Iona Energy Inc.
Condensed Consolidated Financial Statements - Unaudited
For the three and nine month periods ended September 30, 2014

Contents

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

(In thousands of US dollars)	Notes		September 30, 2014		December 31, 2013
ASSETS					
Current Assets					
Cash and cash equivalents		**$**	**28,029**	$	19,808
Accounts receivable			**18,733**		15,126
Prepaid expenses			**984**		551
Restricted cash	5		**61,736**		78,024
Inventory			**1,891**		1,802
Derivative instruments	13		**581**		293
Total Current Assets			**111,954**		115,604
Restricted cash	5		**6,953**		7,090
Exploration and evaluation assets	6		**135,689**		134,163
Property and equipment	7		**213,515**		274,164
Goodwill			**14,058**		14,058
Total Non-Current Assets			**370,215**		429,475
Total Assets		**$**	**482,169**	$	545,079
LIABILITITES AND SHAREHOLDERS' EQUITY					
Current Liabilities					
Accounts payable and accrued liabilities	5	**$**	**26,030**	$	19,662
Current derivative liabilities	13		**-**		16,867
Total Current Liabilities			**26,030**		36,529
Non-Current Liabilities					
Secured debt instrument	8		**266,124**		262,450
Decommissioning liabilities	9		**33,710**		17,763
Derivative liabilities	13		**22,975**		31,038
Deferred tax liability			**9,954**		5,111
Total Non-Current Liabilities			**332,763**		316,362
Total Liabilities			**358,793**		352,891
Shareholders' Equity					
Share capital			**178,730**		177,359
Contributed surplus			**11,217**		10,151
Accumulated other comprehensive loss			**(8,452)**		(8,055)
Retained earnings (deficit)			**(58,119)**		12,733
Total Shareholders' Equity			**123,376**		192,188
Total Liabilities and Shareholders' Equity		**$**	**482,169**	$	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 Income / (Loss) - Unaudited

(In thousands of US dollars, except for per share and share amounts)	Notes		Three Months Ended September 30 2014	Three Months Ended September 30 As restated (Note 16) 2013		Nine Months Ended September 30 2014	Nine Months Ended September 30 As restated (Note 16) 2013
Revenues	3	$	**22,403**	18,082	$	**85,151**	31,783
Operating costs			**(8,363)**	(3,431)		**(25,974)**	(9,836)
Depletion			**(14,271)**	(12,532)		**(49,869)**	(17,949)
Gross Profit			**(231)**	2,119		**9,308**	3,998
Expenses							
General and administrative			**(3,221)**	(2,133)		**(7,781)**	(8,614)
Exploration and evaluation costs	6		**(9)**	(5)		**(292)**	(779)
Impairment			**(27,777)**	-		**(27,777)**	-
Transaction costs			**(3,445)**	-		**(6,597)**	(953)
Gain on acquisition			**-**	-		**-**	6,327
Total Expenses			**(34,452)**	(2,138)		**(42,447)**	(4,019)
Loss before other expenses			**(34,683)**	(19)		**(33,139)**	(21)
Gain / (loss) on risk management contracts	13		**1,263**	(8,851)		**(7,211)**	(18,675)
Other finance costs			**(8,514)**	(10,371)		**(24,586)**	(14,170)
Finance income			**3**	18		**9**	30
Foreign exchange (loss) / gain			**(728)**	5,748		**(1,080)**	6,611
Net loss before tax			**(42,659)**	(13,475)		**(66,007)**	(26,225)
Income tax recovery (expense)			**172**	14,374		**(4,845)**	24,296
Net (Loss) / Income			**(42,487)**	899		**(70,852)**	(1,929)
Unrealized foreign exchange gain on net investments			**7,471**	6,575		**7,643**	5,799
Exchange loss on re-translation of foreign operations			**(7,467)**	(11,994)		**(8,040)**	(11,770)
Comprehensive Loss for the Period		$	**(42,483)**	(4,520)	$	**(71,249)**	(7,900)
Net loss per share							
- basic		$	**(0.12)**	**0.00**	$	**(0.19)**	**(0.01)**
- diluted		$	**(0.12)**	**0.00**	$	**(0.19)**	**(0.01)**
Weighted average shares outstanding							
- basic			**368,053,694**	366,824,344		**367,270,428**	358,688,767
- diluted			**368,053,694**	366,824,344		**367,270,428**	358,688,767

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

Iona Energy Inc.
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 (Deficit)		Total Equity
Balance December 31, 2013	$	177,359	10,151	(8,055)	12,733	$	192,188
Net loss for the period		-	-	-	(70,852)		(70,852)
Share based payments		-	1,066	-	-		1,066
Foreign currency translation		-	-	(8,040)	-		(8,040)
Unrealized foreign exchange on net investment		-	-	7,643	-		7,643
Issue of shares		1,371	-	-	-		1,371
Balance September 30, 2014	$	178,730	11,217	(8,452)	(58,119)	$	123,376,

(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		-	-	-	(1,929)	(1,929)
Share based payments		-	2,974	-	-	2,974
Foreign currency translation		-	-	(11,770)	-	(11,770)
Unrealized foreign exchange gain on net investments		-	-	5,799	-	5,799
Issue of shares (net of issue costs)		20,760	-	-	-	20,760
Balance September 30, 2013	$	177,359	9,182	(3,832)	(18,662)	164,047

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		Nine Months Ended September 30 2014		Nine Months Ended September 30 2013
Cash flows from / (used in) operating activities					
Net loss for the period		**$**	**(70,852)**	$	(1,929)
Items not involving cash:					
Depletion, depreciation and amortization			**49,990**		17,949
Unrealized FX gain / loss			**(419)**		-
Gain on acquisition			**-**		(6,605)
Unrealized (gain) / loss on fair value of derivative instruments	13		**(25,219)**		4,880
Amortization of loan costs			**-**		-
Income tax recovery / (expense)			**4,845**		(24,296)
Impairment			**27,777**		-
Share based payments			**1,066**		2,974
Finance costs			**23,968**		14,170
			11,156		7,143
Changes in non-cash working capital balances:					
Accounts receivable			**(1,152)**		(6,774)
Prepaid expenses			**(433)**		372
Inventory			**(89)**		(2,323)
Accounts payable and accrued liabilities			**18,110**		558
Cash flow used in operating activities			**27,592**		(1,024)
Cash flows from / (used in) financing activities					
Issue of common shares, net of issue costs			**916**		20,760
Put options – credit facility			**-**		(7,186)
Derivative call options, sold			**-**		60,000
Bank loan draw downs net of costs			**-**		134,300
Repayment of credit facility			**-**		(139,700)
Proceeds from issuance of bond, net of costs			**-**		260,082
Interest on credit facility			**-**		(3,726)
Bank fees and other interest charges			**(353)**		(5,735)
Interest on bond			**(26,125)**		-
Repayment of subsidiary loans and derivatives			**-**		(55,889)
Cash flow from financing activities			**(25,562)**		262,906
Cash flows from / (used in) investing activities					
Expenditures on property and equipment			**(4,238)**		(2,262)
Recovery of drilling expenditures			**-**		3,600
Expenditures on exploration and evaluation			**(6,025)**		(12,814)
Expenditure on acquisition of Orlando interest			**-**		(45,300)
Purchase of Huntington oil field			**-**		(137,572)
Disposal of exploration and evaluation assets			**-**		36,800
Restricted cash			**16,426**		(110,664)
Cash flow used in investing activities			**6,163**		(268,212)
Effect of exchange rate changes on cash			**28**		763
Increase / (decrease) in cash and cash equivalents		**$**	**8,221**	**$**	(5,567)
Cash and cash equivalents, beginning of period			**19,808**		15,579
Cash and cash equivalents, end of period			**28,029**		10,012

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 Limited	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 November 27, 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 functional and presentation currency

The Company changed the functional currency of Iona Energy Company (UK) Limited (“Iona UK”) from Pounds Sterling to US dollars with effect from October 1, 2013. This change was triggered by the achievement of plateau oil and gas production in the Huntington field and the issuance of $275 million of US denominated debt by Iona UK. Oil and gas prices received by the Company are benchmarked against the US Dollar Brent oil standard. The statement of financial position of Iona UK was translated to US dollars at the October 1, 2013 rate of 1.6204 GBP per 1 USD. Transactions impacting the statement of operations and comprehensive income were translated to US dollar using rates which approximate the rates at the date of transaction. The resulting gains and losses were recorded in the statement of comprehensive income.

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

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

2. Basis of Presentation - continued

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 rising on translation were shown as a foreign currency translation line item within the AOCI reserve equity. The resulting effect of the change in presentation currency for the three and nine months ended September 30, 2014 of ($4,999,000) and ($4,768,000) respectively on the comparative figures is reflected in the accumulated other comprehensive income at September 30, 2013.

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.

Future Accounting Pronouncements

- IFRS 9 Financial Instruments – since November, 2009, the IASB has been in the process of completing a three-phase project to replace IAS 39 Financial Instruments: Recognition and Measurement with IFRS 9, which includes requirements for hedge accounting, accounting for financial assets and liabilities, and impairment of financial instruments. The mandatory effective date of IFRS 9 has been set to January 1, 2018. The Company has not yet determined the impact of the amendments on the Company’s financial statements.

- IFRS 15 Revenue from Contracts with Customers: IFRS 15 specifies how and when to recognize revenue as well as requiring entities to provide users of financial statements with more informative, relevant disclosures. The standard supersedes IAS 18 Revenue, IAS 11 Construction Contracts, and a number of revenue-related interpretations. IFRS 15 will be effective for annual periods beginning on or after January 1, 2017. Application of the standard is mandatory and early adoption is permitted. The Company has not yet determined the impact of the amendments on the Company’s financial statements.

3. Revenue

		Three Months Ended September 30,			Nine Months Ended September 30,	
		2014	2013		**2014**	2013
Oil sales	$	**17,408**	14,280	$	**74,617**	23,003
Gas sales		**4,995**	3,802		**10,534**	8,780
	$	**22,403**	18,082	$	**85,151**	31,783

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4. 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.

	Nine Month Period Ended September 30, 2014			
	United Kingdom	**United States**	**Corporate**	**Total**
Revenue	85,151	-	-	**85,151**
Operating costs	(25,974)	-	-	**(25,974)**
Depletion	(49,869)	-	-	**(49,869)**
Gross Profit	9,308	-	-	**9,308**
Other expenses net finance costs	(72,059)	(32)	(3,224)	**(75,315)**
Taxation – expense	(4,845)	-	-	**(4,845)**
Net loss	(67,596)	(32)	(3,224)	**(70,852)**
	As at September 30, 2014			
Total assets	480,578	938	653	**482,169**
Total liabilities	358,253	4	536	**358,793**

	Three Month Period Ended September 30, 2014			
	United Kingdom	**United States**	**Corporate**	**Total**
Revenue	22,403	-	-	22,403
Operating costs	(8,363)	-	-	(8,363)
Depletion	(14,271)	-	-	(14,271)
Gross Profit / Loss	(231)	-	-	(231)
Other expenses, gain on acquisition, net finance costs	(40,908)	(4)	(1,516)	(42,428)
Taxation – recovery	172	-	-	172
Net loss	(40,967)	(4)	(1,516)	(42,487)

	Nine Month Period Ended September 30, 2013			
	United Kingdom	**United States**	**Corporate**	**Total**
Revenue	31,783	-	-	31,783
Operating costs, includes movement in inventory	(9,836)	-	-	(9,836)
Depletion	(17,949)	-	-	(17,949)
Gross Profit / Loss	3,998	-	-	3,998
Other expenses, gain on acquisition, net finance costs	(25,788)	- -	(4,435)	(30,223)
Taxation - recovery	24,296	-	-	24,296
Net Income (loss)	2,506	-	(4,435)	(1,929)
	As at September 30, 2013			
Total assets	608,615	937	3,385	612,937
Total liabilities	448,066	-	824	448,890

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

4. Segmented Information - continued

	Three Month Period Ended September 30, 2013			
	United Kingdom	United States	Corporate	Total
Revenue	18,082	-	-	18,082
Operating cost, includes movement in inventory	(3,431)	-	-	(3,431)
Depletion	(12,532)	-	-	(12,532)
Gross Profit / Loss	2,119	-	-	2,119
Net finance costs/other expenses	(13,775)	-	(1,819)	(15,594)
Taxation – recovery	14,374	-	-	14,374
Net Income (loss)	2,718	-	(1,819)	899

5. Restricted Cash

Current

As of September 30, 2014, the Company had a current asset of $61,736,000 (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 8). There are no restrictions with respect to the timing of the use of these funds for qualifying items, as such the restricted cash has been reflected as a classified as a current asset. Upon confirmation that both Orlando and Kells have reached first oil any remaining funds will become unrestricted.

Non-Current

At September 30, 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 September 30, 2014, the Company had $6,901,000 of restricted cash (December 31, 2013 - $7,038,000) held for the Company's decommissioning liabilities on the Trent & Tyne properties.

6. Exploration and Evaluation Assets

	Total E&E
As at December 31, 2013	134,163
Additions	1,526
As at September 30, 2014	**135,689**

General E&E

During the three and nine months ended September 30, 2014, the Company expensed $9,000 (2013 - $5,000) and $292,000 (2013 - $779,000), respectively 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.)

7. Property and Equipment

	Development & Production Oil and Gas Assets	Other Fixed Assets	Total
Cost			
At December 31, 2013	331,919	170	332,089
Additions	16,650	638	17,288
At September 30, 2014	**348,569**	**808**	**349,377**
Accumulated depletion, depreciation and amortization			
At December 31, 2013	34,768	74	34,842
Charge for the period	50,063	96	50,159
At September 30, 2014	**84,831**	**170**	**85,001**
Accumulated impairment as at December 31, 2013	23,580	**-**	23,580
Charge for the period as at September 30, 2014	27,777	-	27,777
	51,357	-	**51,357**
Exchange differences	**496**	-	**496**
Carrying amount at December 31, 2013	274,068	96	274,164
Carrying amount at September 30, 2014	**212,877**	**638**	**213,515**

On April 28, 2014, 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). This acquisition would have constitute a business combination. To date the company has expensed $6,597,000 of costs relating to the acquisition.

In the third quarter of 2014, the Company determined that the T&T producing assets would continue to generate negative cash flows for the remaining life of the field and as such has recognized an impairment charge of $27.8 million with respect to the T&T producing assets. The CGU was written down to the estimated recoverable amount based on fair value less cost of disposal. The estimated fair value was determined using future cash flows adjusted for risks specific to the asset and discounted using an before tax discount rate of 25%. The key assumptions in estimating the future cash flows for recoverable amounts are anticipated future commodity prices, expected production volumes and future operating and development costs. A 1% change in the discount rate would not significantly change the estimated recoverable amount.

The SPA had a number of conditions, which were required to be satisfied by October 28, 2014. These conditions could not be satisfied by October 28, 2014 and therefore the SPA has been terminated. The $2 million refundable deposit is now included in Accounts Receivable.

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

8. 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 in net proceeds. As at September 30, 2014 the fair value of the Bonds were $258.5 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:

Payment date	Nominal installment amount	Premium on nominal installment
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 certain of the restricted group's cash and cash equivalents and restricted cash balances) 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 December 31, 2016, and minimum 50% thereafter.

The restricted group is defined as Iona Energy Company (UK) plc and Iona UK Huntington Limited.

Under the Bond Agreement an event of default constitutes two consecutive quarterly covenant violations. The quarter ended December 31, 2013 was 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 September 30, 2014, the Company was in compliance with the required Bond covenants.

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

8. Senior Debt Instruments - continued

The table below delineates the Company's position with respect to the Bond covenants at September 30, 2014.

	30-September-14	Covenant
Liquidity as defined	$89,284	Greater than $30,000
Restricted Group Capital Employed Ratio	48%	Greater than 40%
Group Capital Employed Ratio	48%	Greater than 40%
Leverage Ratio	2.27	Not greater than 3.0x

The Bonds are secured against the assets of the Company and its subsidiaries Iona Energy Company (UK) plc and Iona UK Huntington Limited.

The effective interest rate on the bond at September 30, 2014 was 12.16%.

Balance, December 31, 2013		262,450
Amortization of discount and transaction costs		3,674
As at September 30, 2014	$	266,124

9. Decommissioning Liabilities

Balance December 31, 2013		17,763
Change in estimate		14,568
Discount rate		833
Accretion		546
Balance September 30, 2014	**$**	**33,710**

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 1.87% to 4.15% 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 majority of the change in estimate during the period was due to a revision in the expected cost of the Huntington decommissioning asset. These cost revisions resulted from an independent decommissioning report completed by the operator of the Company for DECC in June 2014. 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.)

10. 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 September 30, 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	**3,750,000**	**1,371**
Share issue costs	**-**	**-**
Ending Balance, September 30, 2014	**370,580,868**	**$ 178,730**

Warrants	Warrants
Opening balance, December 30, 2014	**-**
Issued	**3,750**
Ending Balance, September 30, 2014	**3,750**

On August 29, 2014, the Company completed a non-brokered private placement for $1,371,000 (CAD$1,500,000) with the Company's Executive Chairman and President & CEO. Pursuant to the terms of the non-brokered private placement financing the Company issued 3,750,000 units ("Units") at a price of CAD$0.40 per Unit. Each Unit shall be comprised of one common share and one warrant ("Warrants") to purchase common shares of the Company. The Warrants shall have a term of five years and will have an exercise price of CAD$0.48 in the first year following closing, and an exercise price of CAD$0.58, CAD$0.69, CAD$0.83 and CAD$1.00 in each year thereafter.

Stock Options

Date of Grant	Number Issued	Forfeited Options	Exercise Price CAD$	Weighted Average Remaining Contractual Life	Date of Expiry	Number Exercisable September 30, 2014
May 31, 2011	9,550,000	(1,950,000)	$0.60	0.92 years	May 31, 2015	7,600,000
November 25, 2011	100,000	(100,000)	$0.60	-	-	-
April 13, 2012	17,070,000	(5,305,000)	$0.57	2.79 years	April 12, 2017	8,362,500
June 17, 2012	210,000	(210,000)	$0.47	-	-	-
August 29, 2012	150,000	(150,000)	$0.38	-	-	-
January 10, 2013	175,000	-	$0.59	3.53 years	January 10, 2018	175,000
March 5, 2013	7,420,000	(3,225,000)	$0.63	3.68 years	March 5, 2018	2,405,000
July 29, 2013	700,000	(700,000)	$0.59	4.08 years	July 29, 2018	-
October 3, 2013	2,500,000	(2,500,000)	$0.63	-	-	-
October 23, 2013	600,000	-	$0.63	4.32 years	October 23, 2018	150,000
May 1, 2014	1,350,000	(262,500)	$0.54	-	-	337,500
July 1, 2014	750,000	-	$0.49	-	-	187,500
September 1, 2014	4,500,000	-	$0.40	4.84 years	May 1, 2019	1,125,000
	45,075,000	**(14,402,500)**				**20,342,500**

On May 1, 2014, Iona Energy issued 1,350,000 stock options to purchase 1,350,000 common shares of the Company to employees of the Company. The options were issued with an exercise price of $0.54 per share, vest as to one quarter immediately and one quarter on each of the first, second and third anniversaries of the date of grant and have a five year term from the date of issuance.

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

10. Share Capital - continued

On July 1, 2014 and September 1, 2014 Iona Energy issued 750,000 and 4,500,000 stock options respectively to purchase 5,250,000 common shares of the Company to employees of the Company. The options were issued with an exercise price of $0.49 and $0.40 per share respectively, vest as to one quarter immediately and one quarter on each of the first, second and third anniversaries of the date of grant and have a five year and four year term, respectively, from the date of issuance.

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:

	September 30, 2014
Average expected volatility	51% - 75%
Risk-free rate	1.47% - 3.50%
Expected life	5 years
Fair Value per Option	CAD$0.15 - $0.40

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

11. Related Party Transactions

During the three and nine months ended September 30, 2014, the Company was charged $288,000 (2013 - $239,000) and $390,000 (2013 - $640,000) respectively, in legal fees of which $NIL (2013 - $95,000) related to share issuance costs by a law firm where a director of the Company is a partner, of which $26,000 is included in accounts payable and accrued liabilities as at September 30, 2014 and $29,000 as at December 31, 2013.

Included in accounts receivable is $117,483 (2013 - $114,000) 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 September 30, 2014. The amounts owing are non-interest bearing and secured. The Company expects full repayment of the remaining balances in 2015.

On September 12, 2014 the Company provided loans to two members of senior management via Demand Promissory Notes for a total amount of $480,000 (CAD$500,000) bearing interest at 3.25% with two members of senior management. These notes are secured by 1,250,000 outstanding common shares and 1,250,000 warrants issued on August 29, 2014. At September 30, 2014 these promissory notes remained outstanding and are included in Accounts Receivable. The Company expects full repayment of the Demand Promissory Notes in the future.

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.

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

12. Commitments and Contingencies

In addition to commitments recorded on the balance sheet, based on management's best estimate, the Company has the following contractual obligations:

	September 30, 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	**4,822**	495	1,485	1,485	1,357
Equipment leases	**41,309**	11,408	21,930	7,971	-
Drilling, completion, facility construction	**21,339**	21,339	-	-	-
Total UK Segment	**67,470**	33,242	23,415	9,456	1,357
Total Contractual Obligations	**67,674**	33,259	23,466	9,507	1,442

Excluded from the table above on January 19, 2012, the Company's UK Subsidiary, Iona UK, acquired full ownership and operatorship from Fairfield Cedrus Limited ("Fairfield") of a 100% interest in Block 3/8d containing the Kells Oil Field. Iona UK reimbursed Fairfield on closing for $8.5 million in pre-development expenditures related to the Kells field. In addition, upon the approval by DECC of a field development plan in respect of Kells, Iona will be obligated to make a cash payment of $5.0 million to Fairfield and pay a net royalty of $2.50 per barrel of production from the Kells Oil Field.

Additionally, future staged payments will be made by Iona to Sorgenia and MPX commencing six months after first production from Orlando. The first payment will be $7.0 million with additional payments of $7.0 million, $7.0 million, $4.0 million, and $4.0 million made every six months thereafter respectively, amounting to a total payment of $29.0 million over 3 years.

13. 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, 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.

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

13. Financial Instruments and Risk Management Contracts - continued

• 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 instruments 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 30 September 2014:

	Level 1	Level 2	Level 3	Total Fair Value
Current assets				
Derivative financial assets	-	581	-	581
Current liabilities				
Derivative financial instruments	-	-	-	-
Non-current liabilities				
Derivative financial instrument liabilities	-	22,975	-	22,975

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

	Three Months Ended September 30		Nine Months Ended September 30	
	2014	2013	**2014**	2013
Cost of derivative options	**-**	-	**-**	(7,239)
Realized gain / (loss) on commodity hedges	**(26,500)**	(6,538)	**(32,430)**	(6,556)
Unrealized gain / (loss) on commodity hedges	**27,763**	(2,313)	**25,219**	(4,880)
Total gain / (loss) on commodity hedges	**1,263**	(8,851)	**(7,211)**	(18,675)

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.)

13. 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.

On August 15, 2014, Iona UK settled the remaining 3,658,051 calls (effective April 2014 through March 2018) for two equal payments of $13,250,000, due on August 18, 2014, paid, and February 10, 2015, included in Accounts Payable. Simultaneously, Iona UK purchased 458,352 puts (effective August 2014 through July 2015) at a strike price of $90.00 per barrel, and sold 1,650,000 calls (effective October 2018 through March 2020) at a strike price of $90.00 per barrel. The payment of the settlement costs will be substantially funded from restricted cash. Under the Bond agreement, restricted cash drawn to settle the BP derivatives has to be re-transferred into restricted cash from Huntington cash flows.

The table below shows Iona's net position on a quarterly basis of the outstanding call and put option structures sold to and bought from BTL on February 21, 2013 and September 30, 2013 and August 15, 2014 respectively.

		Call Options (bbls)				Put Options (bbls)	
		Sold	Bought	Net Position	Strike ($/bbl)	Bought	Strike ($/bbl)
2014	Q4	496,901	496,901	-	95	133,684	90
2015	Q1	274,396	274,396	-	95	105,770	90
	Q2	334,045	334,045	-	95	91,526	90
	Q3	377,830	377,830	-	95	30,996	-
	Q4	394,678	394,678	-	95	-	-
2016	Q1	390,723	390,723	-	95	-	-
	Q2	401,251	401,251	-	95	-	-
	Q3	418,356	418,356	-	95	-	-
2018	Q3	274,298	-	274,298	90	-	90
	Q4	274,298	-	274,298	90	-	90
2019	Q1	274,298	-	274,298	90	-	90
	Q2	274,298	-	274,298	90	-	90
	Q3	274,298	-	274,298	90	-	90
2020	Q4	274,298	-	274,298	90	-	90
	Q1	274,298	-	274,298	90	-	90
Total		5,008,266	3,088,180	1,920,086		361,976	

13. 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. The Company does not have any floating rate debt.

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 September 30, 2014, and did not provide for any doubtful accounts nor was it required to write-off any receivables during the period ended September 30, 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 September 30, 2014, September 30, 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 September 30, 2014 would have impacted the net loss and comprehensive loss of the Company for the nine month period ended September 30, 2014 by approximately $46,000 (nine months ended September 30, 2013 – $353,000).

In addition at September 30, 2014, the Company held approximately $7,347,000 (£4,532,000) (2013- $53,014,000 (£32,769,000)) 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 September 30, 2014 would impact the net loss and comprehensive loss of the Company for the nine month period ended September 30, 2014 by approximately $73,000 (nine months ended September 30, 2013 - $530,000).

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

13. Financial Instruments and Risk Management Contracts - continued

risks may necessitate the Company to issue equity, obtain debt financing, or sell assets. The Company's contractual obligations are included in Note 12 and further details of liquidity are discussed in Note 14.

14. 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 September 30, 2014, the Company has net assets of $123.4 million, working capital of $85.9 million and commitments due in the next 12 months as further detailed in Note 12. The Company intends to finance its obligations as they come due from current working capital supplemented by future cash flow generated from operations.

15. Subsequent Events

On April 28, 2014, the Company signed a Sale and Purchase Agreement with Perenco UK Limited, to purchase Perenco's remaining 80% working interest in the Trent & Tyne fields. That SPA had a number of conditions, which were required to be satisfied by October 28, 2014. These conditions could not be satisfied by the 28 of October 2014 and therefore the SPA has been terminated under a clause which the Company is entitled to repayment of the $2 million deposit which is included in Accounts Receivable.

On October 27, 2014, the Company, through its wholly owned UK subsidiary, Iona UK, closed out 361,976 outstanding put options (effective October 2014 – July 2015) realizing proceeds of $1.9 million. Simultaneously, the Company put in place "costless collar" arrangements over 396,197 barrels (effective December 2014 – December 2015) with a floor price of US$80.00 per barrel and a ceiling price of US$92.75 per barrel.

16. 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 and nine month periods ended September 30, 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 Q3 2013 exchange rate of 0.9629 USD: CAD and the nine month average exchange rate of 0.9773. The effect of the translation is as follows:

For the three month period ended September 30, 2013		**As previously reported CAD $000**		**As restated $000**
Revenues	$	18,786	$	18,082
Operating costs		(3,563)		(3,431)
Depletion		(13,015)		(12,532)
Gross Profit		2,208		2,119
Expenses				
General and administrative		(2,217)		(2,133)
Exploration and evaluation costs		(5)		(5)
Transaction costs		(6)		-
Gain on acquisition		-		-
Total Expenses		(2,228)		(2,138)
Loss before other expenses		(20)		(19)
Gain / (loss) on risk management contracts		(9,192)		(8,851)
Other finance costs		(4,373)		(10,371)[1]
Finance income		19		18
Foreign exchange gain / (loss)		(428)		5,748[1]
Net income / (loss) before tax		(13,994)		(13,475)
Income tax recovery / (expense)		14,928		14,374
Net Loss		934		899
Unrealized foreign exchange gain / (loss) on net investments		6,828		6,575
Exchange gain / (loss) on re-translation of foreign operations		(5,353)		(11,994)
Comprehensive Loss for the Period	$	2,409	$	(4,520)
Net loss per share				
- basic	$	0.00	$	0.00
- diluted	$	0.00	$	0.00

[1]Certain amounts have been restated based on the 2013 audited financial statements. The restatement resulted from the Company including $6,160,000 finance costs as foreign exchange differences in error in the previously reported financial statements.

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

16. Adjustment of Previously Reported Financial Information Due to Change in Presentation Currency - continued

For the nine month period ended September 30, 2013	As previously reported CAD $000	As restated $000
Revenues	$ 32,701	$ 31,783
Operating costs	(10,069)	(9,836)
Depletion	(18,517)	(17,949)
Gross Profit	4,115	3,998
Expenses		
General and administrative	(8,799)	(8,614)
Exploration and evaluation costs	(791)	(779)
Transaction costs	(968)	(953)
Gain on acquisition	6,426	6,327
Total Expenses	(4,132)	(4,019)
Loss before other expenses	(17)	(21)
Gain / (loss) on risk management contracts	(19,170)	(18,675)
Other finance costs	(8,232)	(14,170)[1]
Finance income	30	30
Foreign exchange gain	448	6,611[1]
Net income / (loss) before tax	(26,941)	(26,225)
Income tax recovery / (expense)	25,003	24,296
Net Loss	(1,938)	(1,929)
Unrealized foreign exchange gain / (loss) on net investments	6,040	5,799
Exchange gain / (loss) on re-translation of foreign operations	(5,125)	(11,770)
Comprehensive Loss for the Period	$ (1,023)	$ (7,900)

Net loss per share		
- basic	$ (0.01)	$ (0.01)
- diluted	$ (0.01)	$ (0.01)

[1]Certain amounts have been restated based on the 2013 audited financial statements. The restatement resulted from the Company including $6,160,000 finance costs as foreign exchange differences in error in the previously reported financial statements.

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

16. Adjustment of Previously Reported Financial Information Due to Change in Presentation Currency - continued

For the nine month period ended September 30, 2013		As previously reported CAD $000	As translated USD $000	Reclassification[1] USD $000	As Adjusted USD $000
Cash flow used in operating activities	$	(6,089)	(6,088)	5,064	(1,024)
Cash flow from financing activities		280,733	272,785	(9,879)	262,906
Cash flows from / (used in) investing activities		(280,627)	(273,027)	4,815	(268,212)
Effect of exchange rate changes on cash		780	763	-	763
Increase / (decrease) in cash and cash equivalents		(5,203)	(5,567)	-	(5,567)
Cash and cash equivalents, beginning of period		15,500	-	-	15,579
Cash and cash equivalents, end of period	$	10,297	-	-	10,012

[1]Certain amounts have been restated based on the 2013 audited financial statements. These restatements primarily result from the Company including costs, expenses and working capital items in cash inflows and outflows from financing activities and investing activities versus operating activities as previously reported.

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CORPORATE INFORMATION

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Roger Laing (2)(4)
Calgary, Alberta

Rod Maxwell (1)(3)
Calgary, Alberta

Jay Zammit (1)(4)
Calgary, Alberta

Richard Ames(2)(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

OFFICERS

Iain McKendrick (3)(5)
Executive Chairman

Tom Reynolds
President and Chief Executive Officer

Robert Gair
Chief Financial Officer

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