to incur costs to remedy such discharge. Implementation of strategies with respect to climate change and reducing greenhouse gases could have material impact on the nature of oil and natural gas operations, including those of Kelt. No assurance can be given that the application of environmental laws to the business and operations of Kelt will not result in a curtailment of production or a material increase in the costs of production, development or exploration activities or otherwise adversely affect Kelt's financial condition, results of operations or prospects.

Global Financial Markets

Market events and conditions, including disruptions in the international credit markets and other financial systems, and the deterioration of global economic conditions caused significant volatility to commodity prices over the last few

years. These conditions have resulted in a loss of confidence in the broader U.S. and global credit and financial markets and resulting in the collapse of, and government intervention in, major banks, financial institutions and insurers and creating a climate of greater volatility, less liquidity, widening of credit spreads, a lack of price transparency, increased credit losses and tighter credit conditions. Notwithstanding various actions by governments, concerns about the general condition of the capital markets, financial instruments, banks, investment banks, insurers and other financial institutions caused the broader credit markets to further deteriorate and stock markets to decline substantially. These factors have negatively impacted company valuations and may continue to impact the performance of the global economy going forward.

If the economic climate in the U.S. or the world generally deteriorates further, demand for petroleum products could diminish further and prices for oil and natural gas could decrease further, which could adversely impact Kelt's results of operations, liquidity and financial condition.

Geo-Political Risks

The marketability and price of oil and natural gas that may be acquired or discovered by Kelt is and will continue to be affected by political events throughout the world that cause disruptions in the supply of oil. Conflicts, or conversely peaceful developments, arising in the Middle East, and other areas of the world, have a significant impact on the price of oil and natural gas. Any particular event could result in a material decline in prices and therefore result in a reduction of Kelt's net production revenue.

In addition, Kelt's expected oil and natural gas properties, wells and facilities could be subject to a terrorist attack. As the oil and gas industry in Canada is a key supplier of energy to the United States, certain terrorist groups may target Canadian oil and gas properties, wells and facilities in an effort to choke the United States economy. If any of Kelt's properties, wells or facilities are the subject of terrorist attack it could have a material adverse effect on Kelt. Kelt does not have insurance to protect against the risk from terrorism.

BUSINESS OUTLOOK

ADVISORY REGARDING FORWARD-LOOKING STATEMENTS

Certain information with respect to Kelt contained herein, including management's assessment of future plans and operations, contains forward-looking statements. These forward-looking statements are based on assumptions and are subject to numerous risks and uncertainties, certain of which are beyond Kelt's control, including the impact of general economic conditions, industry conditions, volatility of commodity prices, currency exchange rate fluctuations, imprecision of reserve estimates, environmental risks, competition from other explorers, stock market volatility and ability to access sufficient capital. As a result, Kelt's actual results, performance or achievement could differ materially from those expressed in, or implied by, these forward-looking statements and, accordingly, no assurance can be given that any events anticipated by the forward-looking statements will transpire or occur. In addition, the reader is cautioned that historical results are not necessarily indicative of future performance.

CURRENT ECONOMIC ENVIRONMENT

The current economic environment continues to be challenging and uncertain. Increasing global crude oil supplies have surpassed global demand and as a result, crude oil prices have been negatively affected. Natural gas infrastructure and capacity constraints continue to impact commodity prices being realized in domestic markets relative to world markets. In addition, uncertainties facing debt markets around the world could lead to tighter credit markets in the future.

In this environment, Kelt is focused on maintaining a strong balance sheet, giving the Company the ability to take advantage of opportunities as they arise. The Company's capital expenditure program is also flexible, with the ability to defer expenditures into the future if the current economic environment deteriorates.

2015 GUIDANCE

The oil and gas industry around the world is currently facing a challenging environment after the recent precipitous decline in global crude oil prices. Due to market instability and volatile commodity prices, many oil and gas companies are reducing their 2015 capital spending plans. Ultimately, lower capital investment in oil and gas drilling can be expected to balance the supply and demand ratio. Kelt believes that the current business environment creates opportunities to add value at a reasonable cost and is optimistic about the long-term outlook for oil and gas commodity prices. The Company is opportunity driven and is confident that it can grow its production base by building on its current inventory of development projects and by adding new exploration prospects.

The table below outlines the Company's financial and operating guidance for 2015, as well as the pro-forma impact of the Artek Arrangement and 2015 Private Placement:

(CA$ millions, except as otherwise indicated)	2015 Guidance	2015 Pro-forma	Percent Change
Average Production			
Oil (bbls/d)	5,050	6,250	24%
NGLs (bbls/d)	1,330	2,000	50%
Gas (mmcf/d)	61.32	70.50	15%
Combined (BOE/d)	16,600	20,000	20%
Production per million common shares (BOE/d)	131	137	5%
Oil / NGLs / Gas production weighting	30%/8%/62%	31%/10%/59%	-
Forecasted Average Commodity Prices			
WTI oil price (USD/bbl)	59.50	59.50	-
NYMEX natural gas price (USD/MMBTU)	3.25	3.25	-
AECO natural gas price ($/GJ)	3.10	3.10	-
Capital Expenditures			
Drilling & completions	90.0	88.0	-2%
Facilities, pipeline & well equipment	30.0	30.0	-
Land, seismic & property "tuck-in" acquisitions	32.0	32.0	-
Artek Arrangement	-	307.0	-
Total Capital Expenditures	152.0	457.0	201%
Funds from operations	88.0	114.4	30%
Per share, diluted	0.68	0.75	10%
Bank debt, net of working capital, at year-end	172.0	198.0	15%
Debt/Trailing funds from operations ratio(1)	2.0 x	1.7 x	-
Weighted average common shares outstanding (MM)	126.9	149.9	18%
Common shares issued & outstanding (MM)	126.9	158.4	25%

(1) Debt/Trailing funds from operations ratio is calculated using estimated bank debt, net of working capital, at December 31st of the year divided by estimated funds from operations for that year.

Kelt has a Credit Facility with a syndicate of financial institutions, and as at December 31, 2014, the authorized borrowing amount was $235.0 million. The Credit Facility is available for a revolving period of 364 days, maturing on May 1, 2015, and may be extended for an additional 364 days at the discretion of the lenders, with a term-out to April 29, 2016 if not renewed. The Company expects that the lenders will extend the Credit Facility for an additional 364

days upon maturity and that the lenders will review the authorized borrowing amount on or before May 1, 2015. The borrowing base is determined, in part, by reference to the Company's reserves. The Company believes that an increase in the borrowing base will be supported by the Artek Arrangement and the significant increase in the Company's reserves as per the December 31, 2014 reserves evaluation.

Changes in forecasted commodity prices and variances in production estimates can have a significant impact on estimated funds from operations and profit. Please refer to the cautionary statement on forward-looking statements and information set out herein.

The information set out herein under the heading "2015 Guidance" is "financial outlook" within the meaning of applicable securities laws. The purpose of this financial outlook is to provide readers with disclosure regarding Kelt's reasonable expectations as to the anticipated results of its proposed business activities for 2015. Readers are cautioned that this financial outlook may not be appropriate for other purposes.

ADDITIONAL INFORMATION

Additional information relating to Kelt, including the Company's Annual Information Form ("AIF") dated March 28, 2014, is filed on SEDAR and can be viewed on their website at www.sedar.com. In addition, the Company's Annual Information Form as at December 31, 2014, will be filed on or about March 11, 2015. Copies of the AIF can also be obtained by contacting Sadiq H. Lalani, Vice President, Finance and Chief Financial Officer at Kelt Exploration Ltd., Suite 300, 311 Sixth Avenue SW, Calgary, Alberta, Canada, T2P 3H2. Further information relating to the Company is also available on its website at www.keltexploration.com.

On behalf of the Board of Directors,

[signed]

David J. Wilson
President and Chief Executive Officer
March 9, 2015

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MANAGEMENT'S REPORT

The accompanying financial statements of Kelt Exploration Ltd. (the "Company") are the responsibility of management. The financial statements have been prepared by management in Canadian dollars in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB") and include certain estimates that reflect management's best judgments. When alternative accounting methods exist, management has chosen those it deems most appropriate in the circumstances.

Management has the overall responsibility for internal controls and maintains a system of internal controls over financial reporting that provides reasonable assurance that the financial information is relevant, reliable and accurate and that the Company's assets are properly accounted for and adequately safeguarded.

The Board of Directors is responsible for ensuring that management fulfills its responsibilities for financial reporting and internal control. The Board exercises this responsibility with the assistance of the Audit Committee. This Committee, consisting of non-management directors, meets with management and independent auditors to ensure that each group is properly discharging its responsibilities and to discuss adequacy of internal controls, accounting policies and financial reporting matters. The Audit Committee has reviewed the financial statements and has reported thereon to the Board of Directors. The Board of Directors has approved the financial statements and authorized them for issuance to shareholders.

PricewaterhouseCoopers LLP, an independent firm of Chartered Accountants, has been engaged, as approved by the shareholders of the Company, to provide an independent audit opinion on the Company's financial statements. Their report, contained herein, outlines the nature of their audit and expresses an unqualified opinion on the financial statements.

[signed]

David J. Wilson
President and Chief Executive Officer
March 9, 2015

[signed]

Sadiq H. Lalani
Vice President, Finance, and Chief Financial Officer
March 9, 2015

INDEPENDENT AUDITOR'S REPORT

To the Shareholders of Kelt Exploration Ltd.

We have audited the accompanying financial statements of Kelt Exploration Ltd., which comprise the statements of financial position as at December 31, 2014 and December 31, 2013 and the statements of profit (loss) and comprehensive income (loss), changes in shareholders' equity and cash flows for the years then ended, and the related notes, which comprise a summary of significant accounting policies and other explanatory information.

Management's responsibility for the financial statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with International Financial Reporting Standards, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained in our audits is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements present fairly, in all material respects, the financial position of Kelt Exploration Ltd. as at December 31, 2014 and December 31, 2013 and its financial performance and its cash flows for the years then ended in accordance with International Financial Reporting Standards as issued by the International Accounting Standards Board.

PricewaterhouseCoopers LLP

Chartered Accountants
Calgary, Alberta
March 9, 2015

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"PwC" refers to PricewaterhouseCoopers LLP, an Ontario limited liability partnership.

KELT EXPLORATION LTD.
STATEMENT OF FINANCIAL POSITION

(CA$ thousands)	[Notes]	**December 31, 2014**	December 31, 2013
ASSETS			
Current assets			
Cash and cash equivalents		**1,049**	32,015
Accounts receivable and accrued revenue	[14]	**35,092**	13,082
Prepaid expenses and deposits		**2,839**	1,240
Derivative financial instruments	[14]	**1,745**	-
Assets held for sale	[6]	**-**	19,635
Total current assets		**40,725**	65,972
Deferred income tax asset	[13]	**-**	1,957
Exploration and evaluation assets	[7]	**79,294**	40,564
Property, plant and equipment	[8]	**770,484**	376,708
Goodwill	[9]	**18,206**	-
Total assets		**908,709**	485,201
LIABILITIES			
Current liabilities			
Accounts payable and accrued liabilities		**96,776**	43,447
Derivative financial instruments	[14]	**-**	532
Deferred premium on flow-through shares	[12]	**692**	1,181
Decommissioning obligations	[11]	**758**	312
Total current liabilities		**98,226**	45,472
Bank debt	[10]	**46,929**	-
Decommissioning obligations	[11]	**94,033**	46,857
Deferred income tax liability	[13]	**49,882**	-
Total liabilities		**289,070**	92,329
SHAREHOLDERS' EQUITY			
Shareholders' capital	[12]	**657,102**	449,876
Reserve from common control transaction	[4]	**(57,668)**	(57,668)
Contributed surplus		**14,692**	5,779
Retained earnings (deficit)		**5,513**	(5,115)
Total shareholders' equity		**619,639**	392,872
Total liabilities and shareholders' equity		**908,709**	485,201

Acquisitions	[5]
Commitments	[16]
Subsequent events	[19]

The accompanying notes form an integral part of these financial statements.

On behalf of the Board of Directors:

[signed]
David J. Wilson, Director

[signed]
Neil G. Sinclair, Director

KELT EXPLORATION LTD.
STATEMENT OF PROFIT (LOSS) AND COMPREHENSIVE INCOME (LOSS)

		Year ended December 31	
(CA$ thousands, except per share amounts)	[Notes]	**2014**	2013
Revenue			
Oil and gas sales		**214,691**	46,656
Royalties		**(28,433)**	(6,321)
		186,258	40,335
Expenses			
Production		**55,901**	11,358
Transportation		**10,719**	4,090
Financing	[15]	**2,521**	329
General and administrative		**3,631**	1,660
Share based compensation	[12]	**9,033**	5,779
Depletion and depreciation		**84,418**	23,337
Exploration and evaluation	[7]	**377**	114
		166,600	46,667
Profit (loss) before other items and taxes		**19,658**	(6,332)
Interest income		**938**	1,095
Transaction costs	[5,6]	**(234)**	(233)
Premium on flow-through shares	[12]	**4,211**	2,419
Gain (loss) on derivative financial instruments	[14]	**1,889**	(883)
Profit (loss) before taxes		**26,462**	(3,934)
Deferred income tax expense	[13]	**15,834**	1,181
Profit (loss) and comprehensive income (loss)		**10,628**	(5,115)
Profit (loss) per common share			
Basic	[12]	**0.09**	(0.07)
Diluted	[12]	**0.09**	(0.07)

The accompanying notes form an integral part of these financial statements.

KELT EXPLORATION LTD.
STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY

(CA$ thousands)	[Notes]	Shareholders' capital	Reserve	Contributed surplus	Retained earnings (deficit)	Total shareholders' equity
Balance at December 31, 2013		**449,876**	**(57,668)**	**5,779**	**(5,115)**	**392,872**
Profit (loss) and comprehensive income (loss)					**10,628**	**10,628**
Common shares issued:						**-**
Private placements	[12]	**148,988**				**148,988**
Less: deferred premium on flow-through shares	[12]	**(3,722)**				**(3,722)**
Pursuant to corporate acquisition	[5]	**66,243**				**66,243**
Share issue costs, net of tax	[12]	**(4,694)**				**(4,694)**
Exercise of stock options	[12]	**411**		**(120)**		**291**
Share based compensation	[12]			**9,033**		**9,033**
Balance at December 31, 2014		**657,102**	**(57,668)**	**14,692**	**5,513**	**619,639**

Balance at December 31, 2012		-	-	-	-	-
Profit (loss) and comprehensive income (loss)					(5,115)	(5,115)
Common shares issued, net of costs:						
Pursuant to the Arrangement	[4,12]	141,961	(57,668)			84,293
Private placements	[12]	320,930				320,930
Less: deferred premium on flow-through shares	[12]	(3,600)				(3,600)
Share issue costs, net of tax	[12]	(9,415)				(9,415)
Share based compensation	[12]			5,779		5,779
Balance at December 31, 2013		449,876	(57,668)	5,779	(5,115)	392,872

The accompanying notes form an integral part of these financial statements.

KELT EXPLORATION LTD.
STATEMENT OF CASH FLOWS

		Year ended December 31	
(CA$ thousands)	[Notes]	**2014**	2013
Operating activities			
Profit (loss)		**10,628**	(5,115)
Items not affecting cash:			
Accretion of decommissioning obligations	[11,15]	**1,701**	247
Share based compensation		**9,033**	5,779
Depletion and depreciation		**84,418**	23,337
Exploration and evaluation		**377**	114
Premium on flow-through shares		**(4,211)**	(2,419)
Unrealized (gain) loss on derivative financial instruments	[14]	**(2,277)**	304
Deferred income tax expense		**15,834**	1,181
Cash premium on derivatives		**-**	228
Settlement of decommissioning obligations	[11]	**(229)**	-
Change in non-cash operating working capital	[17]	**(2,883)**	3,235
Cash provided by operating activities		**112,391**	26,891
Financing activities			
Increase in bank debt		**46,929**	-
Issue of common shares	[12]	**148,988**	301,330
Proceeds on exercise of stock options	[12]	**291**	19,600
Share issue costs		**(6,267)**	(12,553)
Cash provided by financing activities		**189,941**	308,377
Investing activities			
Pursuant to the Arrangement	[4]	**-**	(23,247)
Exploration and evaluation assets		**(101,524)**	(46,717)
Property, plant and equipment		**(149,723)**	(49,735)
Property acquisitions	[5]	**(24,714)**	(209,444)
Property dispositions	[6]	**19,635**	-
Corporate acquisition	[5]	**(104,663)**	-
Change in non-cash investing working capital	[17]	**27,691**	25,890
Cash used in investing activities		**(333,298)**	(303,253)
Net change in cash and cash equivalents		**(30,966)**	32,015
Cash and cash equivalents, beginning of period		**32,015**	-
Cash and cash equivalents, end of period		**1,049**	32,015

The accompanying notes form an integral part of these financial statements.

(All tabular amounts in thousands of Canadian dollars, except as otherwise indicated)

1. DESCRIPTION OF THE BUSINESS

Kelt Exploration Ltd. ("Kelt" or the "Company") was incorporated under the *Business Corporations Act* (Alberta) on October 11, 2012 as 1705972 Alberta Ltd. and was inactive until February 26, 2013. On October 19, 2012, Articles of Amendment were filed to change the name of the Company to Kelt Exploration Ltd. The head office of Kelt is located at Suite 300, 311 – 6th Avenue S.W., Calgary, Alberta T2P 3H2.

Kelt is an oil and gas company based in Calgary, Alberta, focused on the exploration, development and production of crude oil and natural gas resources, primarily in west central Alberta and northeastern British Columbia. The Company is a single reporting entity and does not have any subsidiaries. Common shares of the Company are listed and posted for trading on the Toronto Stock Exchange ("TSX") under the symbol "KEL".

Additional information relating to Kelt can be found on SEDAR at www.sedar.com.

2. BASIS OF PRESENTATION

a) Statement of compliance

These audited annual financial statements have been prepared in accordance with Canadian generally accepted accounting principles ("GAAP") as set out in the CPA Canada Handbook – Accounting ("CPA Handbook"). The CPA Handbook incorporates International Financial Reporting Standards ("IFRS") and publicly accountable enterprises, such as Kelt, are required to apply such standards.

These audited annual financial statements were approved and authorized for issue by the Company's Board of Directors on March 9, 2015.

b) Basis of measurement

All references to dollar amounts in these financial statements and related notes are thousands of Canadian dollars, unless otherwise indicated.

These financial statements have been prepared on a historical cost basis, except for certain financial instruments which are recorded at fair value. The methods used to measure fair values are described in note 14 of these financial statements.

c) Significant judgments and estimates

The timely preparation of the financial statements requires management to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amount of assets, liabilities, income and expenses. Actual results may differ materially from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimates are reviewed and for any future years affected. Significant judgments, estimates and assumptions made by management in these financial statements are discussed below.

Common control transaction

In connection with the Arrangement and pursuant to the terms of the Conveyance Agreement, the Celtic Assets were transferred from Celtic to Kelt and Kelt assumed certain obligations and liabilities of Celtic. Kelt was a wholly owned subsidiary of Celtic immediately preceding closing of the Arrangement and immediately subsequent to closing, Kelt was controlled by the same shareholders as Celtic; consequently, the entities were under common control at the time the Celtic Assets were transferred. Business combinations involving entities under common control are outside the scope of IFRS 3 *Business Combinations*. IFRS provides no guidance on the accounting for these types of

transactions and an entity is required to develop an accounting policy. The three most common methods utilized are the purchase method, the predecessor values since inception method, and the predecessor values from date of transaction method. A business combination involving entities under common control is a business combination in which all of the combining entities are ultimately controlled by the same party, both before and after the business combination, and control is not transitory. Management has determined the predecessor values from date of transaction method to be most appropriate. This method requires the financial statements to be prepared using the predecessor carrying values without any step up to fair value. The difference between any consideration and the aggregate carrying value of the assets and liabilities is recorded as a reserve from common control transaction in shareholders' equity.

Assets held for sale

The decision to classify a non-current asset or disposal group as held for sale requires judgment to determine if the carrying amount will be recovered through a sale transaction rather than through continuing use. In order to draw this conclusion, management must assert that the asset or disposal group is available for immediate sale in its present condition and believe that it is highly probable that a sale transaction will be completed within one year of designating the asset as held for sale. As more particularly described in note 6 of the financial statements, estimates and assumptions are also required to measure the assets held for sale at their fair value less costs of disposal.

Depletion, depreciation and reserves

The Company calculates depletion based on total proved reserves as determined in accordance with the Canadian Oil and Gas Evaluation Handbook ("COGEH"). The process of determining reserves is complex. Significant judgments are based on available geological, geophysical, engineering, and economic data. These judgments are based on estimates and assumptions that may change substantially as additional data from ongoing development activities and production performance becomes available and as economic conditions impacting oil and gas prices and costs change. The reserve estimates are based on current production forecasts, prices and economic conditions. As circumstances change and additional data becomes available, reserve estimates also change. Estimates made are reviewed and revised, either upward or downward, as warranted by the new information. Revisions are often required due to changes in well performance, prices, economic conditions and governmental restrictions.

Although every reasonable effort is made to ensure that reserve estimates are accurate, reserve estimation can be impacted by subjective decisions, new geological or production information and a changing environment. In addition, revisions to reserve estimates can arise from changes in forecast oil and gas prices and reservoir performance. Such revisions can be either positive or negative.

Changes in reserve estimates impact the financial results of the Company as reserves and estimated future development costs are used to calculate depletion. Reserves are used in measuring the fair value less costs of disposal ("FVLCD") of property, plant and equipment ("PP&E") for impairment calculations and for determining the fair value of PP&E acquired in a business combination. Reserves also impact the Company's assessment of the commercial viability and technical feasibility of an exploration project and the decision to transfer exploration and evaluation ("E&E") assets to PP&E.

Determination of Cash Generating Units ("CGUs")

The determination of CGUs requires judgment in defining a group of assets that generate cash inflows that are largely independent of the cash inflows from other assets or groups of assets. CGUs are determined by similar geological structure, shared infrastructure, geographical proximity, commodity type, similar exposure to market risks and materiality.

Impairment of non-financial assets

Significant judgment is required to assess the Company's non-financial assets, namely PP&E, E&E and goodwill, for impairment. Management must first determine whether indicators of impairment exist that suggest the carrying value may not be recoverable through the asset's continued use or sale. As a result of a significant decline in current and forecast oil and natural gas prices, an indication of potential impairment was identified and the Company was required to perform a formal impairment test and calculate the recoverable amount as at December 31, 2014.

Significant judgment and estimates are required to calculate the recoverable amount in an impairment test. Management calculated the recoverable amount of each CGU based on its FVLCD, using an after-tax discounted cash flow analysis derived from proved plus probable reserves. Reserve estimates and expected future cash flows from production of reserves are subject to measurement uncertainty as discussed above and are subject to variability due to changes in forecasted commodity prices. In addition, the present value of forecast future cash flows is highly sensitive to the discount rate. Judgment is required to determine an appropriate discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. Refer to note 8 of the financial statements for a discussion of the specific estimates and assumptions applied in the calculation of the recoverable amount. For the purpose of impairment testing, goodwill is allocated to the CGU expected to benefit from the business combination.

Exploration and evaluation assets

The decision to transfer assets from E&E to PP&E requires judgment as it is based on estimated proved reserves, which are used, in part, to determine a project's technical feasibility and commercial viability. Judgment is also required to determine the level at which E&E is assessed for impairment; for Kelt, the recoverable amount of E&E assets is assessed at the operating segment level.

Decommissioning obligations

The Company estimates the decommissioning obligations for oil and gas wells and their associated production facilities and infrastructure. In most instances, dismantling of assets and remediation occurs many years into the future. The value of the ultimate decommissioning obligation can fluctuate in response to many factors including changes to relevant legal requirements, the emergence of new restoration techniques, experience at other production sites, and changes to the risk-free discount rate. The expected timing and amount of expenditure can also change, for example, in response to changes in reserves or changes in laws and regulations or their interpretation. Judgments include the most appropriate discount rate to use, which management has determined to be a risk-free rate.

Kelt estimates abandonment and reclamation costs based on a combination of publically available industry benchmarks and internal site specific information. For producing wells and facilities, the expected timing of settlement is estimated based on the proved plus probable period to abandonment for each field, as per the independent reserve report. For non-producing wells, the expected timing of settlement is estimated to be half of the period applied to producing wells in that field, unless the timing to abandon and reclaim a specific well site or facility is known based on budgeted expenditures.

Business combinations

Business combinations are accounted for using the acquisition method of accounting. The determination of fair value often requires management to make assumptions and estimates about future events. The assumptions and estimates with respect to determining the fair value of exploration and evaluation assets and property, plant and equipment acquired generally require the most judgment and include estimates of reserves acquired, forecast benchmark commodity prices and discount rates. Assumptions are also required to determine the fair value of decommissioning obligations associated with the properties. Changes in any of these assumptions or estimates used in determining the fair value of acquired assets and liabilities could impact the amounts assigned to assets, liabilities and goodwill (or gain from a bargain purchase) in the acquisition equation. Future profit (loss) can be affected as a result of changes in future depletion and depreciation or impairment.

Deferred income taxes

The Company follows the liability method for calculating deferred income taxes. Tax interpretations, regulations and legislation in the jurisdictions in which the Company operates are subject to change. As such, deferred income taxes are subject to measurement uncertainty. Deferred income tax assets are assessed by management at the end of the reporting period to determine the likelihood that they will be realized from future taxable earnings. Given the Company had a net deferred income tax liability as at December 31, 2014, judgment with respect to the recoverability of deferred income tax assets was not required in the current reporting period. The provision for deferred income taxes also includes the following significant judgments of management:

- Classification of intangible drilling and completion costs as Canadian exploration expenses ("CEE") or Canadian

development expenses (“CDE”) – CEE is deductible at a rate of 100% per year, whereas CDE may be deducted on a declining basis at 30% per year. Accordingly, the allocation of resource deductions will impact the period in which Kelt may become taxable in the future. In addition, the designation of certain expenditures as CEE and/or CDE impacts the Company’s ability to satisfy its flow-through share obligations; and

- Recognition of unrecognized deferred income tax asset – per IAS 12, deferred income taxes are not initially recognized on transactions that are not business combinations. The unrecognized deferred income tax asset that arose on the Common Control Transaction is being amortized based on the corporate weighted average depletion factor for the period.

Share based compensation

The Company uses the fair value method of accounting for its long-term incentive plans, which include an Incentive Stock Option Plan and a Restricted Share Unit Plan. Judgments include which valuation model is most appropriate for the grant of the award to estimate its fair value. Estimates and assumptions are then used in the valuation model to determine fair value.

For stock options, the Company uses the Black-Scholes option pricing model which requires that management make assumptions for the expected life of the option, the anticipated volatility of the share price over the life of the option, the risk-free interest rate for the life of the option, and the number of options that will ultimately vest. The assumptions used by the Company are discussed in note 12.

The fair value of restricted share units is estimated based on the volume weighted average trading price on the TSX over three trading days immediately prior to the date of grant. Judgment is also required to estimate the number of restricted share units that will ultimately vest. The assumptions used by the Company are discussed in note 12.

Flow-through shares

There is no IFRS guidance that specifically addresses accounting for flow-through shares, therefore the Company is required to develop an accounting policy. The two most common methods are the residual method and the relative fair value method. The Company has applied the residual method to appropriately reflect the substance transaction. Under the residual method, the proceeds from the issuance are allocated between i) the proceeds of the offering of shares, and ii) the renunciation of tax deductions. At the time the flow-through shares are issued: i) shareholders’ capital is credited based on the fair value of ordinary common shares, and ii) the tax deductions to be renounced are deferred and presented as a liability in the Statement of Financial Position, at an amount equal to the residual difference between the fair value of the Company’s ordinary common shares relative to the amount the investor pays for the flow-through shares.

Determination of the fair value of ordinary shares requires judgment. Typically, it is based on the share price at the time the parties agree to the transaction, which is generally at a date earlier than closing. If there are significant changes in the share price between the date the parties agree to the offering and closing, additional judgment may be required.

Judgment is also required to determine when the Company has fulfilled its obligation to pass on the tax deduction to investors, at which time, the premium on flow-through shares is recognized in income. The Company deems the obligation to have been fulfilled in the period that eligible expenditures are incurred, regardless of the period in which the tax deductions are legally renounced. This is based on the view that the renunciation is perfunctory and that the accounting should be reflected when the expenditure is made.

3. SIGNIFICANT ACCOUNTING POLICIES

Joint Interests

A substantial portion of the Company’s exploration, development and production activities is conducted jointly with others through unincorporated joint ventures. These financial statements reflect only the Company’s proportionate interest of these jointly controlled assets and the proportionate share of the relevant revenue and related costs.

Foreign currency translation

The financial statements are presented in Canadian dollars, which is the Company's functional and presentation currency. Transactions in foreign currencies are initially recorded at the exchange rate in effect at the time of the transactions. Monetary assets and liabilities denominated in foreign currencies are translated to Canadian dollars using the closing exchange rate at the Statement of Financial Position date. The resulting exchange rate differences are included in the Statement of Profit and Comprehensive Income.

Business combinations

Business combinations are accounted for using the acquisition method. The identifiable net assets acquired are measured at their fair value at the date of acquisition. Any excess of the purchase price over the fair value of the net assets acquired is recognized as goodwill. Any deficiency of the purchase price below the fair value of the net assets acquired is recorded as a gain in the Statement of Profit and Comprehensive Income. Transaction costs associated with the acquisition are expensed when incurred.

Common control transaction

Business combinations involving entities under common control are outside the scope of IFRS 3 *Business Combinations*. IFRS provides no guidance on the accounting for these types of transactions and an entity is required to develop an accounting policy. The three most common methods utilized are the purchase method, the predecessor values since inception method, and the predecessor values from date of transaction method. A business combination involving entities under common control is a business combination in which all of the combining entities are ultimately controlled by the same party, both before and after the business combination, and control is not transitory. Management has determined the predecessor values from date of transaction method to be most appropriate. This method requires the financial statements to be prepared using the predecessor carrying values without any step up to fair value. The difference between any consideration and the aggregate carrying value of the assets and liabilities are recorded as a reserve from common control transaction in shareholders' equity. Transaction costs associated with a common control transaction are recognized as an expense in the period.

Assets held for sale

Non-current assets and disposal groups are classified as held for sale if their carrying amounts will be recovered through a sale transaction rather than through continuing use. This condition is regarded as met only when the sale is highly probable and the asset or disposal group is available for immediate sale in its present condition subject only to terms that are usual and customary for sales of such assets. Management must be committed to the sale, which should be expected to qualify for recognition as a completed sale within one year from the date of classification as held for sale. Non-current assets and disposal groups classified as held for sale are measured at the lower of the carrying amount and fair value less costs of disposal, and depletion & depreciation ceases at the time this designation is made.

If a non-current asset or disposal group has been classified as held for sale, but subsequently ceases to meet the criteria to be classified as held for sale, the Company ceases to classify the asset or disposal group as held for sale. Non-current assets and disposal groups that cease to be classified as held for sale are measured at the lower of carrying amount before the asset or disposal group was classified as held for sale (adjusted for any depreciation, amortization or revaluation that would have been recognized had the asset or disposal group not been classified as held for sale) and its recoverable amount at the date of the subsequent decision not to sell. Any adjustment to the carrying amount is recognized in profit or loss in the period in which the asset ceases to be classified as held for sale.

Financial instruments

Financial assets and liabilities are recognized when the Company becomes a party to the contractual provisions of the instrument. Financial assets are derecognized when the rights to receive cash flows from the assets have expired or have been transferred and the Company has transferred substantially all risks and rewards of ownership.

Financial assets and liabilities are offset and the net amount is reported in the Statement of Financial Position when there is a legally enforceable right to offset the recognized amounts and there is an intention to settle on a net basis, or realize the asset and settle the liability simultaneously.

At initial recognition, the Company classifies its financial instruments in the following categories depending on the purpose for which the instruments were acquired:

i) Financial assets and liabilities at fair value through profit or loss

A financial asset or liability is classified in this category if acquired principally for the purpose of selling or repurchasing in the short-term. Derivatives are also included in this category unless they are designated as hedges.

Financial instruments in this category are recognized initially and subsequently at fair value. Transaction costs are expensed in the Statement of Profit and Comprehensive Income. Gains and losses arising from changes in fair value are presented in profit or loss in the period in which they arise.

Financial assets and liabilities at fair value through profit or loss are classified as current in the Statement of Financial Position, except for any portion expected to be realized or paid beyond twelve months of the Statement of Financial Position date.

ii) Available-for-sale investments

Available-for-sale investments are non-derivatives that are either designated in this category or not classified in any of the other categories. The Company does not currently hold any available-for-sale investments.

iii) Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. The Company's loans and receivables are comprised of cash and cash equivalents, accounts receivable and deposits. They are included in current assets due to their short-term nature.

Loans and receivables are initially recognized at the amount expected to be received less any required discount to reduce the loans and receivables to fair value. Subsequently, loans and receivables are measured at amortized cost using the effective interest method less any provision for impairment.

iv) Financial liabilities at amortized cost

Financial liabilities at amortized cost include accounts payable and bank debt. Accounts payable are initially recognized at the amount required to be paid less any required discount to reduce the payables to fair value. Bank debt is recognized initially at fair value, net of any transaction costs incurred, and subsequently at amortized cost using the effective interest method. Financial liabilities are classified as current liabilities if payment is due within twelve months. Otherwise, they are presented as non-current liabilities.

v) Derivative financial instruments

The Company may use derivative financial instruments for risk management purposes. All derivatives have been classified at fair value through profit or loss. Financial instruments are included on the Statement of Financial Position within derivative financial instruments and are classified as current or non-current based on the contractual terms specific to the instrument. Gains and losses on re-measurement of derivatives are included in profit or loss in the period in which they arise.

Exploration and evaluation assets ("E&E") and Property, plant and equipment ("PP&E")

i) Recognition and measurement

Pre-license costs

Costs incurred prior to acquiring the legal rights to explore an area are charged directly to profit or loss as exploration expense in the period incurred. The Company did not incur pre-license costs in the current or prior period.

Exploration and evaluation assets

All costs directly associated with the exploration and evaluation of petroleum and natural gas reserves are initially capitalized. Exploration and evaluation costs include unproved property acquisition costs such as undeveloped land and mineral leases, geological and geophysical costs, and costs associated with exploratory drilling, sampling and

appraisals.

The costs are accumulated by field or exploration area pending determination of technical feasibility and commercial viability. The technical feasibility and commercial viability is considered to be achieved when proved reserves are determined to exist. Prior to being transferred to PP&E, E&E costs are first tested for impairment. If proved/probable reserves have not been established through the completion of exploration and evaluation activities and there are no future plans for activity in that field, then the costs are determined to be impaired and the amounts are charged to the Statement of Profit and Comprehensive Income.

Such costs are not subject to depletion or depreciation until they are reclassified from E&E to PP&E.

Property, plant and equipment

Property, plant, and equipment primarily consists of petroleum and natural gas development and production assets, and is measured at cost less accumulated depletion and depreciation and accumulated impairment losses. These costs include property acquisitions, development drilling, completion, gathering and infrastructure, estimated decommissioning costs and transfers from E&E. In addition, borrowing costs incurred for the construction of qualifying assets are capitalized during the period of time that is required to complete and prepare the assets for their intended use.

ii) Subsequent costs

Costs incurred subsequent to the determination of technical feasibility and commercial viability and the costs of replacing components of equipment are recognized as property, plant and equipment only when they increase the future economic benefits embodied in the specific asset to which they relate. All other expenditures are expensed as incurred. Such capitalized amounts generally represent costs incurred in developing proved and/or probable reserves and bringing in or enhancing production from such reserves. The carrying amount of any replaced or sold component is derecognized.

The gain or loss from the divestitures of property, plant and equipment is recognized in the Statement of Profit and Comprehensive Income. In addition, risk-sharing agreements in which the Company cedes a portion of its working interest to a third-party are generally considered to be disposals of property, plant and equipment, potentially resulting in a gain or loss on disposition.

Exchanges of assets within property, plant and equipment are measured at fair value unless the exchange transaction lacks commercial substance or the fair value of neither the asset received nor the asset given up is reliably measurable. Unless the fair value of the asset received is more clearly evident, the cost of the acquired asset is measured at the fair value of the asset given up. Where fair value is not used, the cost of the acquired asset is measured at the carrying amount of the asset given up. The gain or loss on derecognition of the asset given up is recognized in profit or loss.

An asset within property, plant and equipment is derecognized upon disposal or when no future economic benefits are expected to arise from the continued use of the asset. Any gain or loss arising on derecognition of the asset (calculated as the difference between the net disposal proceeds and the carrying value of the asset) is included in profit or loss in the period in which the item is derecognized.

iii) Depletion and depreciation

Development and production costs are accumulated on a field or geotechnical area basis (“depletion units”). The net carrying value of each depletion unit is depleted using the unit of production method by reference to the ratio of production in the year to the related proved reserves, taking into account estimated future development costs necessary to bring those reserves into production. Future development costs are estimated taking into account the level of development required to produce the reserves. These estimates are reviewed by independent reserve engineers at least annually. Where significant components of development or production assets have different useful lives, they are accounted for and depreciated as separate items of property, plant and equipment.

Impairment of assets

Non-financial assets

The Company reviews the carrying value of its non-financial assets, including PP&E and E&E, on a quarterly basis to determine whether there is any indication of impairment. Goodwill is evaluated when facts and circumstances indicate that it is impaired, or at least on an annual basis. If any such indication exists, then the asset's recoverable amount is estimated. E&E assets are also assessed for impairment prior to being reclassified to PP&E.

For the purpose of impairment testing, assets are grouped together into the smallest group of assets that generates cash inflows from continuing use that are largely independent of the cash inflows of other assets or CGUs. The recoverable amount of an asset or a CGU is the greater of its value in use and its fair value less costs of disposal ("FVLCD"). Goodwill is allocated to the CGU expected to benefit from the business combination. E&E assets are assessed for impairment at the operating segment level.

FVLCD is defined as the amount obtainable from the sale of an asset or cash generating unit in an arm's length transaction between knowledgeable, willing parties, less the costs of disposal. The Company calculates FVLCD by reference to the after-tax future cash flows expected to be derived from production of proved plus probable reserves, less estimated selling costs. The estimated after-tax future cash flows are discounted to their present value using a discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. Value in use is generally computed by reference to the present value of the future cash flows expected to be derived from production of proved reserves.

An impairment loss is recognized if the carrying amount of an asset or its CGU exceeds its estimated recoverable amount. Impairment losses are recognized in the Statement of Profit and Comprehensive Income. Impairment losses recognized in respect of CGUs are allocated to reduce the carrying amounts of the assets in the CGU on a pro rata basis.

Impairment losses recognized in prior years are assessed at each reporting date for any indication that the loss has decreased or no longer exists. An impairment loss is reversed if there has been a change in the estimate used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depletion and depreciation, if no impairment loss had been recognized.

Financial assets

A financial asset is assessed at each reporting date to determine whether there is any objective evidence that it is impaired. A financial asset is considered to be impaired if objective evidence indicates that one or more events have had a negative effect on the fair value or estimated future cash flows of an asset.

An impairment loss in respect of a financial asset measured at amortized cost is calculated as the difference between its carrying amount and the present value of the estimated future cash flows discounted at the original effective interest rate. Individually significant financial assets are tested for impairment on an individual basis. The remaining financial assets are assessed collectively in groups that share similar credit risk characteristics.

All impairment losses are recognized in profit or loss. An impairment loss is reversed if the reversal can be related objectively to an event occurring after the impairment loss was recognized. For financial assets measured at amortized cost the reversal is recognized in profit or loss.

Goodwill

The Company records goodwill relating to a business combination when the consideration paid exceeds the fair value of the net identifiable assets and liabilities of the acquired business. Goodwill is reported at cost less any impairment and is not amortized. Goodwill is evaluated when facts and circumstances indicate that it is impaired, or at least on an annual basis. Goodwill impairments are not reversed.

Leases

Leases where the Company assumes substantially all the risks and rewards of ownership are classified as finance

leases. Upon initial recognition, the leased asset is measured at an amount equal to the lower of its fair value and the present value of the minimum lease payments. Subsequent to initial recognition, the asset is accounted for in accordance with the accounting policy applicable to that asset. Minimum lease payments made under finance leases are apportioned between the finance expenses and the reduction of the outstanding liability. The finance expenses are allocated to each year during the lease term so as to produce a constant periodic rate of interest on the remaining balance of the liability. The Company does not currently have any finance leases.

All of the Company's leases are operating leases, which are not recognized on the Statement of Financial Position. Rather, payments in respect of operating leases are recognized in the Statement of Profit and Comprehensive Income on a straight-line basis over the term of the lease. In the event that lease inducements are received to enter into operating leases, such inducements are recognized as a deferred credit. The aggregate benefit of inducements is recognized as a reduction of the related rental expense on a straight-line basis, except where another systematic basis is more representative of the time pattern in which economic benefits from the leased asset are consumed.

Provisions and Contingencies

Provisions are recognized when the Company has a present obligation as a result of a past event, if it is probable that an outflow of resources will be required and if a reliable estimate can be made of the amount of the obligation. Provisions are measured based on the best estimate of discounted future cash outflows.

Decommissioning obligations

The Company's activities give rise to dismantling, decommissioning and site disturbance remediation activities. An obligation is accrued for the estimated cost of site restoration and the corresponding amount is included in the cost of the assets to which the obligations relate. Decommissioning obligations are measured at the present value of management's best estimate of the expenditure required to settle the present obligation at the Statement of Financial Position date. Subsequent to the initial measurement, the obligation is adjusted at the end of each period to reflect the passage of time and changes in the estimated future cash flows underlying the obligation, changes to the expected timing of site restoration, as well as any changes in the risk-free discount rate. Increases in the provision due to the passage of time are recognized as a financing expense in the Statement of Profit and Comprehensive Income whereas increases/decreases due to changes in the estimated future cash flows are capitalized. Actual costs incurred upon settlement of the decommissioning obligations are charged against the provision to the extent the provision is established.

Contingencies

Contingent liabilities are possible obligations whose existence will only be confirmed by future events not wholly within the control of the Company. When a contingency is substantiated by confirming events, can be reliably measured and will likely result in an economic outflow, a liability is recognized in the financial statements as the best estimate required to settle the obligation. A contingent liability is disclosed where the existence of an obligation will only be confirmed by future events, or where the amount of a present obligation cannot be measured reliably or will likely not result in an economic outflow.

Contingent assets are only disclosed when the inflow of economic benefits is probable. When the economic benefit becomes virtually certain, the asset is no longer contingent and is recognized in the financial statements.

Income taxes

Total income tax expense is composed of both current and deferred income taxes.

Current tax is the expected tax payable on taxable income for the year, using tax rates enacted or substantively enacted at the reporting date, and any adjustment to tax payable in respect of previous years.

The Company follows the liability method of accounting for income taxes. Under this method, deferred income tax is recognized in respect of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred taxes are allocated between income and equity depending on the nature of the account balance or transaction that gives rise to the temporary difference.

Deferred tax liabilities are recognized for taxable temporary differences. Deferred tax assets are recognized for

deductible temporary differences, unused tax losses and unused tax credits only if it is probable that sufficient future taxable income will be available to utilize those temporary differences and losses. Such deferred tax liabilities and assets are not recognized if the temporary difference arises from goodwill or from the initial recognition of an asset or liability in a transaction which is not a business combination and, at the time of the transaction, affects neither accounting profit nor taxable income. Deferred tax is measured at the tax rates that are expected to be applied to temporary differences when they reverse, based on the laws that have been enacted or substantively enacted by the reporting date. The effect of a change in income tax rates on deferred tax assets and liabilities is recognized in the Statement of Profit and Comprehensive Income in the period that the change occurs.

Deferred tax assets and liabilities are offset if there is a legally enforceable right to offset current tax liabilities and assets, and they relate to income taxes levied by the same tax authority on the same taxable entity or on different tax entities but they intend to settle current tax liabilities and assets on a net basis or their tax assets and liabilities will be realized simultaneously. Deferred tax assets and liabilities are recorded on a non-discounted basis.

Revenue recognition

Revenue from the sale of oil and natural gas is recorded when the significant risks and rewards of ownership of the product are transferred to the buyer which is usually when legal title passes to the external party and collectability is reasonably assured. This is generally at the time product enters the pipeline. Royalties, which are presented as a reduction in revenue in the Statement of Profit and Comprehensive Income, are recognized at the time of production. Net revenues earned from properties in which the Company shares a joint interest, are recognized proportionately based on the Company's working interest in those properties.

Royalty income is recognized as it accrues in accordance with the terms of the overriding royalty agreements.

Financing expense

Financing expenses include interest expense on borrowings and accretion of the discount on decommissioning obligations due to the passage of time.

Borrowing costs incurred for the construction of qualifying assets are capitalized during the period of time required to complete and prepare the assets for their intended use. All other borrowing costs are recognized in financing expense using the effective interest method.

Share based compensation

The Company has an Incentive Stock Option Plan and Restricted Share Unit Plan (collectively, the "Plans"). Pursuant to the Plans, stock options and restricted share units ("RSUs") may be granted to officers, directors, employees and certain consultants, which call for settlement through the issuance of new common shares of the Company.

The Company applies the fair value method of accounting for stock options, whereby each tranche in an award is valued separately on the grant date using the Black-Scholes option pricing model. The fair value of RSUs is calculated based on the volume weighted average trading price over three trading days immediately prior to the date of grant. The total fair value associated the stock options and RSUs is recognized over the service period using graded vesting, as share based compensation expense with a corresponding increase to contributed surplus. An estimated forfeiture rate is applied against the total fair value on the grant date and is adjusted to reflect the actual number of options that ultimately vest each period. The consideration received by the Company on the exercise of stock options is recorded as an increase in shareholders' capital, together with the corresponding amounts previously recognized in contributed surplus.

Flow-through shares

Canadian tax legislation permits entities meeting specified criteria to issue securities to investors whereby the deductions for tax purposes related to eligible expenditures may be claimed by the investors rather than by the entity (hereinafter referred to as "flow-through shares"). The Company uses the residual method to account for flow-through shares. Under this method, the proceeds from the issuance are allocated between i) the proceeds of the offering of shares, and ii) the renunciation of tax deductions. At the time the flow-through shares are issued: i) shareholders' capital is credited based on the fair value of ordinary common shares, and ii) the tax deductions to be renounced are deferred and presented a liability in the Statement of Financial Position, at an amount equal to the residual difference

between the fair value of the Company's ordinary common shares relative to the amount the investor pays for the flow-through shares. At the time the Company fulfills its obligation to pass on the tax deductions to investors, which is deemed to occur when the eligible expenditures are incurred, the liability (deferred premium) is drawn down in proportion to the eligible expenditures incurred in the period and the premium on flow-through shares is recognized as income in the Statement of Profit and Comprehensive Income. Concurrently, a deferred income tax liability is recognized for the taxable temporary difference that arises from the difference between the carrying amount of the eligible expenditures capitalized as an asset for accounting purposes and a tax base of nil, because the deduction has been renounced to investors.

Per share amounts

Basic profit (loss) per common share is calculated by dividing profit (loss) for the period attributable to common shareholders of the Company by the weighted average number of common shares outstanding during the period. Common shares issued as part of the consideration transferred in a business combination or common control transaction are included in the weighted average number of common shares starting from the acquisition date.

Diluted profit (loss) per common share is calculated giving effect to the potential dilution that would occur if all outstanding "in-the-money" stock options were exercised or converted to common shares. The weighted average number of common shares outstanding during the period is adjusted by the incremental number of shares calculated in accordance with the treasury stock method. The treasury stock method assumes that the proceeds received from the exercise of all potentially dilutive instruments are used to repurchase common shares at the volume weighted average market price during the period.

New or amended IFRSs effective January 1, 2014

IAS 32 *Financial Instruments: Presentation,* has been amended to clarify 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 upon a future event. The adoption of this amendment did not impact the Company's financial statements.

IAS 36 *Impairment of Assets,* has been amended to require additional disclosures in the event of recognizing an impairment of assets. The Company did not recognize an impairment of assets as at or during the year ended December 31, 2014 and as a result, the adoption of this amendment did not impact the Company's financial statement disclosures.

Effective January 1, 2014, the Company retrospectively adopted International Financial Reporting Interpretation Committee ("IFRIC") 21 *Levies.* IFRIC 21 clarified that an entity recognizes a liability for a levy when the activity that triggers payment occurs. For a levy that is triggered upon reaching a minimum threshold, the interpretation clarified that no liability should be anticipated before the minimum threshold is reached. The adoption of this interpretation did not have an impact on the Company's financial statements.

Accounting standards issued but not yet effective

IFRS 15 *Revenue from Contracts with Customers,* provides clarification for recognizing revenue from contracts with customers and establishes a single revenue recognition and measurement framework that applies to contracts with customers. The new standard is effective for annual periods beginning on or after January 1, 2017, with early adoption permitted. Management is currently assessing the potential impact of the adoption of IFRS 15 on the Company's financial statements.

IFRS 9 *Financial Instruments*, is intended to replace IAS 39 *Financial Instruments: Recognition and Measurement* and uses a single approach to determine whether a financial asset is measured at amortized cost or fair value, replacing the multiple rules in IAS 39. For financial liabilities designated at fair value through profit or loss, a company can recognize the portion of the change in fair value related to the change in the company's own credit risk through other comprehensive income rather than profit or loss. The new standard also requires a single impairment method to be used, replacing the multiple impairment methods in IAS 39, and incorporates new hedge accounting requirements. The new standard is effective for annual periods beginning on or after January 1, 2018, with early adoption permitted. Management is currently assessing the potential impact of the adoption of IFRS 9 on the Company's financial statements.

4. COMMON CONTROL TRANSACTION

The Company was incorporated as a wholly owned subsidiary of Celtic Exploration Ltd. ("Celtic"), for the purposes of participating in a Plan of Arrangement (the "Arrangement") between ExxonMobil Canada Ltd. ("ExxonMobil Canada"), ExxonMobil Celtic ULC (formerly 1690731 Alberta ULC) (the "Purchaser"), Celtic and Kelt. Pursuant to the Arrangement, the Purchaser purchased all of Celtic's outstanding common shares ("Celtic Shares"), including Celtic Shares issued upon conversion of Celtic's 5% convertible debentures, at a cash price of $24.50 per Celtic Share. Additionally, Celtic shareholders received one-half (1/2) of a share of Kelt for each Celtic Share.

Pursuant to the Arrangement and a conveyance agreement (the "Conveyance Agreement") entered into by Celtic and Kelt upon closing of the Arrangement on February 26, 2013, Celtic transferred certain petroleum and natural gas assets (the "Celtic Assets") to Kelt in exchange for $142.0 million of common share consideration (the "Common Control Transaction"). The Celtic Assets transferred pursuant to the Common Control Transaction included all of Celtic's rights, title, estate and interest in the petroleum, natural gas and related hydrocarbon rights and related personal property interests within, upon or under the lands and leases, including: a liquids-rich gas property in the Inga area of northeastern British Columbia; a gas property in the Grande Cache area of Alberta; and an oil prospect in the Karr area of west central Alberta.

Kelt commenced active operations on February 27, 2013 following the completion of the Arrangement and Common Control Transaction on February 26, 2013. Prior to closing of the Arrangement, Kelt was a wholly owned subsidiary of Celtic and immediately subsequent to closing, Kelt was controlled by the same shareholders as Celtic; consequently, the entities were under common control. The Common Control Transaction has been accounted for using the predecessor values from the date of transaction method, whereby the Celtic Assets are transferred to Kelt based on the historical carrying value carved-out of Celtic. The Statement of Profit (Loss) and Comprehensive Income (Loss) includes the results of operations for the period subsequent to completion of the Arrangement, commencing on February 27, 2013.

The following table summarizes the carrying value of the net assets transferred as of February 26, 2013:

Exploration and evaluation assets		12,785
Property, plant and equipment		
Cost	126,062	
Accumulated depletion and depreciation	(22,218)	103,844
Decommissioning obligations		(9,089)
Net working capital		(23,247)
Carrying value of net assets transferred		**84,293**

Pursuant to the Conveyance Agreement, Celtic incurred certain costs on behalf of Kelt prior to closing of the Arrangement. These costs relate primarily to capital expenditures in respect of the Celtic Assets. Accordingly, net working capital in the amount of $23.2 million is presented as a reduction of the carrying value of the net assets transferred.

The difference between the common share consideration of $142.0 million and the carrying value of the Celtic Assets is recognized as a reserve from common control transaction in shareholders' equity, as follows:

Common shares	[note 12]	141,961
Carrying value of net assets transferred		(84,293)
Reserve from common control transaction		**57,668**

Under the terms of the Arrangement, the Company acquired tax pools in the amount of $165.2 million relating to the Celtic Assets. The Company did not initially recognize a deferred income tax asset of $14.4 million related to the excess of tax pools acquired relative to the carrying value of the net assets transferred because the Common Control Transaction is not a business combination and is therefore subject to the initial recognition exemption under IAS 12 *Income taxes*. Refer to note 13 for additional information.

5. ACQUISITIONS

a) Corporate acquisition

On July 2, 2014, the Company closed the acquisition of Capio Exploration Ltd. ("Capio"), a private Canadian oil and gas company, by acquiring all of the issued and outstanding common shares of Capio, which held crude oil and natural gas assets located at Valhalla/La Glace, adjacent to Kelt's core producing areas at Pouce Coupe/Spirit River in west central Alberta. Pursuant to the terms of the acquisition, which had an effective date of May 1, 2014, the consideration paid by Kelt, after closing adjustments, consisted of $72.1 million in cash and the issuance of 4,270,956 common shares of Kelt. In addition, Kelt assumed a working capital deficit of $37.4 million, including $32.5 million of bank indebtedness which was repaid at closing and Capio's demand loan credit facility was terminated. Immediately following closing of the acquisition, all of the property, assets and liabilities of Capio were assigned to Kelt and Capio was subsequently dissolved.

The table below summarizes the allocation of the purchase price:

Cash consideration, after closing adjustments	72,136
Issuance of common shares[(1)]	66,243
Total consideration	**138,379**
Net working capital deficit[(2)]	(37,439)
Exploration and evaluation assets	10,832
Property, plant and equipment	184,757
Goodwill	18,206
Decommissioning obligations	(399)
Deferred income tax liability	(37,578)
Fair value of net assets acquired	**138,379**

(1) The number of common shares issued pursuant to the acquisition was negotiated based on a total value of $58.0 million divided by the five day volume weighted average price of Kelt common shares that traded on the Toronto Stock Exchange from June 9th to 13th of $13.58 per common share. Under IFRS 3 *Business Combinations*, the value of common share consideration must be recognized based on acquisition date fair value. Accordingly, the value of common share consideration of $66.2 million reported above is based on the closing price of Kelt common shares on July 2, 2014 of $15.51 per common share.

(2) The net working capital deficit includes $32.5 million of bank indebtedness which was repaid by Kelt at closing pursuant to the change in control provisions under Capio's credit agreement.

The assets acquired are a complimentary fit with Kelt's existing core assets in west central Alberta. The goodwill recognized on the acquisition is attributed to the expected synergies and potential future cash flows to be derived from further exploration and development opportunities.

Pursuant to the terms of the agreement, the majority of transaction costs in respect of the acquisition were borne by Capio shareholders and reduced the ultimate amount of cash consideration paid by Kelt after closing adjustments. Kelt incurred approximately $0.2 million of transaction costs which were recognized as an expense in the period.

The Statement of Profit (Loss) and Comprehensive Income (Loss) includes the results of operations for the period following closing of the transaction on July 2, 2014. Specifically, Kelt's profit for the year ended December 31, 2014 includes approximately $17.4 million of revenue and $8.2 million of operating income generated from the acquired properties subsequent to closing. If the acquisition had occurred on January 1, 2014, pro-forma revenue and operating income for the assets acquired is estimated to be approximately $44.1 million and $22.1 million, respectively, for the year ended December 31, 2014. Operating income is defined as revenue, net of royalties, less production and transportation expenses. This pro-forma information is not necessarily indicative of the results of operations that would have resulted had the acquisition been effected on the dates indicated, or the results that may be obtained in the future.

b) Property acquisitions

Stoddart property acquisition

On December 18, 2014, the Company acquired petroleum and natural gas assets for cash consideration of $10.4 million, after estimated closing adjustments. The assets acquired are primarily located at Stoddart, adjacent to the Company's core producing area at Inga/Fireweed, in northeastern British Columbia. The transaction has been accounted for as a business combination using the acquisition method whereby the net assets acquired and the liabilities assumed are recorded at fair value.

The following table summarizes the fair value of net assets acquired pursuant to the Stoddart acquisition:

Exploration and evaluation assets	1,698
Property, plant and equipment	14,079
Decommissioning obligations	(5,420)
Fair value of net assets acquired	**10,357**
Cash consideration, after closing adjustments	**10,357**

The acquisition had an effective date of October 1, 2014 and the purchase price was adjusted for the results of operations between the effective date and closing of the transaction. The fair values of identifiable assets and liabilities acquired as reported in the table above were estimated based on information available at the time of preparation of these financial statements. Actual amounts recognized by the Company once the acquisition accounting is finalized may differ materially from these estimates.

The Statement of Profit (Loss) and Comprehensive Income (Loss) includes the results of operations for the period following closing of the transaction on December 18, 2014. Specifically, Kelt's profit for the year ended December 31, 2014 includes approximately $0.2 million of revenue and $0.1 million of operating income generated from the Stoddart property subsequent to closing. If the acquisition had occurred on January 1, 2014, pro-forma revenue and operating income for the acquired property is estimated to be approximately $7.8 million and $3.0 million, respectively, for the year ended December 31, 2014. Operating income is defined as revenue, net of royalties, less production and transportation expenses. This pro-forma information is not necessarily indicative of the results of operations that would have resulted had the acquisition been effected on the dates indicated, or the results that may be obtained in the future.

Other property acquisitions

During the year ended December 31, 2014, the Company completed several minor acquisitions of petroleum and natural gas assets for aggregate cash consideration of approximately $14.4 million, after estimated closing adjustments. The property acquisitions have been accounted for as business combinations using the acquisition method, whereby the net assets acquired and the liabilities assumed are recorded at fair value. The assets acquired are primarily located in the Pouce Coupe/Spirit River area of west central Alberta, and are a complimentary fit with Kelt's existing core assets.

The following table summarizes the aggregate fair value of net assets acquired pursuant to the minor property acquisitions during 2014:

Exploration and evaluation assets	6,670
Property, plant and equipment	9,410
Decommissioning obligations	(1,723)
Fair value of net assets acquired	**14,357**
Cash consideration, after closing adjustments	**14,357**

Fireweed property acquisition

On August 9, 2013, the Company acquired natural gas assets at Fireweed, adjacent to the Company's core producing area at Inga, in northeastern British Columbia, for cash consideration of $15.5 million, before closing adjustments. The acquisition had an effective date of April 1, 2013 and the purchase price was adjusted for the results of operations between the effective date and closing of the transaction resulting in a reduction of the purchase price by $1.3 million after closing adjustments. The transaction has been accounted for as a business combination using the acquisition method whereby the net assets acquired and the liabilities assumed are recorded at fair value.

The following table summarizes the fair value of net assets acquired pursuant to the Fireweed acquisition:

Exploration and evaluation assets	1,045
Property, plant and equipment	13,718
Decommissioning obligations	(585)
Fair value of net assets acquired	**14,178**
Cash consideration, after closing adjustments	**14,178**

Pouce Coupe/Spirit River property acquisition

On December 20, 2013, the Company acquired certain crude oil and natural gas assets located at Pouce Coupe/Spirit River, for cash consideration of $192.0 million, before closing adjustments. The acquisition had an effective date of October 1, 2013 and the purchase price was adjusted for the results of operations between the effective date and closing of the transaction resulting in a reduction of the purchase price by $1.3 million after closing adjustments. The transaction has been accounted for as a business combination using the acquisition method whereby the net assets acquired and the liabilities assumed are recorded at fair value.

The following table summarizes the fair value of net assets acquired pursuant to the Pouce Coupe/Spirit River acquisition:

Exploration and evaluation assets	8,682
Property, plant and equipment[(1)]	197,592
Decommissioning obligations[(2)]	(15,533)
Fair value of net assets acquired	**190,741**
Cash consideration, after closing adjustments	**190,741**

(1) Includes $20.6 million of property, plant and equipment classified as held for sale as at December 31, 2013, and disposed on February 10, 2014.
(2) Includes $1.0 million of decommissioning obligations classified as held for sale as at December 31, 2013, and disposed on February 10, 2014.

6. DISPOSITION OF ASSETS HELD FOR SALE

On February 10, 2014, Kelt completed the disposition of certain non-core and non-operated assets located in northwestern Alberta (collectively referenced herein as the "Assets Held for Sale"). The Company received proceeds of approximately $19.6 million, after closing adjustments.

The Assets Held for Sale were acquired on December 20, 2013, as part of the greater Pouce Coupe/Spirit River property acquisition, as described in note 5. Management entered into negotiations to sell and received an initial offer to purchase the Assets Held for Sale, prior to closing of the acquisition. As of the acquisition date, it was considered highly probable that the disposition would be successfully completed. Accordingly, the acquired assets to be sold were classified as held for sale on the acquisition date and measured at their fair value less costs of disposal. The disposition had an effective date of January 1, 2014 and the fair value has been reduced by approximately $0.4 million in respect of estimated closing adjustments between the effective date and closing of the transaction.

The fair value of the property, plant and equipment held for sale, net of the fair value of associated decommissioning obligations, is outlined in the table below:

	December 31, 2014	December 31, 2013
Property, plant and equipment	**-**	20,635
Decommissioning obligations	**-**	(1,000)
Assets Held for Sale	**-**	19,635

In accordance with IFRS 5, the Company did not recognize depletion and depreciation expense on the Assets Held for Sale because they were designated as held for sale on the acquisition date. Thus, the property, plant and equipment held for sale does not have any associated accumulated depletion and depreciation.

The Statement of Profit and Comprehensive Income for the year ended December 31, 2014 includes approximately $0.7 million of revenue and $0.4 million of operating income in respect of the Assets Held for Sale for the 40 day period up to closing of the disposition on February 10, 2014. There were no future development costs assigned to these assets. The disposition did not result in a reduction of the authorized borrowing amount available under the Credit Facility (note 10).

7. EXPLORATION AND EVALUATION ASSETS

Exploration and evaluation assets consist of the Company's undeveloped land, geological and geophysical assets, and exploratory drilling costs for projects in which the technical feasibility or commercial viability has yet to be determined. At the time sufficient information becomes available to determine whether the project is technically feasible or commercially viable, which is generally the point at which proved reserves are discovered, the costs are transferred to property, plant, and equipment.

The following table reconciles movements of exploration and evaluation assets during the period:

	December 31, 2014	December 31, 2013
Balance, beginning of period	**40,564**	-
Common control transaction [note 4]	**-**	12,785
Additions	**101,524**	46,717
Property acquisitions [note 5]	**8,368**	11,355
Corporate acquisition [note 5]	**10,832**	-
Transfers to property, plant and equipment	**(81,617)**	(30,179)
Expired mineral leases	**(377)**	(114)
Balance, end of period	**79,294**	40,564

The Company did not capitalize any general and administrative costs in respect of exploration activities during the current or prior periods.

8. PROPERTY, PLANT AND EQUIPMENT

Net carrying value	**December 31, 2014**	December 31, 2013
Development and production assets	**769,951**	376,399
Corporate assets	**533**	309
Total net carrying value of property, plant and equipment	**770,484**	376,708

The following table reconciles movements of property, plant and equipment during the period:

Property, plant and equipment, at cost	D&P[(1)] Assets	Corporate Assets	Total PP&E
Balance at December 31, 2012	-	-	-
Common control transaction [note 4]	126,062	-	126,062
Additions	49,321	414	49,735
Property acquisitions [note 5]	198,089	-	198,089
Decommissioning costs	38,833	-	38,833
Transfers from E&E	30,179	-	30,179
Assets held for sale [note 6]	(20,635)	-	(20,635)
Balance at December 31, 2013	**421,849**	**414**	**422,263**
Additions	**149,087**	**636**	**149,723**
Property acquisitions [note 5]	**23,489**	**-**	**23,489**
Corporate acquisition [note 5]	**184,757**	**-**	**184,757**
Dispositions	**-**	**(22)**	**(22)**
Decommissioning costs	**38,608**	**-**	**38,608**
Transfers from E&E	**81,617**	**-**	**81,617**
Balance at December 31, 2014	**899,407**	**1,028**	**900,435**

Accumulated depletion and depreciation	D&P[(1)] Assets	Corporate Assets	Total PP&E
Balance at December 31, 2012	-	-	-
Common control transaction [note 4]	22,218	-	22,218
Depletion and depreciation expense	23,232	105	23,337
Balance at December 31, 2013	**45,450**	**105**	**45,555**
Depletion and depreciation expense	**84,006**	**412**	**84,418**
Dispositions	**-**	**(22)**	**(22)**
Balance at December 31, 2014	**129,456**	**495**	**129,951**

(1) Development and production assets have been abbreviated as "D&P assets"

The Company did not capitalize any general and administrative costs in respect of development and production activities. There were no borrowing costs capitalized in the current or prior year, as the Company did not have any qualifying assets.

Future capital costs required to develop proved reserves in the amount of $382.8 million (2013 – $219.6 million) are included in the depletion calculation for development and production assets.

For the purpose of impairment testing, assets are grouped together into the smallest group of assets that generate cash inflows from continuing use that are largely independent of the cash inflows of other assets or CGUs. The Company reviewed each CGU for indicators of possible impairment as of December 31, 2014. As a result of a decrease in forecast oil and natural gas prices, an indication of potential impairment was identified for all CGUs. Recoverable amounts for the Company's CGUs were estimated based on FVLCD, calculated using the present value of the CGUs' expected future cash flows (after-tax). The primary source of cash flow information was derived from a

report on the Company's oil and gas reserves (the "Sproule Report") which was prepared by an independent qualified reserve evaluator, Sproule Associates Limited ("Sproule"). The projected cash flows in the Sproule Report reflect current market assessments of key assumptions, including long-term forecasts of commodity prices, inflation rates, and foreign exchange rates (Level 3 fair value inputs). Cash flow forecasts are also based on past experience, historical trends and Sproule's evaluation of the Company's reserves and resources to determine production profiles and volumes, operating costs, maintenance and future development capital expenditures. Production profiles, reserves volumes, operating costs, capital expenditures are consistent with the estimates approved through the Company's annual reserves evaluation process. Future cash flow estimates are discounted using after-tax risk-adjusted discount rates that reflect the risk specific to the assets in the CGU. The after-tax discount rate applied in the impairment calculation as at December 31, 2014 was 10% for all CGUs. Based on this analysis, the recoverable amount of each CGU exceeded its' carrying value, and accordingly, no impairment losses were recorded.

Forecast future prices used in the impairment evaluation as at December 31, 2014 reflect benchmark prices (WTI, Canadian Light Sweet, Henry Hub, AECO-C) adjusted for basis differentials to determine local reference prices, transportation costs and tariffs, heat content and quality as follows:

	2015	2016	2017	2018	2019[(1)]
Oil ($/bbl)	65.23	82.17	92.85	94.33	95.83
NGLs ($/bbl)	43.82	56.81	66.06	67.31	68.62
Natural gas ($/mcf)	3.41	3.81	4.02	4.67	5.31

(1) Prices escalate at 1.5% thereafter

The recoverable amount is highly sensitive to the discount rate and forecast future commodity prices. If the discount rate applied to forecasted future net cash flows increased by 1%, the Company would have recognized an impairment of PP&E of approximately $1.0 million. If forecast commodity prices decreased by 5%, the Company would have recognized an impairment of PP&E of approximately $3.8 million.

During the previous year ended December 31, 2013, there were no indicators of impairment identified. Accordingly, an impairment test was not required and there were no impairment losses recognized in the prior year.

9. GOODWILL

	December 31, 2014	December 31, 2013
Balance, beginning of period	**-**	-
Acquisition of Capio Exploration Ltd. [note 5]	**18,206**	-
Balance, end of period	**18,206**	-

The carrying value of goodwill is attributable to the acquisition of Capio on July 2, 2014. The Capio assets are located at Valhalla/La Glace, adjacent to Kelt's core producing assets at Pouce Coupe/Spirit River in the Grande Prairie area of west central Alberta. For the purposes of impairment testing, the carrying value of goodwill was allocated to the Company's Greater Grande Prairie CGU. As more particularly described in note 8, the Company completed an impairment test as at December 31, 2014 and concluded that the Greater Grande Prairie CGU, including allocated goodwill, was not impaired.

10. BANK DEBT

The Company has a committed term credit facility (the "Credit Facility") with a syndicate of financial institutions. The authorized borrowing amount available under the Credit Facility is $235.0 million. The Credit Facility is available for a revolving period of 364 days, maturing on May 1, 2015, and may be extended for an additional 364 days at the discretion of the lenders, with a term-out to April 29, 2016 if not renewed. Repayments of principal are not required provided that the borrowings under the facility do not exceed the authorized borrowing amount and the Company is in compliance with all covenants, representations and warranties. The Credit Facility is subject to semi-annual borrowing base reviews, occurring approximately in April and October of each year. In the event that the lenders reduced the borrowing base below the amount drawn at the time of the redetermination, the Company has 60 days to

eliminate any borrowing base shortfall by repaying the amount drawn in excess of the redetermined borrowing base or by providing additional security or other consideration satisfactory to the lenders. Covenants include reporting requirements, permitted indebtedness, permitted dispositions, permitted hedging, permitted encumbrances and other standard business operating covenants. There are no financial covenants under the Credit Facility. Security is provided for by a first fixed and floating charge debenture over all assets in the amount of $800.0 million and general assignment of book debts.

	December 31, 2014	December 31, 2013
Bank loan	**47,200**	-
Bankers' acceptances	**-**	-
Unamortized financing fees	**(271)**	-
Bank debt	**46,929**	-

Interest is payable monthly for borrowings through direct advances. Interest rates fluctuate based on a pricing grid and range from bank prime plus 1.0% to bank prime plus 2.5%, depending upon the Company's then current debt to cash flow ratio of between less than one and one tenth times to greater than three times. Under the Credit Facility, borrowings through the use of bankers' acceptances are also available. Stamping fees fluctuate based on a pricing grid and range from 2.0% to 3.5%, depending upon the Company's then current debt to cash flow ratio of between less than one and one tenth times to greater than three times.

11. DECOMMISSIONING OBLIGATIONS

Decommissioning obligations arise as a result of the Company's net ownership interests in petroleum and natural gas assets including well sites, processing facilities and infrastructure. The following table provides a reconciliation of the carrying amount of the obligation associated with the retirement of oil and gas properties:

	December 31, 2014	December 31, 2013
Balance, beginning of period	**48,169**	-
Common control transaction [note 4]	**-**	9,089
Obligations incurred	**3,259**	1,698
Obligations acquired(1) [note 5]	**7,542**	16,231
Disposition of obligations held for sale [note 6]	**(1,000)**	-
Obligations settled	**(229)**	-
Changes in discount rate(1)	**35,095**	21,491
Revisions to estimates	**254**	(587)
Accretion expense	**1,701**	247
Balance, end of period	**94,791**	48,169
Current portion of decommissioning obligations	**(758)**	(312)
Obligations associated with assets held for sale [note 6]	**-**	(1,000)
Long-term portion of decommissioning obligations	**94,033**	46,857

(1) Decommissioning obligations acquired as part of a business combination are initially measured at fair value using a credit-adjusted risk-free rate to discount estimated future cash outflows. The revaluation of obligations acquired using the risk-free rate at the end of the period results in an increase in the present value of the obligation reported in the Statement of Financial Position.

The key assumptions on which the carrying amount of the decommissioning obligations is based, include a risk-free rate of 2.3% (2013 – 3.2%) and an inflation rate of 2.0% (2013 – 2.0%). The underlying cost estimates are derived from a combination of published industry benchmarks as well as site specific information. As at December 31, 2014, the undiscounted amount of the estimated cash flows required to settle the obligation is $105.9 million (2013 – $74.0 million), and is expected to be incurred over the next 50 years.

Accretion of the decommissioning obligation due to the passage of time is presented within financing expenses in the Statement of Profit (Loss) and Comprehensive Income (Loss) (note 15).

12. SHARE CAPITAL

Authorized

The Company is authorized to issue an unlimited number of common shares and an unlimited number of preferred shares, each without par value.

Issued and outstanding

The following table summarizes the change in common shares issued and outstanding:

	Number of Shares (000's)	Amount ($ thousands)
Balance at December 31, 2012	-	-
Issued pursuant to the Arrangement [note 4]	61,126	141,961
Issued for cash through private placement offerings	48,900	320,930
Deferred premium on flow-through shares	-	(3,600)
Share issue costs, net of deferred income taxes ($3,138)	-	(9,415)
Balance at December 31, 2013	**110,026**	**449,876**
Issued for cash through private placement offering	**12,592**	**148,988**
Deferred premium on flow-through shares	**-**	**(3,722)**
Issued pursuant to corporate acquisition [note 5]	**4,271**	**66,243**
Issued for cash on exercise of stock options	**45**	**291**
Transfer from contributed surplus on exercise of stock options	**-**	**120**
Share issue costs, net of deferred income taxes ($1,573)	**-**	**(4,694)**
Balance at December 31, 2014	**126,934**	**657,102**

There are no preferred shares issued or outstanding as of December 31, 2014 (2013 – nil).

i) Common share offerings

On December 18, 2014, the Company completed a non-brokered private placement of 0.182 million flow-through common shares at a price of $11.00 per flow-through common share, providing gross proceeds of $2.0 million. The implied premium on the flow-through shares was determined to be $0.7 million or $3.80 per flow-through share, assuming a market price of $7.20 per ordinary common share. The market price of an ordinary common share was determined using a five day volume weighted average trading price, as defined in the TSX Company Manual, given there was no concurrent offering of ordinary common shares. Pursuant to the provisions in the *Income Tax Act* (Canada), the Company shall incur Canadian exploration expenses (the "Qualifying Expenditures") after December 18, 2014 and prior to December 31, 2015 in the aggregate amount of not less than $2.0 million. As of December 31, 2014, the Company had not incurred any Qualifying Expenditures, leaving $2.0 million of Qualifying Expenditures to be incurred in 2015. Kelt shall renounce the Qualifying Expenditures so incurred to the subscriber of the flow-through shares such that $11.00 per flow-through share shall be deductible against the subscriber's income for the fiscal year ended December 31, 2014.

On July 2, 2014, the Company issued 4,270,956 common shares to the shareholders of Capio as partial consideration for the acquisition (note 5). The number of common shares issued pursuant to the acquisition was negotiated based on a total value of $58.0 million divided by the five day volume weighted average price of Kelt common shares that traded on the Toronto Stock Exchange from June 9th to 13th of $13.58 per common share. Under IFRS 3 *Business Combinations*, the value of common share consideration must be recognized based on acquisition date fair value. Accordingly, the value of common share consideration of $66.2 million reported above is based on the closing price of Kelt common shares on July 2, 2014 of $15.51 per common share.

On March 25, 2014, Kelt completed brokered and non-brokered private placement equity offerings for aggregate gross proceeds of $147.0 million. Pursuant to the brokered private placement, the Company issued 9.775 million

common shares at a price of $11.60 per common share (which includes the exercise, in full, of the over-allotment option to purchase 1.275 million common shares) and issued 1.53 million common shares on a “flow-through” basis at a price of $12.75 per flow-through share. The Company issued an additional 1.105 million flow-through common shares at a price of $12.75 per flow-through share to certain directors, officers and employees of the Company, pursuant to the non-brokered private placement. The implied premium on the flow-through shares was determined to be $3.0 million or $1.15 per flow-through share. Kelt shall, pursuant to the provisions in the *Income Tax Act* (Canada), incur eligible Canadian development expenses (the “Qualifying Expenditures”) after March 25, 2014 and prior to December 31, 2014 in the aggregate amount of not less than the total amount of the gross proceeds raised from the issue of flow-through common shares of $33.6 million. As of December 31, 2014, the Company had incurred the full commitment of $33.6 million of Qualifying Expenditures. Kelt renounced the Qualifying Expenditures incurred to the subscribers of the flow-through common shares in an amount equal to $12.75 per flow-through common share with an effective date of December 31, 2014.

On December 3, 2013, Kelt raised aggregate gross proceeds of $101.06 million through a brokered and non-brokered subscription receipt equity financing. Pursuant to an agreement with a syndicate of underwriters, on a bought deal private placement basis, the Company issued 10.0 million subscription receipts of Kelt at a price of $8.15 per subscription receipt, resulting in gross proceeds of $81.5 million. Certain officers and directors of the Company purchased an additional 2.4 million subscriptions receipts at a price of $8.15 per subscription receipt, on a non-brokered private placement basis, providing additional gross proceeds of $19.56 million. The subscription receipts were converted into common shares of the Company on December 20, 2013, at no additional cost, following successful completion of the Pouce Coupe/Spirit River acquisition.

On August 27, 2013, the Company issued 11.5 million common shares at a price of $8.00 per common share (which includes the exercise in full of the over-allotment option to purchase 1.5 million common shares) for gross proceeds of $92.0 million. In addition, the Company issued 2.0 million flow-through shares in respect of Canadian exploration expenses at a price of $9.80 per flow-through share, providing additional gross proceeds of $19.6 million. The implied premium on the flow-through shares was determined to be $3.6 million or $1.80 per flow-through share. The Company incurred approximately $13.2 million of qualifying expenditures from August 27, 2013 to December 31, 2013. During the first two months of 2014, the Company incurred the remaining $6.4 million of qualifying expenditures and as of February 28, 2014, the Company had fulfilled the full commitment. Qualifying expenditures in the amount of $19.6 million were renounced to investors with an effective renunciation date of December 31, 2013.

On April 5, 2013, Kelt completed brokered and non-brokered equity financings for aggregate gross proceeds of $94.35 million. Pursuant to an agreement with a syndicate of underwriters, the underwriters agreed to purchase for resale to the public, on a bought deal private placement basis, 11.0 million common shares at a price of $5.55 per common share, resulting in gross proceeds to the Company of $61.05 million. In conjunction with the brokered private placement, Kelt agreed to issue to certain directors, officers and employees of the Company, on a non-brokered basis, an additional 6.0 million common shares at a price of $5.55 per common share, resulting in additional gross proceeds of $33.3 million.

On February 26, 2013, the Arrangement described in note 4 was completed by way of a statutory plan of arrangement under Section 193 of the *Business Corporations Act* (Alberta). Pursuant to the Arrangement, the Purchaser acquired all of the issued and outstanding Celtic Shares, including Celtic Shares issued upon conversion of Celtic’s 5% convertible debentures, for cash consideration of $24.50 per Celtic Share. In addition to the cash consideration, each Celtic shareholder received one-half (1/2) of a share of Kelt for each Celtic Share, resulting in the issuance of 61,126,119 Kelt common shares for consideration of $142.0 million. Concurrently with the closing of the Arrangement on February 26, 2013, Kelt also completed the private placement of 6.0 million common shares at a price of $2.32 per share for aggregate gross proceeds of approximately $13.92 million.

ii) Stock options

Kelt has an Incentive Stock Option Plan (the "Option Plan") that provides for granting of stock options to directors, officers, employees and certain consultants. The stock options granted pursuant to the Option Plan are to be settled through the issuance of new common shares of the Company and have a maximum term of five years to expiry. The vesting schedule is determined at the discretion of the Company's Compensation Committee of the Board of Directors; stock options typically vest in equal tranches over a three year period. Each stock option granted permits the holder to purchase one common share of the Company at the stated exercise price. The exercise price is determined based on the volume weighted average trading price on the TSX over three trading days immediately prior to the date of grant.

The following table summarizes the change in stock options outstanding:

	Number of Options (000's)	Average Exercise Price ($/share)
Balance at December 31, 2012	-	-
Granted	2,421	6.84
Balance at December 31, 2013	**2,421**	**6.84**
Granted	**2,624**	**9.79**
Exercised[(1)]	**(45)**	**6.47**
Forfeited	**(73)**	**8.91**
Balance at December 31, 2014	**4,927**	**8.38**

(1) The weighted average share price on the date of exercise for stock options exercised in 2014 was $10.15 per common share.

The total fair value of each option granted is estimated on the date of grant using the Black-Scholes option pricing model with weighted average assumptions as follows:

	Year ended December 31	
	2014	2013
Risk free interest rate	**1.2%**	1.2%
Expected life (years)	**3.5**	3.6
Expected volatility[(1)]	**37.3%**	51.6%
Expected dividend yield	**0.0%**	0.0%
Expected forfeiture rate	**0.6%**	0.4%
Fair value of options granted during the year ($/share)	**2.72**	2.61

(1) The Company estimates the expected volatility over the life of the option based on Kelt's historical volatility and a peer group average for junior/intermediate oil and gas companies, given there was no stock price history for the Company prior to the listing of KEL shares on March 1, 2013.

The following table summarizes information regarding stock options outstanding at December 31, 2014:

Range of exercise prices per common share	Number of options outstanding (000's)	Weighted average remaining term (years)	Weighted average exercise price for options outstanding ($/share)	Number of options exercisable (000's)	Weighted average exercise price for options exercisable ($/share)
$5.00 to $10.00	3,704	3.9	7.00	759	6.85
$10.01 to $15.00	1,163	4.3	12.42	-	-
$15.01 to $20.00	60	4.5	15.40	-	-
Total	**4,927**	**4.0**	**8.38**	**759**	**6.85**

iii) Restricted share units

Kelt has a Restricted Share Unit Plan (the "RSU Plan") that provides for granting of RSUs to officers, employees and certain consultants. The RSUs granted under the RSU Plan are to be settled through the issuance of new common shares upon vesting. The vesting schedule is determined at the discretion of the Company's Compensation Committee of the Board of Directors; RSUs typically vest in two equal tranches with the first half vesting after two years and the second half after three years. On the vesting date, one common share is released from treasury for each RSU.

The following table summarizes the change in RSUs outstanding:

	Number of RSUs (000's)
Balance at December 31, 2012	-
Granted	1,623
Balance at December 31, 2013	**1,623**
Granted	**208**
Forfeited	**(69)**
Balance at December 31, 2014	**1,762**

Share based compensation expense

The total fair value associated with stock options and RSUs is recognized over the service period using graded vesting, resulting in share based compensation expense as follows:

	Year ended December 31	
	2014	2013
Stock options	**4,116**	2,593
Restricted share units	**4,917**	3,186
Total share based compensation expense	**9,033**	5,779

Per share amounts

The table below summarizes the weighted average number of common shares outstanding used in the calculation of basic and diluted profit (loss) per common share:

	Year ended December 31	
(000's of common shares)	**2014**	2013
Weighted average common shares outstanding, basic	**121,779**	74,554
Effect of stock options and RSUs	**2,517**	539
Weighted average common shares outstanding, diluted	**124,296**	75,093

The Company uses the treasury stock method to determine the dilutive effect of stock options and RSUs. Under this method, only "in-the-money" dilutive instruments impact the calculation of diluted profit per common share. In computing the diluted loss per common share for the year ended December 31, 2013, the Company excluded the effect of stock options and RSUs as they were anti-dilutive.

13. INCOME TAXES

The Company's current and deferred income tax expense is outlined in the following table:

	Year ended December 31	
	2014	2013
Current income tax expense	**-**	-
Deferred income tax expense	**15,834**	1,181
Total income tax expense	**15,834**	1,181

Kelt was not required to pay current income taxes in the current or prior year as the Company had sufficient income tax deductions available to shelter taxable income. Tax deductions available as of December 31, 2014 are estimated to be approximately $599.8 million (2013 – $447.0 million).

The following table reconciles income taxes calculated at the Canadian statutory rate with the actual provision for deferred income taxes per the Statement of Profit (Loss) and Comprehensive Income (Loss):

	Year ended December 31	
	2014	2013
Profit (loss) before income taxes	**26,462**	(3,934)
Canadian statutory tax rate	**25.09%**	25.00%
Expected income tax expense (recovery)	**6,640**	(984)
Increase (decrease) resulting from:		
Non-deductible expenses[(1)]	**2,272**	1,449
Recognition of unrecognized deferred income tax asset	**(2,061)**	(1,972)
Qualifying Expenditures on flow-through shares [note 12]	**10,044**	3,293
Premium on flow-through shares [note 12]	**(1,057)**	(605)
Other	**(4)**	-
Deferred income tax expense	**15,834**	1,181

(1) Non-deductible expenses primarily include share based compensation

The Canadian statutory tax rate per the rate reconciliation above represents the combined federal and provincial corporate tax rate. The enacted federal corporate tax rate is 15.0% and the provincial tax rate is 10.0% in Alberta and 11.0% in British Columbia.

Under the terms of the Arrangement and Common Control Transaction described in note 4, the Company acquired tax pools in the amount of $165.2 million relating to the Celtic Assets. The Company did not initially recognize a deferred income tax asset of $14.4 million related to the excess of tax pools acquired relative to the carrying value of the net assets transferred because the Common Control Transaction is not a business combination and is therefore subject to the initial recognition exemption under IAS 12 *Income taxes*. The unrecognized deferred income tax asset is being amortized based on the corporate weighted average depletion factor for the period.

During the year ended December 31, 2014, the Company renounced tax pools in the amount of $40.0 million related to Qualifying Expenditures incurred pursuant to flow-through common share offerings. The Company's renounced $13.2 million of tax pools to the subscribers of flow-through common shares during the previous year ended December 31, 2013.

The movement in deferred income tax assets and liabilities, without taking into consideration the offsetting balances within the same tax jurisdiction are as follows:

Deferred income tax asset (liability)	Balance at December 31, 2013	Recognized in profit and CI[1]	Recognized in balance sheet	**Balance at December 31, 2014**
Derivative financial instruments	133	(571)		**(438)**
PP&E and E&E	(6,780)	(31,134)	(40,280)	**(78,194)**
Decommissioning obligations	11,792	11,894	100	**23,786**
Share and debt issue costs	2,599	(889)	1,573	**3,283**
Reserve from common control transaction	(12,445)	2,015		**(10,430)**
Non-capital losses[2]	6,658	2,851	2,602	**12,111**
	1,957	(15,834)	(36,005)	**(49,882)**

Deferred income tax asset (liability)	Balance at December 31, 2012	Recognized in profit and CI[1]	Recognized in balance sheet	Balance at December 31, 2013
Derivative financial instruments	-	133	-	133
PP&E and E&E	-	(6,780)	-	(6,780)
Decommissioning obligations	-	11,792	-	11,792
Share and debt issue costs	-	(539)	3,138	2,599
Reserve from common control transaction	-	(12,445)	-	(12,445)
Non-capital losses[2]	-	6,658	-	6,658
	-	(1,181)	3,138	1,957

(1) Comprehensive income has been abbreviated as "CI"
(2) The Company's non-capital losses expire in 15-20 years.

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 deferred income tax liability associated with derivative financial instruments is expected to reverse over the next twelve month period as it relates to a short-term risk management contract. The Company does not expect any other deferred income tax assets or liabilities to reverse within the next twelve months.

14. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT

Financial instruments of the Company include cash and cash equivalents, accounts receivable and accrued revenue, deposits, accounts payable and accrued liabilities, derivative financial instruments and bank debt. The fair value of the Company's financial assets and liabilities approximate their carrying value due to the short-term maturity of those instruments. In addition, the fair value of bank debt approximates its carrying value given it bears a floating rate of interest. The methodology used to determine the fair value for the Company's derivative financial instruments is described further in this note.

Fair value measurements

The Company classifies fair value measurements using a fair value hierarchy that reflects the significance of the inputs used in making the measurements. The fair value hierarchy has the following levels:

- Level 1 – Values are based on unadjusted quoted prices available in active markets for identical assets or liabilities as of the reporting date.
- Level 2 – Values are based on inputs, including quoted forward prices for commodities, time value and volatility factors, which can be substantially observed or corroborated in the marketplace. Prices in Level 2 are either directly or indirectly observable as of the reporting date.
- Level 3 – Values are based on prices or valuation techniques that are not based on observable market data.

Assessment of the significance of a particular input to the fair value measurement requires judgment and may affect the placement within the fair value hierarchy.

The table below summarizes fair value measurements for each hierarchy level as at December 31, 2014:

	Level 1	Level 2	Level 3
Financial assets			
Derivative financial instruments	-	1,745	-

Offsetting of financial instruments

Financial assets and liabilities are only offset if the Company has the current legal right to offset and intends to settle on a net basis or settle the asset and liability simultaneously. Kelt offsets derivative contracts assets and liabilities when the counterparty, commodity, currency and timing of settlement are the same. As at December 31, 2014, there are no offsetting derivative contracts.

Risk Management Overview

The Company is exposed to financial risks arising from its financial assets and liabilities that include credit and liquidity risk in addition to the market risks associated with commodity prices, and interest and foreign exchange rates. Profit (loss), cash flows and the fair value of financial assets and liabilities may fluctuate due to movement in market prices or as a result of the Company's exposure to credit and liquidity risks. This note presents information about the Company's exposure to each of the above risks, the Company's objectives, policies and processes for measuring and managing risk, and the Company's management of capital. Further quantitative disclosures are included throughout these financial statements.

The Board of Directors has overall responsibility for the establishment and oversight of the Company's risk management framework. The Company's management has implemented and continues to maintain and monitor risk management procedures for the benefit of the organization. The Company's risk management policies are established to: i) identify and analyze the risks faced by the Company; ii) set appropriate risk limits and controls; and iii) monitor risks and consider the implications of market conditions in relation to the Company's activities.

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 and arises primarily from Kelt's receivables from joint venture partners and oil and gas marketers. The composition of the Company's accounts receivable is set out in the following table:

Accounts receivable & accrued revenue	**December 31, 2014**	December 31, 2013
Joint venture partners	**11,972**	5,771
Oil and gas marketers	**15,488**	4,384
GST input tax credits	**5,461**	1,981
Interest receivable	**-**	33
Risk management contracts	**1,681**	-
Other	**490**	913
Accounts receivable & accrued revenue	**35,092**	13,082

During the year ended December 31, 2014, sales to three external customers each individually represented more than 10% of total revenue. Sales to these customers account for approximately 53%, 16%, and 15% of total revenue, respectively. During the previous year ended December 31, 2013, sales to two external customers accounted for approximately 55% and 29% of total revenue, respectively.

The carrying amount of cash and cash equivalents, accounts receivable and accrued revenue, deposits and derivative financial instrument assets represent the Company's maximum credit exposure. Cash and cash equivalents are held on deposit with a Canadian chartered bank.

The credit risk exposure for oil and gas marketers is mitigated through the use of approved credit policies governing the Company's credit portfolio and with credit practices that limit transactions according to counterparty credit quality as well as requiring collateral where deemed appropriate. The Company does not typically obtain collateral from its oil and gas marketers or joint venture partners.

The credit risk from joint venture receivables is mitigated by obtaining partner approval of significant capital expenditures prior to expenditure and in certain circumstances may require cash deposits in advance of incurring financial obligations on behalf of joint venture partners. However, the receivables are from participants in the oil and gas industry and collection of the outstanding balances is dependent on industry factors such as changes in commodity prices, escalating costs and the risk of unsuccessful drilling. In addition, further risk exists with joint venture partners from occasional contractual disputes that increase the potential for non-collection. The Company does have the ability to withhold production from joint venture partners in the event of non-payment or may be able to register security on the assets of joint venture partners.

The Company has an International Swaps and Derivatives Association ("ISDA") agreement with a Canadian chartered bank to address counterparty credit risk associated with derivative financial instruments. These agreements and confirmations provide some credit protection in that they generally allow parties to aggregate amounts owing to each other under all outstanding transactions and settle with a single net amount in the case of a credit event.

The oil and gas industry has a pre-arranged monthly clearing day for payment of revenues from all buyers of oil and natural gas; this occurs on the 25th day following the month of sale. As a result, the Company's production revenues are current. All other accounts receivable are generally contractually due within 30 days.

The ageing of the Company's accounts receivable is summarized in the following table:

Accounts receivable & accrued revenue	Current	30-60 days	60-90 days	Over 90 days	Total
Balance at December 31, 2014	**31,071**	**2,499**	**208**	**1,314**	**35,092**
Balance at December 31, 2013	11,799	194	834	255	13,082

The balance of accounts receivable outstanding for more than 90 days relates primarily to receivables from the Company's joint venture partners. Management has reviewed past due accounts receivable balances and expects the accounts to be fully collectible.

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 financial liabilities include accounts payable and bank debt. Kelt's approach to managing liquidity is to ensure, as far as possible, that it will have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking harm to the Company's reputation.

As at December 31, 2014, the Company had a net working capital deficit of $57.5 million. The capital intensive nature of Kelt's activities may create a working capital deficiency position during periods with high levels of capital investment. The Company manages liquidity risk through prudent use of bank debt and an actively managed production and capital expenditure budgeting process. In addition, risk management contracts such as derivative financial instruments may be used from time to time. As discussed further under the Capital Management section to follow, Kelt targets a relatively low debt to trailing funds from operations ratio. To manage this, the Board of Directors approves an annual capital expenditure budget, which is regularly monitored and updated as necessary in response to changing capital requirements. The Company utilizes a control system with respect to authorizations for expenditures on both operated and non-operated projects to further manage capital expenditures.

As discussed in note 10, Kelt has drawn $46.9 million on its $235.0 million committed term Credit Facility. The Credit Facility is available for a revolving period of 364 days, maturing on May 1, 2015, and may be extended for an additional 364 days at the discretion of the lenders, with a term-out to April 29, 2016 if not renewed. Repayments of principal are not required provided that the borrowings under the Credit Facility do not exceed the authorized borrowing amount and the Company is in compliance with all covenants, representations and warranties. The Company is not subject to any financial covenants under the Credit Facility and as at December 31, 2014, Kelt is in

compliance with all other covenants. As a result of the precipitous decline in commodity prices, many oil and gas companies, including Kelt, are facing a number of uncertainties. Although management expects that the lenders will extend the Credit Facility in 2015, there is no assurance that the financial institutions will choose to do so. Should the financial institutions not extend the loan, the Company would need to seek alternative sources of debt or equity financing.

The table below outlines a contractual maturity analysis for Kelt's financial liabilities as at December 31, 2014:

	Within 1 Year	1 to 5 Years	More than 5 Years	Total
Accounts payable and accrued liabilities	96,776	-	-	96,776
Bank debt and estimated interest[(1)]	1,888	47,816	-	49,704
Total	**98,664**	**47,816**	**-**	**146,480**

(1) Estimated interest for future periods related to the Credit Facility was calculated using the weighted average interest rate for the year ended December 31, 2014, applied to the principal balance outstanding as at that date. Principal repayment of the Company's revolving Credit Facility is assumed on April 29, 2016.

Market Risks

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

The Company uses derivative financial instruments from time to time in order to manage market risks. All such transactions are conducted in accordance with the Company's established risk management procedures.

Commodity price risk

Inherent to the business of producing oil and gas, the Company's cash provided by operating activities is subject to commodity price risk. Commodity price risk is the risk that future cash flows will fluctuate as a result of changes in commodity prices. Commodity prices for oil and natural gas are impacted by world economic events that dictate the levels of supply and demand as well as the currency exchange rate relationship between the Canadian and U.S. dollar. The Company mitigates commodity price risk through the use of various derivative financial instruments.

The Company's current risk management policies permit management to enter into commodity agreements, provided that: i) the contracts are not entered into for speculative purposes; ii) that the notional quantity hedged, at the time of entering into the contract, does not exceed 65% of average daily production; and iii) that the term does not exceed 36 months.

The following table summarizes the Company's financial derivative risk management contracts outstanding as of December 31, 2014:

Commodity	Notional volume	Pricing point	Contract Price	Remaining term	Fair value Asset (Liability)
Propane	250 bbls/d	OPIS-Conway	US$ 40.95/bbl	Mar 1 to Dec 31, 2015	**1,745**
Net derivative financial instrument asset[(1)]					**1,745**

(1) The fair value of the derivative financial instruments is sensitive to changes in commodity prices. If the Canadian dollar equivalent OPIS-Conway propane price increases (decreases) by $1.00 per barrel, the fair market value of the contract would decrease (increase) by $0.1 million.

The table below summarizes realized and unrealized gains (losses) on risk management contracts:

	Year ended December 31	
	2014	2013
Realized loss	**(388)**	(579)
Unrealized gain (loss)	**2,277**	(304)
Gain (loss) on derivative financial instruments	**1,889**	(883)

Interest rate risk

Interest rate risk is the risk that future cash flows will fluctuate as a result of changes in market interest rates. The Company is exposed to interest rate risk to the extent that changes in market interest rates will impact the Company's Credit Facility which is subject to a floating interest rate. Assuming all other variables remain constant, an increase (decrease) of 1% in market interest rates would have decreased (increased) shareholders' equity and profit less than $0.1 million for the year ended December 31, 2014.

Since commencing active operations in February 2013, Kelt had not incurred any bank debt until the fourth quarter of 2014. The Company seeks to manage interest rate risk through the use of short-term fixed rate bankers' acceptances. In addition, the Company may utilize derivative risk management contracts such as interest rate swaps, however, the Company did not have any such contracts in place during the current or prior year.

Foreign exchange rate risk

Foreign exchange risk is the risk that future cash flows will fluctuate as a result of changes in foreign exchange rates. While all of the Company's oil and natural gas sales are transacted in Canadian dollars, the Company is exposed to the risk of changes in the Canadian/U.S. dollar exchange rate because the Company's realized price is directly influenced by U.S. dollar benchmark prices. The effects of foreign exchange fluctuations are embedded in the Company's results and the total effect of foreign exchange fluctuations are not separately identifiable.

The Company did not have any foreign exchange rate contracts in place during the current or prior year. Subsequent to December 31, 2014, the Company entered into a forward foreign exchange contract fixing the US/Canadian dollar exchange rate at US$0.7949 on a notional US$3.0 million per month from March to December 2015, representing approximately 40% of the Company's budgeted oil revenue currency exposure for the same period. The contract will settle monthly, based on the difference between the fixed rate and the average noon exchange rate for the month per the Bank of Canada.

In order to mitigate a portion of the risk relating to revenue that is subject to fluctuations in the exchange rate, the Company may enter into commodity swap transactions whereby commodity prices denominated in U.S. dollars are converted to Canadian dollars. There are no such contracts in place as at December 31, 2014.

Capital Management

The Company's capital structure is comprised of shareholders' equity, bank debt and working capital. Kelt's objectives when managing its capital structure is to maintain financial flexibility in order to meet financial obligations, as well as to finance future growth through capital expenditures relating to exploration, development and acquisition activities.

The Company monitors its capital structure and short-term financing requirements using a debt to trailing funds from operations ratio, which is a non-GAAP financial measure.

	December 31, 2014	December 31, 2013
Bank debt	**46,929**	-
Working capital deficiency (surplus)	**57,501**	(20,500)
Total debt (surplus)	**104,430**	(20,500)
Trailing funds from operations[(1)(2)]	**118,656**	37,584
Debt to trailing funds from operations ratio	**0.9**	N/A[(3)]

(1) Funds from operations is a non-GAAP measure which is calculated as cash provided by operating activities, before settlement of decommissioning obligations and change in non-cash operating working capital.

(2) Trailing funds from operations is annualized based on the most recent quarter's funds from operations.

(3) The Company had a surplus as at December 31, 2013, therefore the debt to trailing funds from operations ratio is not applicable.

Kelt targets a debt to trailing funds from operations ratio of less than 2.0 times. The Company manages its capital structure and makes adjustments according to market conditions in order to maintain flexibility to achieve its objectives stated above. To adjust its capital structure, the Company may increase or decrease capital expenditures, issue new shares, issue new debt or repay existing debt.

As described in note 10, Kelt is subject to certain non-financial covenants under the Credit Facility agreement. As at December 31, 2014, the Company is in compliance with all covenants. The Company is not subject to any other externally imposed capital requirements.

15. FINANCING EXPENSES

The following table summarizes significant components of the Company's financing expenses:

	Year ended December 31	
	2014	2013
Interest and fees on bank debt	**820**	82
Accretion of decommissioning obligations [note 11]	**1,701**	247
Financing expense	**2,521**	329

16. COMMITMENTS

As of December 31, 2014, the Company is committed to future payments under the following agreements:

(CA$ thousands)	2015	2016	2017	2018	2019	Thereafter
Operating lease – office buildings	1,095	1,229	1,253	495	114	19
Operating lease – vehicles	219	157	69	1	-	-
Flow-through shares	2,002	-	-	-	-	-
Firm transportation commitments	2,967	1,173	14	-	-	-
Total annual commitments	**6,283**	**2,559**	**1,336**	**496**	**114**	**19**

Payments under the office building operating leases relate to the Company's head office in Calgary, Alberta, and the field office in Grande Prairie, Alberta. The head office and field office leases expire on April 30, 2018 and February 28, 2020, respectively, if not extended.

On December 18, 2014, the Company issued 0.182 million flow-through shares at a price of $11.00 per flow-through share. Pursuant to the provisions in the *Income Tax Act* (Canada), the Company shall incur Canadian exploration expenses (the "Qualifying Expenditures") after December 18, 2014 and prior to December 31, 2015 in the aggregate amount of not less than $2.0 million. As of December 31, 2014, the Company had not incurred any Qualifying Expenditures, leaving $2.0 million of Qualifying Expenditures to be incurred in 2015. Kelt shall renounce the Qualifying Expenditures so incurred to the subscriber of the flow-through shares such that $11.00 per flow-through share shall be deductible against the subscriber's income for the fiscal year ended December 31, 2014.

17. SUPPLEMENTAL CASH FLOW INFORMATION

	Year ended December 31	
Changes in non-cash working capital	**2014**	2013
Accounts receivable and accrued revenue	**(16,675)**	(13,082)
Prepaid expenses and deposits	**(1,557)**	(1,240)
Accounts payable and accrued liabilities	**43,040**	43,447
Change in non-cash working capital	**24,808**	29,125
Relating to:		
Operating activities	**(2,883)**	3,235
Investing activities	**27,691**	25,890
Change in non-cash working capital	**24,808**	29,125

Cash outlays in respect of interest and taxes	Year ended December 31 2014	2013
Interest and standby fees on bank debt	**359**	70
Taxes	**-**	-

18. RELATED PARTY TRANSACTIONS

A director of the Company is also a partner at a law firm which Kelt has engaged to provide legal services. During the year ended December 31, 2014, the Company incurred $0.4 million (2013 – $0.6 million) in legal fees and disbursements, of which, less than $0.1 million is payable at December 31, 2014 (2013 – $0.2 million). The Company expects to continue using the services of this law firm from time to time.

Key management personnel are those persons having authority and responsibility for planning, directing and controlling the activities of the Company. The following table summarizes compensation paid or payable to officers and directors of the Company:

	Year ended December 31 2014	2013
Salaries, bonuses and other benefits	**715**	485
Share based compensation	**4,096**	3,392
Total compensation	**4,811**	3,877

During the year ended December 31, 2014, key management personnel were granted an aggregate of 970,000 stock options with an average exercise price of $9.34 per share. During the previous year ended December 31, 2013, key management personnel were granted an aggregate of 789,000 restricted share units and 1,250,000 stock options with an exercise price of $6.47 per share.

In addition, the Common Control Transaction is considered to be a related party transaction because Kelt was a wholly owned subsidiary of Celtic immediately prior to closing of the Arrangement. Refer to note 4 for additional information regarding accounting for the transaction.

19. SUBSEQUENT EVENTS

Acquisition of Artek Exploration Ltd.

On February 20, 2015, Kelt entered into an agreement with Artek Exploration Ltd. (“Artek”), pursuant to which Kelt will acquire all of the issued and outstanding common shares of Artek on the basis of 0.34 of a Kelt common share for each Artek common share. The acquisition will be effected by way of a statutory plan of arrangement (the “Artek Arrangement”).

Based on the volume-weighted average trading price of the Kelt common shares for the five trading days ended February 20, 2015 of $8.10 on the TSX, the total consideration is approximately $307 million, comprised of the issuance of approximately 26.9 million Kelt common shares and the assumption of an estimated $89.5 million of bank debt, net of working capital, as at February 20, 2015, which includes estimated associated transaction costs of approximately $5.6 million.

Completion of the Artek Arrangement, which is anticipated to occur on or around April 16, 2015, is subject to, among other things, the approval of at least 66⅔% of votes cast by Artek shareholders voting at a special meeting of shareholders to be held on or around April 16, 2015, the approval of the Court of Queen’s Bench of Alberta, receipt of all necessary regulatory and stock exchange approvals and certain closing conditions that are customary for a transaction of this nature. Artek has agreed not to solicit or initiate any discussion regarding any other business combination or sale of material assets. Artek has also granted Kelt a right to match any superior proposal and has agreed to pay a termination fee of $8.5 million to Kelt in certain events, including if Artek recommends, approves or enters into an agreement with respect to a superior proposal.

The acquisition of Artek will consolidate the majority of Kelt's land acreage in its Inga-Fireweed-Stoddart, British Columbia core area to 100% and is consistent with the Company's strategy to operate and control all of its major core exploration and development prospects. In addition, Kelt's acquisition of Artek will result in 100% ownership by Kelt in key infrastructure including compression facilities and pipelines in the area.

Equity Private Placement

In February 2015, the Company agreed to issue by way of private placement, on a non-brokered basis, 3,881,400 common shares on a "flow-through" basis in respect of Canadian development expenses at a price of $8.60 per flow-through common share (the "2015 Private Placement"), resulting in gross proceeds of $33.4 million. Certain directors and officers of the Company subscribed to purchase 1,714,500 flow-through common shares for gross proceeds of $14.9 million, representing approximately 44% of the aggregate issue. The 2015 Private Placement will be completed in three tranches. The first tranche of 1,000,000 flow-through common shares closed on February 27, 2015. The second tranche of 2,300,000 flow-through common shares closed on March 6, 2015. The remaining tranche of 581,400 flow-through common shares is expected to close on or about March 16, 2015. Net proceeds of the offering will be used to partially finance drilling and completion expenditures during the remainder of 2015.

Kelt shall, pursuant to the provisions of the *Income Tax Act* (Canada), incur eligible Canadian development expenses, (the "Qualifying Expenditures") after the closing date and prior to December 31, 2015 in the aggregate amount of not less than the total amount of the gross proceeds raised from the issue of flow-through common shares. Kelt shall renounce the Qualifying Expenditures so incurred to the purchasers of the flow-through common shares in an amount equal to $8.60 per flow-through common share on or prior to December 31, 2015.

The Kelt common shares issued and to be issued in connection with the 2015 Private Placement are subject to a statutory hold period of four months plus one day from the respective dates of completion of the offering, in accordance with applicable securities legislation.

ABBREVIATIONS

bbls	barrels
mbbls	thousand barrels
bbls/d	barrels per day
BOE	barrels of oil equivalent
mBOE	thousand barrels of oil equivalent
BOE/d	barrels of oil equivalent per day
mcf	thousand cubic feet
mmcf	million cubic feet
bcf	billion cubic feet
mmcf/d	million cubic feet per day
mmbtu	million British Thermal Units
GJ	gigajoules
LT	long tonnes
AECO-C	Alberta Energy Company “C” Meter Station of the Nova Pipeline System
WTI	West Texas Intermediate
NYMEX	New York Mercantile Exchange
API	American Petroleum Institute
CICA	Canadian Institute of Chartered Accountants
MD&A	Management’s Discussion and Analysis
Q1	First quarter ended March 31st
Q2	Second quarter ended June 30th
Q3	Third quarter ended September 30th
Q4	Fourth quarter ended December 31st
BT	Before income taxes
AT	After income taxes
1P	Proved reserves
2P	Proved plus probable reserves
FD&A	Finding, development and acquisition costs
F&D	Finding and development costs

CONVERSION OF UNITS

Imperial = Metric

1 acre = 0.4 hectares

2.5 acres = 1 hectare

1 bbl = 0.159 cubic metres

6.29 bbls = 1 cubic metre

1 foot = 0.3048 metres

3.281 feet = 1 metre

1 mcf = 28.2 cubic metres

0.035 mcf = 1 cubic metre

1 mile = 1.61 kilometres

0.62 miles = 1 kilometre

1 mmbtu = 1.054 GJ

0.949 mmbtu = 1 GJ

Natural gas is equated to oil on the basis of 6 mcf = 1 BOE

Sulphur is equated to gas on the basis of 1LT = 10 mcf (1 BOE = 0.6 LT)

CORPORATE INFORMATION

BOARD OF DIRECTORS

Robert J. Dales [2, 3, 4, 6]
President, Valhalla Ventures Inc.

William C. Guinan [1, 5, 6]
Partner, Borden Ladner Gervais LLP

Eldon A. McIntyre [2, 3, 4, 6]
President, Jarrod Oils Ltd.

Neil G. Sinclair [2, 3, 4, 5]
President, Sinson Investments Ltd.

David J. Wilson [5]
President & Chief Executive Officer,
Kelt Exploration Ltd.

1 chairman of the board

2 member of the audit committee

3 member of the reserves committee

4 member of the compensation committee

5 member of the health, safety and environment committee

6 member of the nominating committee

OFFICERS

David J. Wilson
President & Chief Executive Officer

Sadiq H. Lalani
Vice President, Finance & Chief Financial Officer

Douglas J. Errico
Vice President, Land

Alan G. Franks
Vice President, Production

Douglas O. MacArthur
Vice President, Operations

Patrick Miles
Vice President, Exploration

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EVALUATION ENGINEERS

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