



**GALE FORCE<sup>TM</sup>**  
**PETROLEUM**

**MANAGEMENT'S DISCUSSION AND ANALYSIS**

**For the three-month periods ended September 30, 2014 and 2013**

**Prepared as at November 25, 2014**



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## BASIS OF PRESENTATION

Throughout this document, Gale Force Petroleum Inc. is referred to as “Gale Force Petroleum”, “we” or the “Company”. This management’s discussion and analysis of the financial condition and results of operations (“**MD&A**”) describes our business, the business environment, our vision and strategy as well as the critical accounting policies used by the Company, which should help the reader understand our financial statements, the principal factors affecting the results of operations, and the Company’s liquidity and capital resources. This discussion should be read in conjunction with the Company’s interim consolidated financial statements, including the notes, as at and for the periods ended September 30, 2014 and September 30, 2013.

The Company’s accounting policies are in accordance with International Financial Reporting Standards (“**IFRS**”) and interpretations of the International Financial Reporting Interpretations Committee (“**IFRIC**”). **All dollar amounts herein are in U.S. dollars unless otherwise indicated.**

Except as otherwise specified, references herein to the period indicated the quarter ended September 30, 2014, and all comparisons are to the quarter ended September 30, 2013. References herein to the year indicate the fiscal year ended June 30, 2015, and all comparisons are to the fiscal year ended June 30, 2014.

## FORWARD-LOOKING STATEMENTS

All statements in this MD&A that do not directly and exclusively relate to historical facts constitute “forward-looking statements”. These statements represent the Company’s intentions, plans, expectations and beliefs, and are subject to risks, uncertainties and other factors, of which many are beyond the control of the Company. These factors could cause actual results to differ materially from such forward-looking statements. These factors include and are not restricted to general economic and business conditions, industry conditions, volatility of commodity prices, currency exchange rate fluctuations, imprecision of reserve estimates, environmental risks, competition from other explorers, stock market volatility, the ability to access sufficient capital, the timing and size of new contracts, acquisitions and other corporate developments, the ability to attract and retain qualified employees, contractors, managers and members of the board, and other risks identified in the MD&A, as well as assumptions regarding the foregoing. The words “believe,” “estimate,” “expect,” “intend,” “anticipate,” “foresee,” “plan,” and similar expressions and variations thereof, identify certain of such forward-looking statements, which speak only as of the date on which they are made. In particular, statements relating to future performance are forward-looking statements. The Company disclaims any intention or obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events or otherwise. Readers are cautioned not to place undue reliance on these forward-looking statements. You will find more information about the risks that could cause our actual results to significantly differ from our current expectations in the Risks and Uncertainties section.

## DEFINITIONS, NOTES AND OTHER CAUTIONARY STATEMENTS

In this document, the abbreviations set forth below have the following meanings:

|      |   |
|------|---|
| bbl  | Barrel.   |
| Mcf  | Thousand cubic feet.  |
| MMcf | Million cubic feet.   |
| BOEs | Barrel of Oil Equivalent. <i>BOEs may be misleading, particularly if used in isolation. The BOE conversion ratio of 6 Mcf:1 bbl is based on an energy equivalency and does not represent a value equivalency at the wellhead.</i> |

## OVERVIEW OF THE COMPANY

Gale Force Petroleum Inc. (the “**Company**”) is a publicly-traded oil and gas company with working interests in conventional oil and gas properties in Texas, and membership interests in an LLC that owns producing Marcellus shale gas in West Virginia.

As of the end of the quarter ended September 30, 2014, the Company was producing 80 BOE per day (to its working interests before royalties). During the quarter, effective August 1, 2014, the Company sold a majority interest of its Texas Reef Properties and its working interest in the Thunder Properties, which reduced its production from 175 BOE per day at the end of the prior period ended June 30, 2014. As at June 30, 2014, the Company had *proved and probable* reserves of 281,000 net bbls of oil and 304,000 net Mcf of natural gas, with the net present value of these reserves being estimated at approximately \$8.1 million using a 10% discount rate.

## STRATEGY, OBJECTIVES AND PLANS

The Company’s business plan since May 2010 has been to acquire and develop oil and gas properties in the southern U.S., taking advantage of the general undervaluation and underinvestment that existed in the Southern U.S. following the financial crisis and oil price collapse in 2008-2009. The funding for these acquisitions and property development projects came from a combination of equity raised through Canadian markets and low-interest U.S. bank debt.

Between May, 2010 and January, 2013, the Company completed ten important acquisitions, various smaller transactions and a land acquisition program, which, in the aggregate, increased the Company’s reserves and grew the Company’s total oil and gas production from zero to a high in 2012 of approximately 650 BOE per day (to its working interests before royalties).

The macroeconomic conditions that helped make the Company’s business plan initially successful have changed. Firstly, the Canadian dollar has declined by roughly 15%, reducing the buying power of funds raised from equity issued in Canada. Also, since the fall of 2012, there has been a significant reduction in demand for the shares of micro and junior oil and gas companies, resulting in a self-fulfilling cycle of decreasing liquidity, and increasing difficulty for junior oil and gas companies to raise new equity financing at reasonable or attractive valuations. At the same time, there is no longer a general undervaluation in the Southern U.S. as the effects of the 2009 U.S. financial crisis have faded, the private oil and gas property market in the Southern U.S. is back in balance.

The Company therefore believes that its business plan to acquire and aggregate smaller properties in the Southern U.S. is no longer appropriate in view of these market trends, and continuing to pursue this business plan would be unlikely to create shareholder value. As a result, the Board of Directors of the Company initiated a strategic review last year, and has since then sold several assets to pay down debts and free-up capital, while searching for a strategic option that will provide the greatest shareholder value.

### *Strategic Alternative Review Process*

The Company has not found an *en bloc* buyer of the Company’s assets, but has found a high level of interest in its individual properties. As a result, the Company has been selling its assets to pay down debts and free-up capital, making itself more attractive for acquisition or merger to strategic counterparts averse to debt and needing cash. The Company is currently actively evaluating various oil and gas companies or assets in North America, where there would be significant scalability in operations, and where the Company’s combination of cash and near-cash assets would have the most impact in creating value.

## RESULTS OF OPERATIONS

### Comparative Financial Analysis

The following table shows selected condensed consolidated statements of financial position information:

#### SELECTED INFORMATION CONSOLIDATED STATEMENTS OF FINANCIAL POSITION

| As at                       | Sept 30, 2014 | June 30, 2014 |
|-----------------------------|---------------|---------------|
| Assets                      | \$ 12,962,611 | \$ 17,548,833 |
| Property and equipment      | 8,747,907     | 14,744,511    |
| Oil and gas investments     | 1,303,388     | 1,303,388     |
| Subordinate notes payable   | -             | 701,255       |
| Bank facility               | 1,750,000     | 4,750,000     |
| Decommissioning liabilities | 234,994       | 306,390       |
| Shareholders' equity        | \$ 9,894,393  | \$ 10,101,909 |
| Current assets              | \$ 2,437,114  | \$ 1,050,934  |
| Current liabilities         | \$ 1,074,224  | \$ 2,298,108  |

During the first quarter of the fiscal year net property and equipment decreased by \$6 million due to sales of \$5.9 million in Texas Reef property and \$50,000 in South Texas.

A portion of sales proceeds was used to repay in full \$701,255 subordinate notes and \$3.0 million of outstanding bank debt.

The following table shows the Company's consolidated sales and revenues:

| CONSOLIDATED REVENUES       |                   |                     |
|-----------------------------|-------------------|---------------------|
| Quarters ended September 30 | 2014              | 2013                |
| Sales                       | \$ 545,653        | \$ 1,093,199        |
| Production taxes            | (25,113)          | (49,900)            |
| <b>Total revenues</b>       | <b>\$ 520,540</b> | <b>\$ 1,043,299</b> |

For the first quarter of the fiscal year revenues decreased 50% compared to the first quarter of the prior fiscal year. The average sales price decreased only \$0.30 to \$83.37 per BOE between the comparable periods. However, production for the first quarter of the fiscal year declined 50% to 6,545 BOE compared to 13,065 BOE for the first quarter of the prior fiscal year. The production decline was due to the sales of Texas Reef and South Texas properties with an effective date of August 1, 2014 and sales of Gregg & Rusk Counties and non-core Wood County properties in the prior fiscal year.

The following table shows the "Cash-Adjusted EBITDA" of the Company, which is a measure to present earnings (loss) after all cash operating expenses, while separating out any non-cash or non-recurring expenses and the effects of capital structure or taxation. It provides better visibility of the Company's cash requirements and/or its ability to generate cash, exclusive of the costs of depreciation, financing or income taxes.

## CASH-ADJUSTED EBITDA

| Quarters ended September 30                              | 2014               | 2013              | change       |
|--|--------------------|-------------------|--------------|
| Revenues   | \$ 520,540         | \$ 1,043,299      | -50%         |
| Realized (loss) gain on swaps – payments (made) received | (20,516)           | (57,706)          | -64%         |
| Operating expenses                                       | (323,950)          | (411,637)         | -21%         |
| General and administrative expenses                      | (273,161)          | (318,584)         | -14%         |
| <b>Cash-Adjusted EBITDA</b>                              | <b>\$ (97,087)</b> | <b>\$ 255,372</b> | <b>-138%</b> |

Cash-adjusted EBITDA decreased \$352,459, or 138% for the first quarter of the fiscal year compared to the prior year period. As noted above, revenues declined 50%, or \$522,759 between the periods. Operating expense decreased \$87,687 between comparable periods due to the sale of properties.

The following table shows the earnings (loss) before interest and taxes (EBIT), which is calculated by deducting non-cash operating expenses from **Adjusted EBITDA**, or by deducting all cash and non-cash operating expenses from revenues. We use EBIT to measure earnings (or losses) after all cash and non-cash expenses, but before taking into account the costs arising from capital structure or taxation.

## EBIT

| Quarters ended September 30                             | 2014                | 2013              | change       |
|---|---------------------|-------------------|--------------|
| <b>Cash-Adjusted EBITDA</b>                             | <b>\$ (97,087)</b>  | <b>\$ 255,372</b> | <b>-138%</b> |
| Change in fair value of embedded derivative liabilities | -                   | (581,693)         | -            |
| Depletion, depreciation and amortization                | 170,998             | 161,725           | 6%           |
| Loss on impairment or sale of property and equipment    | 45,661              | 101,839           | -55%         |
| Restructuring costs                                     | 153,566             | -                 | -            |
| Share-based compensation                                | 32,152              | 34,092            | -6%          |
| Unrealized (gain) loss on hedges                        | (310,076)           | 250,179           | 224%         |
| <b>Earnings (loss) before interest and taxes</b>        | <b>\$ (189,388)</b> | <b>\$ 289,230</b> | <b>-165%</b> |

EBIT declined 165% to \$189,388 loss for the first quarter of the fiscal year compared to the prior year period. The principal driver was a \$506,026 decrease in EBITDA noted above. In the first quarter of the prior fiscal year the fair value of embedded derivative liabilities (broker warrants) decreased \$581,693. All outstanding broker warrants expired unexercised in the fourth quarter of the prior fiscal year. The unrealized value of hedges (oil swaps) increased \$310,076 in the first quarter of the current fiscal year compared to \$250,179 loss in the same period of the prior year. See Note 8 of the Company's September 30, 2014 interim consolidated financial statements for information concerning its outstanding oil swaps.

The following table shows the consolidated statements of comprehensive income of the Company:

**CONSOLIDATED STATEMENTS OF  
OPERATIONS AND COMPREHENSIVE (LOSS) INCOME**

| Quarters ended September 30                             | 2014                | 2013                |
|---|---------------------|---------------------|
| Sales   | \$ 545,653          | \$ 1,093,199        |
| Production taxes  | (25,113)            | (49,900)            |
| <b>Total revenues</b>                                   | <b>\$ 520,540</b>   | <b>\$ 1,043,299</b> |
| Change in fair value of embedded derivative liabilities | -                   | (581,693)           |
| Depreciation, depletion and amortization                | 170,998             | 161,725             |
| General and administrative expenses                     | 273,161             | 318,584             |
| Loss on impairment or sale of property and equipment    | 45,661              | 101,839             |
| Operating expenses                                      | 323,950             | 411,637             |
| Realized (gain) loss on hedges                          | 20,516              | 57,706              |
| Share-based compensation                                | 32,152              | 34,092              |
| Restructuring costs                                     | 153,566             | -                   |
| Unrealized (gain) loss on hedges                        | (310,076)           | 250,179             |
| <b>EBIT</b>   | <b>(189,388)</b>    | <b>289,230</b>      |
| Financial expenses                                      | 54,165              | 77,245              |
| <b>Net comprehensive income (loss)</b>                  | <b>\$ (243,553)</b> | <b>\$ 211,985</b>   |

Financial expenses for the first quarter of the fiscal year declined \$21,471, or 28% compared to the first quarter of the prior fiscal year as subordinate notes were paid in full and bank debt was reduced \$3 million in the quarter.

Net loss for the first quarter of the fiscal year was \$243,553 compared to \$211,985 net income for the prior fiscal year period as Cash-Adjusted EBITDA (see above table) decreased 138%, or \$352,459 and net non-cash expenses increased \$126,159 from the comparable period.

## OPERATIONS PERFORMANCE OVERVIEW

The following table shows production and revenue information from the Company's properties:

### PRODUCTION SUMMARY

| Quarters ended September 30                                     | 2014              | 2013        | change |
|---|-------------------|-------------|--------|
| Total gross production to the Company's revenue interests (BOE) | 6,545             | 13,066      | -50%   |
| Average sale price (\$/BOE)                                     | 83.37             | 83.67       | -      |
| <b>Gross revenues</b>   | <b>\$ 545,653</b> | \$1,093,199 | -50%   |
| Production taxes  | (25,113)          | (49,900)    | -50%   |
| <b>Total revenues</b>   | <b>\$ 520,540</b> | \$1,043,299 | -50%   |

In the Company's financial statements, only revenues and production taxes to the Company's interests that it receives or pays are accounted for.

During the first quarter of the fiscal year, 99% of the Company's sales were from oil production and 1% of its sales were from natural gas production. For each barrel sold by the Company during the period, the average sales price was \$91.52. For each Mcf of natural gas sold during the period the average sales price was \$1.34. This calculates to an average sales price per BOE of \$83.37. After royalties and production taxes were paid, the Company received an average \$68.75 per barrel of oil and \$1.07 per Mcf of natural gas, for an average of \$62.81 per BOE.

The following tables show the Company's oil and natural gas netbacks:

### OIL AND NATURAL GAS NETBACK

| Quarters ended September 30        | 2014         | 2013   | change | 2014          | 2013   | change |
|------------------------------------|--------------|--------|--------|---------------|--------|--------|
|                                    | \$/bbl       | \$/bbl |        | \$/Mcf        | \$/Mcf |        |
| Average sale price                 | 91.52        | 98.74  | -7%    | 1.43          | 3.88   | -63%   |
| Royalties and production taxes     | 22.77        | 25.36  | -10%   | .35           | .98    | -64%   |
| Production and operations expenses | 42.52        | 29.37  | 45%    | 1.09          | .87    | 25%    |
| <b>Netback</b>                     | <b>26.23</b> | 44.01  | -40%   | <b>(0.01)</b> | 2.03   | -100%  |

Oil netbacks declined in the current quarter of this fiscal year versus the comparable quarter last year. This decline is the result of 1) \$7.22 decrease in the average price of oil and 2) operating costs incurred, but no production, on the South Texas property before the property's sale effective August 1, 2014. The Company also sold a majority of its interest in the Texas Reef property and retained a non-operating working interest and overriding royalty interest. During the quarter Texas Reef operating costs were high and production was curtailed as the new operator reworked some of the wells. Higher netbacks from Texas Reef are expected in the future as the wells are returned to production.

The average price for natural gas declined \$2.45 to \$1.43 per MCF. As noted above, gas production from the retained interest in the Texas Reef property was minimal and operating costs were unusually high. There was no production from the more liquids rich South Texas property, which was sold effective August 1, 2014.



## QUARTERLY OPERATING INFORMATION

The following tables summarize key financial and operating information by quarter:

### QUARTERLY OPERATING INFORMATION

#### October 1, 2013 to September 30, 2014

| Quarters ended                                   | Dec. 31, 2013       | Mar. 31, 2014       | Jun. 30, 2014         | Sep. 30, 2014       |
|--|---------------------|---------------------|-----------------------|---------------------|
| Production (BOE) <sup>(1)</sup>                  | 13,355              | 14,492              | 12,060                | 6,545               |
| Avg. price to Company's interests (\$/BOE)       | 76.02               | 74.12               | 75.77                 | 83.37               |
| <b>Oil and natural gas revenues</b>              | <b>\$ 1,015,237</b> | <b>\$ 1,125,956</b> | <b>\$ 913,764</b>     | <b>\$ 545,653</b>   |
| Production taxes                                 | (47,368)            | (51,830)            | (41,466)              | (25,113)            |
| <b>Total revenues</b>                            | <b>967,869</b>      | <b>1,074,126</b>    | <b>872,298</b>        | <b>520,540</b>      |
| Realized gain (loss) on hedges                   | 30,124              | (18,483)            | (57,291)              | (20,516)            |
| Cash operating income (expenses)                 | (673,987)           | (743,495)           | (710,738)             | (597,111)           |
| <b>Cash-Adjusted EBITDA</b>                      | <b>324,006</b>      | <b>312,148</b>      | <b>104,269</b>        | <b>(97,087)</b>     |
| Non-cash operating income (expenses)             | (195,159)           | (209,133)           | (131,547)             | (203,150)           |
| Other income (expenses)                          | 370,171             | (113,901)           | (4,706,431)           | 110,849             |
| <b>Earnings (loss) before interest and taxes</b> | <b>499,018</b>      | <b>(10,886)</b>     | <b>(4,733,709)</b>    | <b>(189,388)</b>    |
| Financial (expenses)                             | (74,267)            | (112,913)           | (105,730)             | (54,165)            |
| <b>Net comprehensive income (loss)</b>           | <b>\$ 424,751</b>   | <b>\$ (123,799)</b> | <b>\$ (4,839,439)</b> | <b>\$ (243,553)</b> |

#### October 1, 2012 to September 30, 2013

| Quarters Ended                                   | Dec. 31, 2012       | Mar. 31, 2013     | Jun. 30, 2013       | Sep. 30, 2013       |
|--|---------------------|-------------------|---------------------|---------------------|
| Production (BOE) <sup>(1)</sup>                  | 21,725              | 12,417            | 12,449              | 13,065              |
| Avg. price to Company's interests (\$/BOE)       | 70.51               | 69.15             | 80.49               | 83.67               |
| <b>Oil and natural gas revenues</b>              | <b>\$ 1,531,774</b> | <b>\$ 861,096</b> | <b>\$ 1,002,057</b> | <b>\$ 1,093,199</b> |
| Royalties and production taxes                   | (71,580)            | (39,041)          | (45,644)            | (49,900)            |
| <b>Total revenues</b>                            | <b>1,460,194</b>    | <b>822,055</b>    | <b>956,413</b>      | <b>1,043,299</b>    |
| Realized gain (loss) on hedges                   | 185,234             | 61,876            | 64,019              | (57,706)            |
| Cash operating income (expenses)                 | (1,398,455)         | (525,865)         | (780,748)           | (730,221)           |
| <b>Cash-Adjusted EBITDA</b>                      | <b>246,973</b>      | <b>358,066</b>    | <b>239,684</b>      | <b>255,372</b>      |
| Non-cash operating income (expenses)             | (249,414)           | (230,145)         | (290,019)           | (195,817)           |
| Other income (expenses)                          | 230,355             | 654,117           | (802,961)           | 229,675             |
| <b>Earnings (loss) before interest and taxes</b> | <b>227,914</b>      | <b>782,038</b>    | <b>(853,296)</b>    | <b>289,230</b>      |
| Financial (expenses)                             | (161,845)           | (112,048)         | (102,134)           | (77,245)            |
| <b>Net comprehensive income (loss)</b>           | <b>\$ 66,069</b>    | <b>\$ 669,990</b> | <b>\$ (955,430)</b> | <b>\$ 211,985</b>   |

(1) Production (BOEs) are to the Company's net revenue interests.

The numbers contained in the above two tables differ slightly from those in the prior published management's discussions and analyses, as certain numbers have been reclassified into the same lines for consistency, while others were adjusted to reconcile with the consolidated annual audited financial statements under IFRS for the year ended June 30, 2013.

## HEDGING

To hedge risks associated with a decline in oil prices, the Company has entered into “production swaps” and purchased “price floors”, which consist of series of put options. As of the date hereof, the Company has the following hedges:

| Contract Month                     | Production Swaps |                       |
|------------------------------------|------------------|-----------------------|
|                                    | Avg. Price (\$)  | Quantity (bbls/Month) |
| October 2014 through December 2014 | 98.25            | 1,250                 |
| January 2015 through December 2015 | 87.32            | 1,150                 |

## LIQUIDITY AND CAPITAL RESOURCES

### *Working Capital and Source of Funds*

As at September 30, 2014, the current ratio of the Company was 2.27, which is the result of \$2,437,114 of current assets divided by \$1,074,224 of current liabilities. The bank loan facility had a balance of \$1.75 million at September 30, 2014, which is fully drawn.

Given the current market price for the Company’s shares, the Company generally views issuing equity as highly dilutive and not likely to result in the accretion of value once any funds are invested. The Company has made overhead and payroll reductions effective on November 1, 2014, following which the Company will be roughly cash-flow neutral from operations. Any available cash will sparingly be used by the Company to invest in crucial development projects to enhance or protect asset values.

## SHARES ISSUED & OUTSTANDING, OPTIONS & WARRANTS

The following table summarizes the equity structure of the Company as of June 30, 2014 and as of the date hereof:

| Security                                       | Quantity<br>Sept 30, 2014 | Quantity<br>Nov 25, 2014 | Aggregate<br>Strike Value (CA\$) |
|--|---------------------------|--------------------------|----------------------------------|
| Common shares                                  | 79,317,121                | 79,996,804               | -                                |
| Preferred shares <sup>(1)</sup>                | 10,708,386                | 10,028,703               | -                                |
| <b>Total direct ownership</b>                  | <b>90,025,507</b>         | <b>90,025,507</b>        | -                                |
| Options at \$0.15 expiring February 1, 2015    | 3,700,000                 | 600,000                  | 90,000                           |
| Options at \$0.06 expiring 2019 <sup>(2)</sup> | -                         | 7,300,000                | 438,000                          |
| <b>Total fully diluted</b>                     | <b>93,725,507</b>         | <b>97,925,507</b>        | <b>\$ 528,000</b>                |

(1) The preferred shares are convertible into common shares of the Company on a 1:1 basis.

(2) These options expire the later of 90 days following the termination of employment of the grantee, or 365 following the closing of a strategic transaction.

## OUTLOOK

With a view towards a strategic alternative, the Company has invested in additional in-depth engineering and geological studies of key properties, as well as in development capital spending to improve production and profitability of key assets, and moved to sell such assets to free-up capital. The Company is seeking to conclude a strategic transaction in the near-term that will re-value the Company in the market or provide a liquidity event to shareholders at a premium to market.

As always, the Company's value is highly dependent on the strength of oil and natural prices. However, barring any significant decline in these resource prices, the Company's assets are highly-marketable in both the private and public markets. We therefore expect to garner significant interest in a strategic transaction from either prospective buyers or merger candidates, either of which should unlock significant value for shareholders.

## ACCOUNTING AND DISCLOSURE/RISKS AND UNCERTAINTIES


The Company's accounting and disclosure controls and policies, as well as the significant risks and uncertainties which may have an impact on the Company's business, can be found in the Company's management discussion and analysis and consolidated annual audited financial statement as at and for the year ended June 30, 2014.

## ADDITIONAL INFORMATION

The Company is an issuer in accordance with the securities legislations of all the Canadian provinces; therefore it has the obligation to deliver financial statements, proxy circulars and annual notices to the various regulating authorities. You can obtain a copy of such documents free of charge by sending your requests to the Company or by visiting [www.SEDAR.com](http://www.SEDAR.com).



Michael McLellan, CFA  
Chief Executive Officer



Don DeMoss, CPA  
Chief Financial Officer