Iona Energy Inc.
Condensed Consolidated Financial Statements - Unaudited
For the three month period ended March 31, 2014

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Iona Energy Inc.
Condensed Consolidated Statements of Financial Position - Unaudited

(In thousands of US dollars)	Notes		March 31, 2014		December 31, 2013
ASSETS					
Current Assets					
Cash and cash equivalents		**$**	**34,713**	$	19,808
Accounts receivable			**14,638**		15,126
Prepaid expenses			**916**		551
Restricted cash	6		**74,909**		78,024
Inventory			**2,524**		1,802
Derivative instruments	14		**-**		293
Total Current Assets			**127,700**		115,604
Restricted cash	6		**7,088**		7,090
Exploration and evaluation assets	7		**139,653**		134,163
Property and equipment	8		**256,660**		274,164
Goodwill			**14,058**		14,058
Total Non-Current Assets			**417,459**		429,475
Total Assets		**$**	**545,159**	$	545,079
LIABILITITES AND SHAREHOLDERS' EQUITY					
Current Liabilities					
Accounts payable and accrued liabilities	6	**$**	**17,287**	$	19,662
Current derivative liabilities	14		**21,637**		16,867
Total Current Liabilities			**38,924**		36,529
Non-Current Liabilities					
Secured bonds	9		**263,629**		262,450
Decommissioning liabilities	10		**18,922**		17,763
Derivative liabilities	14		**25,687**		31,038
Deferred tax liability			**6,164**		5,111
Total Non-Current Liabilities			**314,402**		316,362
Total Liabilities			**353,326**		352,891
Shareholders' Equity					
Share capital	11		**177,359**		177,359
Contributed surplus			**10,189**		10,151
Accumulated other comprehensive loss			**(8,110)**		(8,055)
Retained earnings			**12,395**		12,733
Total Shareholders' Equity			**191,833**		192,188
Total Liabilities and Shareholders' Equity		**$**	**545,159**	$	545,079

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

Iona Energy Inc.
Condensed Consolidated Statements of Operations and Comprehensive Loss - Unaudited

(In thousands of US dollars, except for per share amounts)	Notes		Three Months Ended March 31 2014		Three Months Ended March 31 2013
Revenues	3	$	**35,648**	$	1,858
Operating costs	4		**(6,508)**		(796)
Depletion	4		**(18,928)**		(966)
Gross Profit			**10,212**		96
Expenses					
General and administrative			**(1,346)**		(3,390)
Exploration and evaluation costs	7		**(199)**		(286)
Transaction costs			**(633)**		(949)
Gain on acquisition			**-**		6,605
Total Expenses			**(2,178)**		1,980
Income before other expenses			**8,034**		2,076
Gain / (loss) on risk management contracts	14		**288**		(23,687)
Other finance costs			**(7,788)**		(799)
Finance income			**2**		8
Foreign exchange gain			**181**		239
Net income / (loss) before tax			**717**		(22,163)
Income tax recovery (expense)			**(1,055)**		10,218
Net Loss			**(338)**		(11,945)
Unrealized foreign exchange gain (loss) on net investments			**5,519**		(5,811)
Exchange gain (loss) on re-translation of foreign operations			**(5,574)**		400
Comprehensive Loss for the Period		$	**(393)**	$	(17,356)

Net loss per share				
- basic	$	**(0.00)**	$	(0.03)
- diluted	$	**(0.00)**	$	(0.03)
Weighted average shares outstanding				
- basic		**366,830,868**		342,596,818
- diluted		**366,830,868**		342,596,818

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

Condensed Consolidated Statements of Changes in Shareholders' Equity - Unaudited

(In thousands of US dollars)		Share Capital	Contributed Surplus	Accumulated other Comprehensive Income (Loss)	Retained Earnings		Total Equity
Balance December 31, 2013	$	177,359	10,151	(8,055)	12,733	$	192,188
Net loss for the period		-	-	-	(338)		(338)
Stock based payments		-	38	-	-		38
Foreign currency translation		-	-	(5,574)	-		(5,574)
Unrealized foreign exchange on investment		-	-	5,519	-		5,519
Issue of shares (net of issue costs)		-	-	-	-		-
Balance March 31, 2014	$	177,359	10,189	(8,110)	12,395	$	191,833

(In thousands of US dollars)		Share Capital	Contributed Surplus	Accumulated other Comprehensive Income (Loss)	Retained Earnings (Deficit)		Total Equity
Balance December 31, 2012	$	156,599	6,208	2,139	(16,733)	$	148,213
Net loss for the period		-	-	-	(11,945)		(11,945)
Stock based payments		-	1,566	-	-		1,566
Foreign currency translation		-	-	(5,811)	-		(5,811)
Unrealized foreign exchange on investment		-	-	400	-		400
Issue of shares (net of issue costs)		17,854	-	-	-		17,854
Balance March 31, 2013	$	174,453	7,774	(3,272)	(28,678)	$	150,277

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

Iona Energy Inc.
Condensed Consolidated Statements of Cash Flows - Unaudited

(In thousands of US dollars)	Notes		Three Months Ended March 31 2014		Three Months Ended March 31 2013
Cash flows from / (used in) operating activities					
Net loss for the period		$	**(338)**	$	(11,945)
Items not involving cash:					
Depletion, depreciation and amortization			**18,941**		966
Unrealized FX gain / loss			**(108)**		-
Accretion			**-**		67
Gain on acquisition			**-**		(6,605)
Unrealized (gain) loss on fair value of derivative instruments	14		**(288)**		16,339
Amortization of loan costs			**-**		26
Income tax recovery (expense)			**1,055**		(10,219)
Share based payments			**38**		1,707
Finance costs			**7,788**		-
			27,088		(9,664)
Changes in non-cash working capital balances:					
Accounts receivable			**488**		1,204
Prepaid expenses			**(365)**		(825)
Inventory			**(127)**		-
Accounts payable and accrued liabilities			**893**		728
Cash flow used in operating activities			**27,977**		(8,557)
Cash flows from / (used in) financing activities					
Issue of common shares, net of issue costs			**-**		21,208
Derivative call options sold			**-**		60,859
Bank loan draw down, net of costs			**-**		136,290
Bank fees and other interest charges			**1**		-
Interest on bond			**(13,063)**		-
Repayment of subsidiary loans and derivatives			**-**		(56,690)
Cash flow from financing activities			**(13,062)**		161,667
Cash flows from / (used in) investing activities					
Expenditures on property and equipment			**(777)**		-
Expenditures on exploration and evaluation			**(2,404)**		(11,650)
Expenditure on acquisition of Orlando interest			**-**		(46,439)
Purchase of Huntington oil field			**-**		(118,628)
Disposal of exploration and evaluation assets			**-**		37,394
Restricted cash			**3,116**		1,082
Cash flow used in investing activities			**(65)**		(138,241)
Effect of exchange rate changes on cash			**55**		(626)
Increase in cash			**14,905**		14,243
Cash and cash equivalents, beginning of period			**19,808**		15,378
Cash and cash equivalents, end of period		$	**34,713**	$	29,621

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

(Unaudited - Tabular amounts are expressed in thousands US dollars, except per share amounts or amounts as otherwise noted.)

1. Corporate Information

Iona Energy Inc. ("Iona" or "the Company") is a publicly traded junior oil and gas company on the TSX Venture Exchange ("TSX-V") under the symbol INA engaged in the evaluation, acquisition, exploration and development of oil and gas properties in the United Kingdom's North Sea and in Alaska.

The registered office of the Company is located at 1600, 333-7th Avenue S.W., Calgary, Alberta, T2P 2Z1.

The following sets out the subsidiaries of the Company and the Company's ownership interest in those subsidiaries:

Name of Subsidiary	Jurisdiction of Incorporation	Ownership
Iona Energy Company (US) Limited	Delaware, USA	100%
Iona Energy Company (UK) plc	United Kingdom	100%
Iona UK Huntington Ltd.	United Kingdom	100%
Iona UK Developments Co Limited	United Kingdom	100%

2. Basis of Presentation

Statement of compliance

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

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

Basis of preparation

Except as noted below, the condensed consolidated financial statements have been prepared using the same accounting policies and methods, including significant judgments and estimates as those disclosed in the consolidated financial statements for the year ended December 31, 2013. These condensed consolidated financial statements should be read in conjunction with the Company's consolidated financial statements for the year ended December 31, 2013.

Change in presentation currency

In 2013, the Company changed its presentation currency from the Canadian dollars ("CAD") to the US dollar. These consolidated financial statements are presented in US dollars, which is the Company's presentation currency. In accordance with IAS 21, the financial statements for all years and periods presented have been translated to the new US dollar presentation currency. For the 2013 comparative balances the statements of comprehensive income (loss) were translated at the average exchange rates for the reporting period, or at the exchange rates prevailing at the date of transactions. Exchange differences arising on translation were taken to the foreign currency translation reserve in shareholders' equity. The resulting effect of the change in presentation currency of $388,000 on the comparative figures is reflected in the accumulated other comprehensive income at March 31, 2013.

(Unaudited - Tabular amounts are expressed in thousands US dollars, except per share amounts or amounts as otherwise noted.)

Basis of Presentation - continued

Changes in accounting policies

As of January 1, 2014, the Company adopted several new IFRS interpretations and amendments in accordance with the transitional provisions of each standard. A brief description of each new accounting policy and its impact on the Company's financial statements follows below:

- IAS 36 "Impairment of Assets" has been amended to reduce the circumstances in which the recoverable amount of cash generating units "CGUs" is required to be disclosed and clarify the disclosures required when an impairment loss has been recognized or reversed in the period. The retrospective adoption of these amendments will only impact Iona's disclosures in the notes to the financial statements in periods when an impairment loss or impairment reversal is recognized.

- IFRIC 21 "Levies" was developed by the IFRS Interpretations Committee ("IFRIC") and is applicable to all levies imposed by governments under legislation, other than outflows that are within the scope of other standards (e.g., IAS 12 "Income Taxes") and fines or other penalties for breaches of legislation. The interpretation clarifies that an entity recognizes a liability for a levy when the activity that triggers payment, as identified by the relevant legislation, occurs. It also clarifies that a levy liability is accrued progressively only if the activity that triggers payment occurs over a period of time, in accordance with the relevant legislation. Lastly, the interpretation clarifies that a liability should not be recognized before the specified minimum threshold to trigger that levy is reached. The retrospective adoption of this interpretation does not have any impact on Iona's financial statements.

3. Revenue

		Three Months Ended March 31, 2014	Three Months Ended March 31, 2013
Oil sales	$	**31,268**	-
Gas sales		**4,380**	1,858
	$	**35,648**	1,858

4. Cost of sales

		Three Months Ended March 31, 2014	Three Months Ended March 31, 2013
Operating expenses	$	**6,508**	796
Depletion		**18,928**	966
	$	**25,436**	1,762

(Unaudited - Tabular amounts are expressed in thousands US dollars, except per share amounts or amounts as otherwise noted.)

5. Segmented Information

The Company's reportable segments and geographical segments are the United Kingdom (North Sea) and the United States. The corporate reportable segment includes the Company's corporate and financing activities.

The accounting policies used for the reportable segments are the same as the Company's accounting policies. For the purposes of monitoring segment performance and allocating resources between segments, the Company's executive officers monitor the tangible, intangible and financial assets attributable to each segment. All assets are allocated to reportable segments. The following tables show information regarding the Company's segments.

	Three Month Period Ended March 31, 2014			
	United Kingdom	United States	Corporate	Total
Revenue	35,648	-	-	**35,648**
Cost of sales, including DD&A	(25,436)	-	-	**(25,436)**
Gross Profit	10,212	-	-	**10,212**
Other expenses, gain on acquisition, net finance costs	(9,282)	(24)	(189)	**(9,495)**
Taxation – recovery / expense	(1,055)	-	-	**(1,055)**
Net income (loss)	(125)	(24)	(189)	**(338)**
	As at March 31, 2014			
Total assets	543,125	938	1,096	**545,159**
Total liabilities	353,011	-	315	**353,326**

	Three Month Period Ended March 31, 2013			
	United Kingdom	United States	Corporate	Total
Revenue	1,858	-	-	**1,858**
Cost of sales, including DD&A	(1,762)	-	-	**(1,762)**
Gross Profit	96	-	-	**96**
Other expenses, gain on acquisition, net finance costs	(19,994)	-	(2,265)	**(22,259)**
Taxation - recovery	10,218	-	-	**10,218**
Net income (loss)	(9,680)	-	(2,265)	**(11,945)**
	As at March 31, 2013			
Total assets	500,291	921	3,377	**504,589**
Total liabilities	352,814	-	1,496	**354,310**

6. Restricted Cash

Current

As of March 31, 2014, the Company had a current asset of $74,909,000 (December 31, 2013 - $78,024,000) of restricted cash related to bond proceeds. The bond proceeds can be utilized to retire tranches of call options sold to Britannic Trading Limited and capital expenditure on the development of Orlando and Kells (Note 9). Upon confirmation that both Orlando and Kells have reached first oil any remaining funds will become unrestricted.

(Unaudited - Tabular amounts are expressed in thousands US dollars, except per share amounts or amounts as otherwise noted.)

6. Restricted Cash - continued

As per the terms of the Bond Agreement, $5,335,000 of the $16,834,000 in accounts payable can be paid out of restricted cash.

Non-Current

At March 31, 2014 and December 31, 2013, the Company had $52,000 of cash held as deposits for work commitment guarantees contained in exploration contracts in Alaska in the United States.

At March 31, 2014, the Company had $7,036,000 of restricted cash (December 31, 2013 - $7,038,000) held for the Company's decommissioning liabilities on the Trent & Tyne properties.

7. Exploration and Evaluation Assets and Deferred Costs

	Total E&E	Deferred Costs
As at December 31, 2012	136,048	38,552
Additions	22,041	-
Acquisitions	14,461	-
Deposit on business combination	-	(6,000)
Transfers to property, plant and equipment	(293)	(32,819)
Exchange differences	(1,294)	267
Disposals	(36,800)	-
As at December 31, 2013	134,163	-
Additions	5,490	-
As at March 31, 2014	**139,653**	-

General E&E

During the three months ended March 31, 2014, the Company expensed $199,000 (2013 - $286,000) of exploration and evaluation costs. The additions to general E&E mainly relates to development expenditure on both the Orlando and Kells fields.

(Unaudited - Tabular amounts are expressed in thousands US dollars, except per share amounts or amounts as otherwise noted.)

8. Property and Equipment

	Development & Production Oil and Gas Assets	Other Fixed Assets	Total
Cost			
At December 31, 2013	331,919	170	332,089
Additions	1,981	9	1,990
At March 31, 2014	**333,900**	**179**	**334,079**
Accumulated depletion, depreciation and amortization			
At December 31, 2013	34,768	74	34,842
Charge for the period	19,480	14	19,494
At March 31, 2014	**54,248**	**88**	**54,336**
Accumulated impairment as at December 31, 2013	**23,580**	**-**	**23,580**
Exchange differences	497	-	497
Carrying value at December 31, 2013	274,068	96	274,164
Carrying value at March 31, 2014	**256,569**	**91**	**256,660**

9. Senior Debt Instruments

As disclosed in Note 12 of the annual audited financial statements for the year ended December 31, 2013, Iona UK issued $275 million in senior secured bonds (the “Bonds”) on September 27, 2013, net of discounts of $6.9 million and transaction cost of $8 million, for $260 million. As at March 31, 2014 the fair value of the Bonds were $275 million (December 31, 2013 - $275 million). The bonds mature on September 30, 2018. The Bonds carry an annual coupon rate of 9.5% payable semi-annually, were issued at 97.5% of par and are callable in whole or in part at the option of Iona UK at any time. Commencing 30 months after September 30, 2013, the Bonds will be repaid at 15% of the face value every six months with a 25% final payment at maturity plus a specified premium. The Bonds amortization schedule is as follows:

(Unaudited - Tabular amounts are expressed in thousands US dollars, except per share amounts or amounts as otherwise noted.)

9. Senior Debt Instruments - continued

Payment date	Nominal instalment amount	Premium on nominal instalment
March 2016	41,250,000	5%
September 2016	41,250,000	4%
March 2017	41,250,000	4%
September 2017	41,250,000	3%
March 2018	41,250,000	3%
September 2018 (Maturity)	68,750,000	2%

Under the Bond Agreement, capital expenditures are limited to assets within the borrowing base (currently Huntington, Trent & Tyne, Orlando, Kells, Ronan and Oran). Under the Bond Agreement a working interest of at least fifty percent must be maintained in Orlando and Kells. Additionally no sale or disposal of any (direct or indirect) ownership interest in the Huntington Asset shall be permitted during the term of the Bonds as long as any call options are outstanding under the BP Structured Energy Derivative.

Under the Bond Agreement the Company must maintain, as calculated quarterly:

- liquidity (defined as the restricted group's cash and cash equivalents) of at least $30 million,
- a leverage ratio (defined as net interest bearing debt divided by twelve months of earnings before interest, taxes, depreciation and amortization ("EBITDA") of not more than 3.0x, and
- ensure a minimum of both the capital employed ratio (defined as equity divided by the sum of equity and net interest bearing debt) and the restricted capital employed ratio (defined as restricted group equity divided by the sum of restricted group equity and net interest bearing debt) of 40% until from December 31, 2016, and minimum 50% thereafter.

The restricted group is defined as Iona UK and Iona UK Huntington Ltd.

Under the Bond Agreement an event of default constitutes two consecutive quarterly covenant violations. The quarter ended December 31, 2013 is the first quarter that the Company is required to maintain the leverage ratio.

The Company was in breach of the Leverage Ratio at December 31, 2013. At March 31, 2014, the Company was in compliance with the leverage ratio due to the amendment to the Bond Agreement dated May 6, 2014 as disclosed in Note 16.

(Unaudited - Tabular amounts are expressed in thousands US dollars, except per share amounts or amounts as otherwise noted.)

9. Senior Debt Instruments - continued

The table below delineates the Company's position with respect to the Bond covenants at March 31, 2014.

	31-March-14	Covenant
Liquidity	$108,701	Greater than $30,000
Restricted Group Capital Employed Ratio	55%	Greater than 40%
Group Capital Employed Ratio	55%	Greater than 40%
Leverage Ratio	2.16	Not greater than 3.0x

The above calculation includes restricted cash in the definition of cash as changed in the amendment to the Bond Agreement effected May 6, 2014, as disclosed in Note 16.

The Bonds are secured against the assets of the Company and its subsidiaries.

The effective interest rate on the bond at March 31, 2014 was 12.16%.

Balance, December 31, 2013	262,450
Amortization of discount and transaction costs	1,179
As at March 31, 2014	$ 263,629

10. Decommissioning Liabilities

Balance December 31, 2012	659
Acquisitions	12,579
Additions	4,220
Change in estimate and discount rate	(133)
Accretion	438
Balance December 31, 2013	17,763
Change in estimate and discount rate	1,055
Accretion	104
Balance March 31, 2014	**18,922**

The total future decommissioning liability was calculated by management based on its net ownership interest in the Orlando, Trent & Tyne and Huntington fields and the estimated costs to be incurred in future periods to reclaim and abandon the wells. The decommissioning liability was measured using pre-tax, risk-free discount rates ranging from 1.85% to 3.39% percent and an inflation rate of 2.00% percent over the estimated life of the asset to calculate the present value of the decommissioning liability. The costs are expected to be incurred at various intervals over the next 18 years.

(Unaudited - Tabular amounts are expressed in thousands US dollars, except per share amounts or amounts as otherwise noted.)

11. Share Capital

The Company has authorized an unlimited number of Common shares, without nominal or par value and unlimited number of Preferred shares, issuable in series. The Company, as at March 31, 2014 had the following common shares, warrants and share options outstanding:

Common shares	Shares	Amounts
Opening balance, December 31, 2013	**366,830,868**	**$ 177,359**
Issued for cash	-	-
Share issue costs	-	-
Ending Balance, March 31, 2014	**366,830,868**	**$ 177,359**

Date of Grant	Number Outstanding	Exercise Price CAD$	Weighted Average Remaining Contractual Life	Date of Expiry	Number Exercisable March 31, 2014
May 31, 2011	7,850,000	$0.60	1.17 years	May 31, 2015	5,887,500
November 25, 2011	75,000	$0.60	1.66 years	November 25, 2015	75,000
April 13, 2012	13,745,000	$0.57	3.04 years	April 12, 2017	6,910,000
January 10, 2013	175,000	$0.59	3.78 years	January 10, 2018	175,000
March 5, 2013	5,452,500	$0.63	3.93 years	March 5, 2018	2,747,500
July 29, 2013	700,000	$0.59	4.33 years	July 29, 2018	175,000
October 23, 2013	600,000	$0.63	4.57 years	October 23, 2018	150,000
	28,597,500				16,120,000

Iona did not issue any new options in Q1 2014.

The Company's share options granted, other than the 175,000 share options granted to person retained to provide investor relations activities, which vest as to ¼ immediately and ¼ on each of the dates three months, six months and nine months thereafter, vest as follows: ¼ immediately and ¼ vesting on the first, second and third anniversary dates and expire five years from the date of issue. The fair value of the issued options was estimated using the Black Scholes option pricing model with the following assumptions:

	March 31, 2014
Average expected volatility	54% - 75%
Risk-free rate	1.72% - 3.50%
Expected life	5 years

An estimated forfeiture rate of 5% is used when recording share based payments.

12. Related Party Transactions

During the three months ended March 31, 2014, the Company was charged $50,000 (2013 - $355,000), in legal fees of which $NIL (2013 - $96,000) related to share issuance costs by a law firm where a director of the Company is a partner, of which $29,000 is included in accounts payable and accrued liabilities as at March 31, 2014 and $29,000 as at December 31, 2013.

(Unaudited - Tabular amounts are expressed in thousands US dollars, except per share amounts or amounts as otherwise noted.)

12. Related Party Transactions - continued

Included in accounts receivable is $117,483 (2013 - $265,000) due from a former officer and director of the Company who resigned from the Company's management team and Board. Of this amount $117,483 remains to be collected as at March 31, 2014. The amounts owing are non-interest bearing and secured. The Company expects full repayment of the remaining balances in 2014.

All related party transactions are in the normal course of operations and have been measured at the agreed to exchange amounts, which is the amount of consideration established and agreed to by the related parties.

13. Commitments and Contingencies

Based on management's best estimate, the Company has the following contractual obligations:

	March 31, 2014				
	Payments Due in Period				
Contractual Obligations	**Total**	**Less than 1 Year**	**1 to 3 Years**	**3 to 5 Years**	**More than 5 Years**
U.S. Segment					
Exploration leases	**204**	17	51	51	85
UK Segment					
Office lease	**130**	87	43	-	-
Drilling, completion, facility construction	**18,013**	18,013	-	-	-
Total UK Segment	**18,143**	18,100	43	-	-
Corporate Segment					
Office lease	**10**	10	-	-	-
Total Contractual Obligations	**18,357**	18,127	94	51	85

14. Financial Instruments and Risk Management Contracts

To estimate fair value of the risk management contracts, the Company uses quoted market prices when available, or industry accepted third-party models and valuation methodologies that utilize observable market data. In addition to market information, the Company incorporates transaction specific details that market participants would utilize in a fair value measurement, including the impact of non-performance risk. The Company characterizes inputs used in determining fair value using a hierarchy that prioritizes inputs depending on the degree to which they are observable. However, these fair value estimates may not necessarily be indicative of the amounts that could be realized or settled in a current market transaction.

The three levels of the fair value hierarchy are as follows:

• Level 1 - inputs represent quoted prices in active markets for identical assets or liabilities (for example,

(Unaudited - Tabular amounts are expressed in thousands US dollars, except per share amounts or amounts as otherwise noted.)

14. Financial Instruments and Risk Management Contracts - continued

exchange-traded commodity derivatives). Active markets are those in which transactions occur in sufficient frequency and volume to provide pricing information on an ongoing basis.

• Level 2 - inputs other than quoted prices included within Level 1 that are observable, either directly or indirectly, as of the reporting date. Level 2 valuations are based on inputs, including quoted forward prices for commodities, market interest rates, and volatility factors, which can be observed or corroborated in the marketplace.

• Level 3 - inputs that are less observable, unavailable or where the observable data does not support the majority of the instrument's fair value.

In forming estimates, the Company utilizes the most observable inputs available for valuation purposes. If a fair value measurement reflects inputs of different levels within the hierarchy, the measurement is categorized based upon the lowest level of input that is significant to the fair value measurement. The valuation of puts and calls is based on similar transactions observable in active markets or industry standard models that primarily rely on market observable inputs. Substantially all of the assumptions for industry standard models are observable in active markets throughout the full term of the instrument. These are categorized as Level 2 and are designated as held-for-trading.

The following table presents the Company's material financial instruments measured at fair value for each hierarchy level as of 31 March 2014:

	Level 1	Level 2	Level 3	Total Fair Value
Current assets				
Derivative financial assets	-	-	-	-
Current liabilities				
Derivative financial instrument liabilities	-	21,637	-	21,637
Non-current liabilities				
Derivative financial instrument liabilities	-	25,687	-	25,687

The table below presents the total loss on financial instruments that has been disclosed through the consolidated statement of comprehensive income:

	Three Months Ended March 31, 2014	Three Months Ended March 31 2013
Cost of derivative options	**-**	**(7,348)**
Unrealized gain / (loss) on commodity hedges	**288**	**(16,339)**
Total gain / (loss) on commodity hedges	**288**	**(23,687)**

All other financial assets are classified as loans and receivables and are accounted for on an amortized cost basis. All financial liabilities are classified as other liabilities.

(Unaudited - Tabular amounts are expressed in thousands US dollars, except per share amounts or amounts as otherwise noted.)

14. Financial Instruments and Risk Management Contracts - continued

i) Commodity Risk

The table above presents the total loss on risk management contracts that has been disclosed through the statement of net and comprehensive income. Commodity price risk related to crude oil prices is the Company's most significant market risk exposure. Crude oil prices and quality differentials are influenced by worldwide factors such as OPEC actions, political events and supply and demand fundamentals. The Company is also exposed to natural gas price movements on un-contracted gas sales. Natural gas prices, in addition to the worldwide factors noted above, can also be influenced by local market conditions. The Company's expenditures are subject to the effects of inflation, and prices received for the product sold are not readily adjustable to cover any increase in expenses from inflation.

The Company may periodically use different types of derivative instruments to manage its exposure to price volatility, thus mitigating fluctuations in commodity-related cash flows.

On February 21, 2013, the Company completed a payment swap whereby Iona received $60 million in exchange for granting BTL, the option to purchase 8.1 MMbbl of Brent blend crude from Iona's Orlando, Kells and Huntington fields for a period of five (5) years at an average price of $95.84 per barrel. In conjunction with the payment swap, Iona also entered into a marketing and offtake agreement with BP Oil International Limited in respect of certain quantities of oil expected to be produced from the Company's Orlando and Kells properties.

On September 27, 2013, the Company offset the risk with respect to the 7.4 million remaining call options previously sold to BTL (as noted above) by purchasing 3.1 million call options effective between October 2014 and September 2016 for $33.5 million.

The table below shows Iona's net position on a quarterly basis of the call option structures sold to and bought from BTL on February 21, 2013 and September 30, 2013 respectively.

		Call Options (bbls)			Strike ($/bbl)
		Sold	Bought	Net Position	
2014	Q1	334,687	-	334,687	100
	Q2	338,407	-	338,407	95
	Q3	342,125	-	342,125	95
	Q4	762,818	496,901	265,917	95
2015	Q1	478,397	274,396	204,001	95
	Q2	483,711	334,045	149,666	95
	Q3	489,027	377,830	111,197	95
	Q4	489,027	394,678	94,349	95
2016	Q1	470,470	390,723	79,747	95
	Q2	470,468	401,251	69,217	95
	Q3	475,639	418,356	57,283	95
	Q4	475,639	-	475,639	95
2017	Q1	316,429	-	316,429	95
	Q2	319,946	-	319,946	95
	Q3	323,461	-	323,461	95
	Q4	323,461	-	323,461	95
2018	Q1	187,206	-	187,206	95
Total		7,080,918	3,088,180	3,992,738	

14. Financial Instruments and Risk Management Contracts - continued

ii) Interest Risk

Interest rate risk refers to the risk that the value of a financial instrument or cash flows associated with the instrument will fluctuate due to changes in market interest rates. The Company currently does not use interest rate hedges or fixed interest rate contracts to manage the Company's exposure to interest rate fluctuations.

Assuming all other variables remain constant, a 1% increase or decrease in interest rates would have increased / (decreased) the net loss for the period by $87,000.

iii) Credit Risk

Credit risk is the risk that arises when a party to a financial instrument will be unable to discharge cash, cash equivalents, restricted cash and accounts receivable. Cash, cash equivalents and restricted cash are placed with major financial institutions. The maximum exposure to credit risk is approximate to the carrying value of such financial instruments. The Company does not have an allowance for doubtful accounts as at March 31, 2014, and did not provide for any doubtful accounts nor was it required to write-off any receivables during the period ended March 31, 2014 or 2013.

iv) Foreign Currency Exchange Risk

The Company operates on an international basis and therefore foreign exchange risk exposures arise from transactions denominated in currency other than the Canadian Dollar. The Company is exposed to foreign currency fluctuations as it holds cash and incurs expenditures in property and equipment in foreign currencies. The Company incurs expenditures in Pound sterling, Euros, United States dollars and Canadian dollars and is exposed to fluctuations in exchange rates in these currencies. There are no exchange rate contracts in place as at or during the period ended March 31, 2014, March 31, 2013, or thereafter.

Assuming all other variables remain constant, a 1% increase or decrease in foreign exchange rates on the foreign cash and restricted cash balances at March 31, 2014 would have impacted the net loss and comprehensive loss of the Company for the three month period ended March 31, 2014 by approximately $87,000 (three months ended March 31, 2013 – $347,000).

In addition at March 31, 2014, the Company held approximately $16,049,000 (£9,625,000) (2013- $31,812,000 (£20,884,000)) of accounts payable in Pound Sterling. Assuming all other variables remain constant, a 1% increase or decrease in foreign exchange rates between Pound Sterling and US dollar at March 31, 2014 would impact the net loss and comprehensive loss of the Company for the three month period ended March 31, 2014 by approximately $160,000 (three months ended March 31, 2013 - $320,000).

v) Liquidity Risk

Liquidity risk includes the risk that, as a result of the Company's operational liquidity requirements:

- The Company will not have sufficient funds to settle commitments as they become due;
- The Company will be forced to sell financial assets at a value which is less than what they are worth; or
- The Company may be unable to settle or recover a financial asset.

As the Company's industry is very capital intensive, the majority of the spending is related to the Company's capital programs. The Company's goal is to prudently spend its capital. As circumstances change, liquidity risks may necessitate the Company to issue equity, obtain debt financing, or sell assets. The Company's contractual obligations are included in Note 13 and further details of liquidity are discussed in Note 15.

15. Capital Risk Management

The Company manages its capital with the prime objectives of safeguarding the business as a going concern, creating investor confidence, maximizing long-term returns and maintaining an optimal structure to meet its financial commitments and to strengthen its working capital position. At present, the capital structure of the Company is primarily composed of senior secured bonds and shareholders' equity. The Company's strategy is to access capital primarily through equity issuances and other alternative forms of debt financing. The Company actively manages its capital structure and makes adjustments relative to changes in economic conditions and the Company's risk profile. In order to uphold its capital structure and to meet the liquidity and sufficient funding tests of the senior secured bonds, the Company may from time to time issue shares and adjust its capital spending to manage current working capital levels.

As at March 31, 2014, the Company has net assets of $191.8 million, working capital of $88.8 million and commitments due in the next 12 months as further detailed in Note 13. The Company intends to finance its obligations as they come due from current working capital supplemented by future cash flow generated from operations.

16. Subsequent Events

Subsequent to the quarter end the Company, through its wholly owned UK subsidiary, Iona UK Developments Co Limited, entered into a Sale and Purchase Agreement ("SPA") with Perenco UK Limited ("Perenco"), to purchase Perenco's remaining 80% working interest, rights, and obligations in the Trent & Tyne fields (including the Trent East Discovery Area).

Upon satisfaction of certain conditions as set out in the SPA, the Company shall pay to Perenco the sum of $20,000,000, as adjusted pursuant to any adjustments as per the SPA and assume all decommissioning liabilities in relation to Licenses being purchased. Payment shall be made no later than six (6) calendar months after the date of the SPA or on such later date as agreed in writing.

On May 6, 2014 the bondholders voted in favour of amending the Bond agreement to clarify that restricted cash is included in the definition of cash and cash equivalents. The amendment was effective from the date of issue of the Bonds.

(Unaudited - Tabular amounts are expressed in thousands US dollars, except per share amounts or amounts as otherwise noted.)

17. Adjustment of previously reported financial information due to change in presentation currency

For comparative purposes, the Consolidated Statements of Operations and Comprehensive Loss for the three month period ended March 31 2013 includes adjustments to reflect the change in accounting policy resulting from the change in presentation currency to US dollars. The amounts previously reported in Canadian Dollars as shown below have been translated into US dollars at the average Q1 2013 exchange rate of 0.9921 USD: CAD. The effect of the translation is as follows:

For the three month period ended March 31, 2014	**As previously reported CAD $000**	**As translated at rate of 0.9921 $000**
Revenues	$ 1,873	$ 1,858
Cost of sales, including DD&A	(1,776)	(1,762)
Gross Profit	97	96
Expenses		
General and administrative	(3,417)	(3,390)
Exploration and evaluation costs	(288)	(286)
Transaction costs	(957)	(949)
Gain on acquisition	6,426	6,605
Total Expenses	1,764	1,980
Income before other expenses	1,861	2,076
Gain / (loss) on risk management contracts	(23,876)	(23,687)
Other finance costs	(805)	(799)
Finance income	8	8
Foreign exchange gain	241	239
Net income / (loss) before tax	(22,571)	(22,163)
Income tax recovery (expense)	10,300	10,218
Net Loss	(12,271)	(11,945)
Unrealized foreign exchange gain (loss) on net investments	(6,140)	(5,811)
Exchange gain (loss) on re-translation of foreign operations	636	400
Comprehensive Loss for the Period	$ (17,775)	$ (17,356)

Net loss per share		
- basic	$ (0.04)	$ (0.03)
- diluted	$ (0.04)	$ (0.03)

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Roger Laing (2)(4)
Calgary, Alberta

Rod Maxwell (1)(3)
Calgary, Alberta

Jay Zammit (1)(2)(4)
Calgary, Alberta

Richard Ames(3)
Charleston, South Carolina

(1)Member of Audit Committee
(2)Member of Compensation Committee
(3)Member of Reserve Committee
(4)Member of the Governance Committee
(5)Member of the Health, Safety and Environment Committee

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Interim Chief Financial Officer

Alan Curran(5)
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Colin Tannock
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