



## **Management's Discussion and Analysis**

For the three months and years ended

December 31, 2013 and 2012

## MANAGEMENT'S DISCUSSION AND ANALYSIS

This Management's Discussion and Analysis ("the MD&A") is dated March 5, 2014. It should be read in conjunction with TORC Oil & Gas Ltd.'s ("TORC" or the "Company") audited financial statements as at and for the years ended December 31, 2013 and December 31, 2012. The reader should be aware that historical results are not necessarily indicative of future performance.

The financial data presented below has been prepared in accordance with International Financial Reporting Standards ("IFRS"), unless otherwise indicated.

### Barrel of Oil Equivalent

Where amounts are expressed on a barrel of oil equivalent ("Boe") basis, natural gas volumes have been converted to Boe using a ratio of 6,000 cubic feet of natural gas to one barrel of oil equivalent. This conversion ratio is based upon an energy equivalent conversion method primarily applicable at the burner tip and does not represent value equivalence at the wellhead. Boe figures may be misleading, particularly if used in isolation.

### Non-IFRS Measurements

The MD&A contains the terms "funds flow from operations, including transaction related costs/recovery", "funds flow from operations, excluding transaction related costs/recovery", "net debt" and "operating netback" which are not defined by IFRS and therefore may not be comparable to performance measures presented by others. Funds flow from operations, including transaction related costs/recovery represents cash flow from operating activities prior to changes in non-cash working capital and settlement of decommissioning obligations. Funds flow from operations, excluding transaction related costs/recovery represents cash flow from operating activities prior to changes in non-cash working capital, settlement of decommissioning obligations and transaction related costs/recovery. Working capital (net debt) is calculated as current assets (excluding financial derivative assets) less current liabilities (excluding financial derivative liabilities), bank debt and non-current deferred lease incentives. Operating netback represents revenue and realized gain or loss on financial derivatives, less royalties, operating expenses and transportation expenses and has been presented on a per Boe basis. Management believes that in addition to net income, the aforementioned non-IFRS measurements are useful supplemental measures as they assist in the determination of the Company's operating performance, leverage and liquidity. Investors should be cautioned, however, that these measures should not be construed as an alternative to both net income and net cash from operating activities, which are determined in accordance with IFRS, as indicators of the Company's performance.

The reconciliation between funds flow from operations, as defined above, and net cash from operating activities, as defined by IFRS, is as follows:

<i>(\$ thousands)</i>	<b>Three months ended Dec 31, 2013</b>	Three months ended Dec 31, 2012	<b>Year ended Dec 31, 2013</b>	Year ended Dec 31, 2012
Net cash from operating activities (defined by IFRS)	\$ 46,912	\$ 3,076	\$ 78,785	\$ 8,514
Settlement of decommissioning obligations	-	-	262	98
Changes in non-cash working capital	<b>(5,454)</b>	1,165	<b>10,489</b>	4,783
Funds flow from operations, including transaction related costs/recovery	\$ 41,458	\$ 4,241	\$ 89,536	\$ 13,395
Transaction related costs (recovery)	<b>(689)</b>	3,798	<b>6,976</b>	3,798
Funds flow from operations, excluding transaction related costs/recovery	\$ 40,769	\$ 8,039	\$ 96,512	\$ 17,193

The reconciliation of net debt, as defined above, is as follows:

<i>(\$ thousands)</i>	<b>Year ended Dec 31, 2013</b>	Year ended Dec 31, 2012
Current assets (excluding financial derivative assets)	\$ 50,068	\$ 101,180
Less: current liabilities (excluding financial derivative liabilities)	<b>(109,971)</b>	(65,647)
Less: bank debt	<b>(85,000)</b>	-
Less: non-current deferred lease incentives	<b>(280)</b>	(456)
Working capital (net debt)	\$ <b>(145,183)</b>	\$ 35,077

The reconciliation for operating netback is found within this MD&A.

TORC's reporting and measurement currency is the Canadian dollar. Amounts in this MD&A are in Canadian dollars unless otherwise stated.

## MANAGEMENT'S DISCUSSION AND ANALYSIS

### Forward-Looking Statements

*This MD&A contains forward-looking statements. More specifically, it contains forward-looking statements respecting: (i) the annual dividend, (ii) TORC's expectation that general and administrative expenses on a Boe basis will decrease, (iii) TORC's expectation that it will continue to realize natural gas prices greater than AECO benchmarks, (iv) the anticipated sources of funding for the Company's capital program, (v) the sufficiency of liquidity and capital resources to fund the Company's capital program and ongoing operations, (vi) the Company's risk management activities and the benefits to be obtained therefrom, and (vii) the estimates regarding the Company's future farm-in commitments.*

*The forward-looking statements contained in this MD&A are based on certain key expectations and assumptions made by TORC, including expectations and assumptions concerning the impact of increasing competition, the general stability of the economic and political environment in which TORC operates, the ability of the Company to obtain qualified staff, equipment and services in a timely and cost efficient manner, drilling results, the ability of the operator of the projects which the Company has an interest in to operate the field in a safe, efficient and effective manner, TORC's ability to obtain financing on acceptable terms, changes in the Company's banking facility, field production rates and decline rates, the ability to reduce operating costs, the ability to replace and expand oil and natural gas reserves through acquisition, development or exploration, the timing and costs of pipeline, storage and facility construction and expansion, the ability of the Company to secure adequate product transportation, future petroleum and natural gas prices, currency, exchange and interest rates, the regulatory framework regarding royalties, taxes and environmental matters in the jurisdictions in which the Company operates, and TORC's ability to successfully market its petroleum and natural gas products. Readers are cautioned that the foregoing list of factors is not exhaustive.*

*Although TORC believes that the expectations and assumptions on which the forward-looking statements are based are reasonable, undue reliance should not be placed on the forward-looking statements because TORC can give no assurance that they will prove to be correct. Since forward-looking statements address future events and conditions, by their very nature they involve inherent risks and uncertainties. Actual results could differ materially from those currently anticipated due to a number of factors and risks, including, without limitation, factors and risks associated with oil and gas exploration, development, exploitation, production, marketing and transportation, loss of markets, volatility of commodity prices, currency fluctuations, imprecision of reserve estimates, environmental risks, competition from other producers, inability to retain drilling rigs and other services, incorrect assessment of the value of acquisitions, failure to realize the anticipated benefits of acquisitions, the inability to fully realize the benefits of acquisitions, delays resulting from or inability to obtain required regulatory approvals and inability to access sufficient capital from internal and external sources. Additional information on these and other factors and risks that could affect the Company's operations and financial results are included in reports on file with Canadian securities regulatory authorities and may be accessed through the SEDAR website ([www.sedar.com](http://www.sedar.com)) or at the Company's website ([www.torcoil.com](http://www.torcoil.com)). Furthermore, the forward looking statements contained in this document are made as at the date of this document and the Company does not undertake any obligation to update publicly or to revise any of the included forward looking statements, whether as a result of new information, future events or otherwise, except as may be required by applicable securities laws.*

## MANAGEMENT'S DISCUSSION AND ANALYSIS

### Significant Events

#### Asset acquisition, financing, credit facility, dividends and share consolidation

On September 9, 2013, the Company completed a \$510 million acquisition of light oil producing assets in southeast Saskatchewan (the "SE Saskatchewan Acquisition"), resulting in the strategic transition of the Company's business model to an intermediate dividend plus growth company. Net of purchase price adjustments, the acquisition price was approximately \$494 million.

In conjunction with the SE Saskatchewan Acquisition, TORC secured an equity investment by the Canada Pension Plan Investment Board ("CPPIB") for \$170.0 million through a private placement of subscription receipts and also raised \$241.6 million through a syndicated bought deal prospectus offering of subscription receipts, for total gross proceeds of \$411.6 million (the "Financings"). In total, the Financings resulted in the issuance of 52,434,000 common shares at \$7.85 per common share (the number of common shares and price per common share indicated here reflect amounts after the Share Consolidation detailed below).

After the Financings, CPPIB owned approximately 24 percent of the outstanding common shares of TORC and is entitled to two board of directors nominees as long as it owns 20 percent or greater of the outstanding common shares of TORC. CPPIB has initially nominated one director, who joined the board of directors in the fourth quarter of 2013.

Also, concurrent with the closing of the SE Saskatchewan Acquisition, the Company's syndicated credit facility was increased to \$350 million. The structure and terms of the increased credit facility is similar to the Company's credit facility prior to the increase.

In September 2013, the Company's shareholders approved TORC's plan to transition its business model to an intermediate dividend plus growth company. Pursuant to this transition, TORC announced a plan to pay an annual dividend of \$0.50 per common share. The Company's dividend plan enables common shareholders to elect to receive dividends in common shares rather than cash, calculated at 95% of the weighted average trading price for the five days immediately prior to the payment date (the "Share Dividend Program"). TORC declared its first monthly dividend of \$0.0417 per common share, paid on October 15, 2013 to common shareholders of record on September 30, 2013. On December 10, 2013, TORC announced an increase to its monthly dividend to \$0.045 per common share, payable on January 15, 2014 to shareholders of record at December 31, 2013.

In September 2013, the Company consolidated its outstanding common shares, stock options, incentive shares and warrants on a 1 for 5 basis (the "Share Consolidation"). As a result, the number of outstanding common shares, stock options, incentive shares and warrants of comparative periods have been reduced by a factor of five, in order for the comparative common share, stock options, incentive shares, warrants, per share and per diluted share amounts to be equivalent.

### Results of Operations

#### Production

	Three months ended Dec 31, 2013	Three months ended Dec 31, 2012	Year ended Dec 31, 2013	Year ended Dec 31, 2012
Crude oil and NGL (Bbl per day) <sup>(1) (2)</sup>	8,841	2,047	5,004	1,114
Natural gas (Mcf per day) <sup>(3)</sup>	7,951	2,824	6,702	1,027
Total (Boe per day)	10,166	2,518	6,121	1,285
% liquids	87%	81%	82%	87%

<sup>(1)</sup> "NGL" refers to natural gas liquids.

<sup>(2)</sup> "Bbl" refers to barrels.

<sup>(3)</sup> "Mcf" refers to thousand cubic feet.

Production in the three months and year ended December 31, 2013 increased compared to the three months and year ended December 31, 2012 (the "Corresponding Periods"). In addition to the Company's on-going drilling success, the increase includes production from the acquisition of Vero Energy Inc. ("Vero") which closed on November 19, 2012 as well as production from the SE Saskatchewan Acquisition which closed on September 9, 2013.

## MANAGEMENT'S DISCUSSION AND ANALYSIS

### Pricing

	Three months ended Dec 31, 2013	Three months ended Dec 31, 2012	Year ended Dec 31, 2013	Year ended Dec 31, 2012
<b>Average realized prices:</b>				
Crude oil (\$ per Bbl)	\$ 81.73	\$ 73.83	\$ 87.11	\$ 78.38
NGL (\$ per Bbl)	54.50	54.57	53.92	54.07
Natural gas (\$ per Mcf)	3.61	3.15	3.31	2.78
Boe (\$ per Boe)	\$ 72.93	\$ 62.89	\$ 73.43	\$ 69.53

During the three months and year ended December 31, 2013, TORC realized oil prices of \$81.73 and \$87.11, respectively. TORC's discount to WTI converted to Canadian dollars approximated \$21 per Bbl and \$14 per Bbl, respectively (Corresponding Periods: \$14 per Bbl and \$14 per Bbl, respectively). In the three months and year ended December 31, 2013, TORC's discount to Edmonton Par averaged approximately \$5 per Bbl and \$6 per Bbl, respectively (Corresponding Periods: \$11 per Bbl and \$8 per Bbl, respectively). The pricing differentials are a function of North American refinery supply/demand fundamentals as well as crude quality.

In the three months and year ended December 31, 2013, the Company realized gas prices of \$3.61 per Mcf and \$3.31 per Mcf, respectively (Corresponding Periods: realized \$3.15 per Mcf and \$2.78 per Mcf, respectively). In the three months and year ended December 31, 2013, the Company's realized gas prices were 13% and 16% above AECO benchmarks, respectively (Corresponding Periods: 9% and 29% above AECO benchmarks, respectively). TORC expects to continue to realize natural gas prices greater than AECO benchmarks due to the higher heat content of its natural gas.

In the three months and year ended December 31, 2013, the average realized price across all products was \$72.93 per Boe and \$73.43 per Boe, respectively. For the three months and year ended December 31, 2013, the average realized price was higher by \$10.04 per Boe and \$3.90 per Boe, respectively, compared to the Corresponding Periods owing largely to a higher crude oil price environments slightly offset by a lower percentage of crude oil production in 2013 relative to 2012.

	Three months ended Dec 31, 2013	Three months ended Dec 31, 2012	Year ended Dec 31, 2013	Year ended Dec 31, 2012
<b>Average Benchmark Prices:</b>				
Crude oil – WTI ( <i>US\$ per Bbl</i> )	97.44	88.18	97.96	94.20
Crude oil – Edmonton Par ( <i>CDN\$ per Bbl</i> )	86.75	84.47	93.40	86.59
Natural gas – AECO Daily Spot ( <i>\$ per Mcf</i> )	3.18	2.90	2.86	2.16
Natural gas – AECO Monthly Spot ( <i>\$ per Mcf</i> )	2.84	2.75	2.85	2.16
Exchange rate – ( <i>CDN\$/US\$</i> )	1.05	0.99	1.03	1.00

### Revenues

	Three months ended Dec 31, 2013	Three months ended Dec 31, 2012	Year ended Dec 31, 2013	Year ended Dec 31, 2012
<i>(\$ thousands)</i>				
Crude oil and NGL	\$ 65,564	\$ 13,735	\$ 155,969	\$ 31,634
Natural gas	2,642	832	8,105	1,077
	\$ 68,206	\$ 14,567	\$ 164,074	\$ 32,711

Revenues in the three months and year ended December 31, 2013 increased compared to the Corresponding Periods due to the Company's on-going drilling success, increased price environments, and the addition of production from acquisitions including the SE Saskatchewan Acquisition which closed on September 9, 2013.

## MANAGEMENT'S DISCUSSION AND ANALYSIS

### Royalties

<i>(\$ thousands, unless otherwise noted)</i>	<b>Three months ended Dec 31, 2013</b>	Three months ended Dec 31, 2012	<b>Year ended Dec 31, 2013</b>	Year ended Dec 31, 2012
Royalties	\$ 10,730	\$ 1,586	\$ 24,353	\$ 3,323
\$ per Boe	\$ 11.47	\$ 6.84	\$ 10.90	\$ 7.06
Percentage of revenue	15.7%	10.9%	14.8%	10.2%

Compared to the Corresponding Periods, the Company's corporate royalty rate increased in the three months and year ended December 31, 2013. The increase in royalties is primarily due to higher royalty rates related to the assets from the SE Saskatchewan Acquisition (which includes the Saskatchewan Resource Tax), Crown royalty incentives that expired for certain wells, and certain wells that were drilled which did not qualify for the Crown royalty incentives.

### Operating Expenses

<i>(\$ thousands, unless otherwise noted)</i>	<b>Three months ended Dec 31, 2013</b>	Three months ended Dec 31, 2012	<b>Year ended Dec 31, 2013</b>	Year ended Dec 31, 2012
Operating expenses	\$ 12,386	\$ 2,796	\$ 26,431	\$ 6,033
\$ per Boe	\$ 13.24	\$ 12.07	\$ 11.83	\$ 12.83

For the three months ended December 31, 2013, the increase on a per Boe basis compared to the Corresponding Period, largely reflects increased costs associated with the properties acquired in the SE Saskatchewan Acquisition.

For the year ended December 31, 2013, the decrease on a per Boe basis compared to the Corresponding Period, largely reflects the benefits associated with further development of infrastructure in the Company's core areas. As the SE Saskatchewan Acquisition closed on September 9, 2013, costs for the three months ended December 31, 2013 more accurately reflect go-forward costs on a Boe basis.

### Transportation Expenses

<i>(\$ thousands, unless otherwise noted)</i>	<b>Three months ended Dec 31, 2013</b>	Three months ended Dec 31, 2012	<b>Year ended Dec 31, 2013</b>	Year ended Dec 31, 2012
Transportation expenses	\$ 2,154	\$ 1,436	\$ 8,156	\$ 3,174
\$ per Boe	\$ 2.30	\$ 6.20	\$ 3.65	\$ 6.75

For the three months and year ended December 31, 2013, the Company's transportation expenses decreased significantly on a per Boe basis, compared to the Corresponding Periods, and largely reflects the benefits associated with further development of infrastructure, economies of scale associated with greater volumes, and lower transportation costs associated with the assets acquired in the SE Saskatchewan Acquisition which closed on September 9, 2013.

## MANAGEMENT'S DISCUSSION AND ANALYSIS

### Operating Netbacks

<i>(\$ per Boe, unless otherwise noted)</i>	<b>Three months ended Dec 31, 2013</b>	Three months ended Dec 31, 2012	<b>Year ended Dec 31, 2013</b>	Year ended Dec 31, 2012
Average daily production (Boepd)	<b>10,166</b>	2,518	<b>6,121</b>	1,285
Crude oil (\$ per Bbl)	<b>\$ 81.73</b>	\$ 73.83	<b>\$ 87.11</b>	\$ 78.38
NGL (\$ per Bbl)	<b>\$ 54.50</b>	\$ 54.57	<b>\$ 53.92</b>	\$ 54.07
Natural gas (\$ per Mcf)	<b>\$ 3.61</b>	\$ 3.15	<b>\$ 3.31</b>	\$ 2.78
Average price prior to hedging	<b>\$ 72.93</b>	\$ 62.89	<b>\$ 73.43</b>	\$ 69.53
Realized gain (loss) on financial derivatives (hedging)	<b>\$ 1.08</b>	\$ 1.24	<b>\$ (0.07)</b>	\$ 0.61
Royalties	<b>(11.47)</b>	(6.84)	<b>(10.90)</b>	(7.06)
Operating	<b>(13.24)</b>	(12.07)	<b>(11.83)</b>	(12.83)
Transportation	<b>(2.30)</b>	(6.20)	<b>(3.65)</b>	(6.75)
Operating netback	<b>\$ 47.00</b>	\$ 39.02	<b>\$ 46.98</b>	\$ 43.50
Operating netback (prior to hedging)	<b>\$ 45.92</b>	\$ 37.78	<b>\$ 47.05</b>	\$ 42.89

### General and Administrative Expenses

During the three months and year ended December 31, 2013, the Company incurred the following general and administrative expenses ("G&A"):

<i>(\$ thousands)</i>	<b>Three months ended Dec 31, 2013</b>	Three months ended Dec 31, 2012	<b>Year ended Dec 31, 2013</b>	Year ended Dec 31, 2012
Gross general and administrative expenses	<b>\$ 4,114</b>	\$ 2,067	<b>\$ 13,148</b>	\$ 7,571
Recoveries <sup>(1)</sup>	<b>(578)</b>	(345)	<b>(2,086)</b>	(1,516)
Capitalized general and administrative expenses <sup>(2)</sup>	<b>(1,336)</b>	(714)	<b>(3,990)</b>	(2,441)
Total general and administrative \$ per Boe	<b>\$ 2,200</b> <b>\$ 2.35</b>	\$ 1,008 \$ 4.35	<b>\$ 7,072</b> <b>\$ 3.17</b>	\$ 3,614 \$ 7.68

<sup>(1)</sup> Recoveries refers to those G&A expenditures which under industry practice are reclassified to operating expenses, exploration and evaluation assets, or property, plant and equipment, dependent on their nature.

<sup>(2)</sup> Capitalized general and administrative expenses are those G&A expenditures which are directly attributable to the acquisition or exploration activities of the Company, and are therefore reclassified to exploration and evaluation assets, or property, plant and equipment, dependent on their nature.

Total general and administrative expenses in the three months and year ended December 31, 2013 increased 118% and 96%, respectively, compared to the Corresponding Periods. This increase was due to the increase in the number of employees resulting in additional employee compensation and other administrative costs resulting from the acquisition of Vero in November 2012 and the addition of the assets from the SE Saskatchewan Acquisition, as well as greater drilling activity and production operations consistent with a growing company. However, for the three months and year ended December 31, 2013, G&A per Boe decreased 46% and 59%, respectively, compared to the Corresponding Periods reflecting improving G&A efficiencies on a Boe basis due to the Company's growth.

## MANAGEMENT'S DISCUSSION AND ANALYSIS

### Transaction Related Costs

<i>(\$ thousands, unless otherwise noted)</i>	Three months ended Dec 31, 2013	Three months ended Dec 31, 2012	Year ended Dec 31, 2013	Year ended Dec 31, 2012
Transaction related costs (recovery)	\$ (689)	\$ 3,798	\$ 6,976	\$ 3,798
\$ per Boe	\$ (0.74)	\$ 16.40	\$ 3.12	\$ 8.07

Transaction related expenses are those costs related to acquisitions that cannot be capitalized as part of the cost of such transactions under IFRS. These costs generally include, but are not limited to, legal fees, advisory fees and administrative integration expenses.

For the three months ended December 31, 2013, there was a \$0.7 million reduction of the estimate of the transaction related costs associated with the SE Saskatchewan Acquisition. The transaction related costs in the Corresponding Period related to the Vero acquisition which closed on November 19, 2012.

For the year ended December 31, 2013, transaction related costs of \$7.0 million related to the SE Saskatchewan Acquisition. The transaction related costs in the Corresponding Period related to the Vero acquisition which closed on November 19, 2012.

### Finance Costs (Income)

<i>(\$ thousands)</i>	Three months ended Dec 31, 2013	Three months ended Dec 31, 2012	Year ended Dec 31, 2013	Year ended Dec 31, 2012
Interest expense (income) and financing charges	\$ 975	\$ (11)	\$ 1,387	\$ (339)
Accretion on decommissioning obligations	651	38	905	59
Total	\$ 1,626	\$ 27	\$ 2,292	\$ (280)
\$ per Boe	\$ 1.74	\$ 0.11	\$ 1.02	\$ (0.59)

For the three months and year ended December 31, 2013, interest expense and financing charges increased compared to the Corresponding Periods due to the Company's bank debt incurred largely in connection with the SE Saskatchewan Acquisition.

For the three months and year ended December 31, 2013, accretion on decommissioning obligations increased compared to the Corresponding Periods due to the additional decommissioning obligations assumed by the Company largely in connection with the SE Saskatchewan Acquisition.

Under IFRS, non-cash accretion expenses related to decommissioning obligations are presented as part of finance costs.

### Stock-Based Compensation Expenses

Stock-based compensation expenses reflect the value ascribed to the non-cash compensation provided by the Company, and were calculated utilizing a fair value assessment methodology. These amounts are net of stock-based compensation costs capitalized to exploration and evaluation assets, and property, plant and equipment when they are related to exploration or acquisition activities (in the same manner that G&A expenses are capitalized).

<i>(\$ thousands)</i>	Three months ended Dec 31, 2013	Three months ended Dec 31, 2012	Year ended Dec 31, 2013	Year ended Dec 31, 2012
Stock-based compensation expenses	\$ 4,316	\$ 850	\$ 6,714	\$ 3,975
Capitalized stock-based compensation expenses	(2,121)	(468)	(3,319)	(2,186)
Total	\$ 2,195	\$ 382	\$ 3,395	\$ 1,789
\$ per Boe	\$ 2.35	\$ 1.65	\$ 1.52	\$ 3.80

For the three months and year ended December 31, 2013, the dollar amounts of stock-based compensation expenses, net of capitalized amounts, increased compared to the Corresponding Periods, largely due to the grants of restricted awards and performance awards to the Company's directors, officers and employees, as part of the Company's business model transition to an intermediate dividend plus growth company.



## MANAGEMENT'S DISCUSSION AND ANALYSIS

### Depletion and Depreciation Expenses

For the three months and year ended December 31, 2013, the Company's depletion and depreciation expenses totaled \$25.4 million (\$27.17 per Boe) and \$59.9 million (\$26.81 per Boe), respectively. This compares to the Corresponding Periods of \$6.9 million (\$29.65 per Boe) and \$18.4 million (\$39.05 per Boe), respectively. The decrease on a per Boe basis is the result of lower cost of reserve additions related to wells drilled in 2013, the Vero acquisition, and the SE Saskatchewan Acquisition.

### Taxes

For the three months and year ended December 31, 2013, the Company recorded a deferred income tax recovery of \$4.0 million and a deferred income tax expense of \$1.9 million, respectively (Corresponding Periods: deferred income tax recovery of \$3.6 million and \$2.3 million, respectively).

### Net Loss

The net loss for the three months and year ended December 31, 2013 was \$17.8 million and \$10.1 million, respectively (Corresponding Periods: \$13.7 million and \$18.8 million, respectively).

Basic and diluted net loss per share for the three months and year ended December 31, 2013 was \$0.20 and \$0.18, respectively (Corresponding Periods: net loss per share of \$0.47 and \$0.81, respectively).

### Funds Flow from Operations, excluding Transaction Related Costs/Recovery

Funds flow from operations, excluding transaction related costs/recovery for the three months and year ended December 31, 2013 was \$40.8 million and \$96.5 million, respectively (Corresponding Periods: \$8.0 million and \$17.2 million, respectively).

Basic funds flow from operations, excluding transaction related costs/recovery per share for the three months and year ended December 31, 2013 was \$0.45 and \$1.76, respectively (Corresponding Periods: \$0.28 and \$0.74, respectively). Diluted funds flow from operations, excluding transaction related costs/recovery per share for the three months and year ended December 31, 2013 was \$0.44 and \$1.72, respectively (Corresponding Periods: \$0.26 and \$0.69, respectively).

### Net Cash from Operating Activities

Net cash from operating activities for the three months and year ended December 31, 2013 was \$46.9 million and \$78.8 million, respectively (Corresponding Periods: \$3.1 million and \$8.5 million, respectively).

Basic net cash from operating activities per share for the three months and year ended December 31, 2013 was \$0.51 and \$1.44, respectively (Corresponding Periods: \$0.11 and \$0.37, respectively). Diluted net cash from operating activities per share for the three months and year ended December 31, 2013 was \$0.50 and \$1.40, respectively (Corresponding Periods: \$0.11 and \$0.37, respectively).

## MANAGEMENT'S DISCUSSION AND ANALYSIS

### Capital Expenditures

Capital expenditures are summarized as follows:

<i>(\$ thousands)</i>	<b>Three months ended Dec 31, 2013</b>	Three months ended Dec 31, 2012	<b>Year ended Dec 31, 2013</b>	Year ended Dec 31, 2012
<b>Cash:</b>				
Land retention costs	\$ 119	\$ 62	\$ 609	\$ 403
Geological and geophysical	591	2	900	1,302
Drilling and completions	47,212	32,169	121,673	110,231
Equipment and facilities	12,061	3,959	30,448	11,864
Administrative assets	92	43	161	56
Exploration and development expenditures	60,075	36,235	153,791	123,856
Capitalized general and administrative expenses	1,336	714	3,990	2,441
Exploration and development expenditures, including capitalized G&A	61,411	36,949	157,781	126,297
Property acquisitions, net of dispositions	(4,859)	2,417	489,954	6,646
Total capital expenditures - cash items	\$ 56,552	\$ 39,366	\$ 647,735	\$ 132,943
<b>Non-cash:</b>				
Corporate acquisition	-	164,726	-	164,726
Property acquisition	-	-	1,631	-
Gain on disposition of undeveloped land	5,000	-	5,000	-
Decommissioning obligations	(868)	665	80,906	3,227
Exploration and evaluation	(38,355)	(13,306)	(38,355)	(13,306)
Capitalized stock-based compensation	2,120	468	3,318	2,186
Total capital expenditures	\$ 24,449	\$ 191,919	\$ 700,235	\$ 289,776

In the three months and year ended December 31, 2013, the Company drilled 21 (12.8 net) wells and 42 (26.5 net) wells, respectively. In the Corresponding Periods, the Company drilled nine (6.8 net) wells and 28 (21.6 net) wells, respectively.

In October 2013, the Company disposed of certain non-core undeveloped land for cash proceeds of \$5.0 million. The Company's carrying cost of this undeveloped land was nominal.

For the year ended December 31, 2013, the Company expensed \$38.4 million (year ended December 31, 2012: \$13.3 million) of exploration and evaluation costs related to projects with a carrying value greater than the current market value estimate.

The Company anticipates that its 2014 exploration and development capital program (excluding acquisitions and dispositions) will be financed primarily through funds flow from operations, bank debt and proceeds from equity issuances, if any.

The Company does not set a budget for acquisitions. When making acquisitions, the Company considers opportunities that align with strategic parameters and evaluates and finances each prospect on a case-by-case basis.

## MANAGEMENT'S DISCUSSION AND ANALYSIS

### Share Capital

	Three months ended Dec 31, 2013	Three months ended Dec 31, 2012	Year ended Dec 31, 2013	Year ended Dec 31, 2012
<b>Weighted average outstanding common shares:</b>				
Basic	91,257,722	29,126,778	54,900,265	23,160,504
Diluted	92,929,448	29,126,778	56,120,796	23,160,504
<b>Outstanding Securities:</b>				
Common shares	91,423,437	38,585,523	91,423,437	38,585,523
Stock options	1,640,195	1,580,803	1,640,195	1,580,803
Incentive shares	129,183	175,940	129,183	175,940
Restricted awards	1,249,373	-	1,249,373	-
Performance awards	1,818,018	-	1,818,018	-
Warrants	3,480,000	3,480,000	3,480,000	3,480,000

In August 2013, in connection with the SE Saskatchewan Acquisition, the Company completed an equity financing by issuing 52,434,000 subscription receipts at \$7.85 per subscription receipt for gross proceeds of \$411.6 million, before share issue costs (the number of subscription receipts and price per subscription receipt indicated here reflect amounts after the Share Consolidation). In September 2013, these subscription receipts were converted into common shares of TORC on a one-for-one basis.

In addition, in September 2013, the Company consolidated its outstanding common shares, stock options, incentive shares and warrants on a 1 for 5 basis (the "Share Consolidation"). As a result, the number of outstanding common shares, stock options, incentive shares and warrants of comparative periods have been reduced by a factor of five, in order for the comparative common share, stock options, incentive shares, warrants, per share and per diluted share amounts to be equivalent.

The Company is authorized to issue an unlimited number of common shares and an unlimited number of preferred shares, issuable in series.

As at March 5, 2014, the Company had 91,694,902 common shares issued and outstanding, 1,640,195 stock options outstanding, 124,079 incentive shares outstanding, 1,826,376 performance awards outstanding, 1,255,117 restricted awards outstanding, and 3,480,000 warrants outstanding.

In September 2013, the Company's shareholders approved an award plan (the "Share Award Plan") whereby restricted awards and performance awards (collectively, "Share Awards") may be granted to the directors, officers and employees of the Company. The maximum number of common shares issuable under the Share Award Plan, combined with the Company's existing stock option and incentive share plans, cannot exceed ten percent of the outstanding Common Shares. In addition, the combined number of restricted awards and performance awards cannot exceed 6.5 percent of the outstanding Common Shares. Share Awards are earned over various periods, up to three years from the date of grant. Upon being earned, the restricted awards are converted into Common Shares and issued from treasury at no cost to the recipient. The performance awards are converted into Common Shares using a multiplier between zero and two, dependent on the Company's performance on a set criteria as determined by the Board of Directors.

## MANAGEMENT'S DISCUSSION AND ANALYSIS

### Liquidity and Capital Resources

The Company has a reserves-based revolving credit facility of \$350 million with a syndicate of banks. The credit facility provides that advances may be made by way of direct advances, bankers' acceptances, or standby letters of credit/guarantees. Direct advances bear interest at the agent bank's prime lending rate plus an applicable margin for Canadian dollar advances and at the agent bank's U.S. base rate plus an applicable margin for U.S. dollar advances. The applicable margin charged by the banks is dependent on the Company's debt to trailing cash flow ratio. The bankers' acceptances bear interest at the applicable bankers' acceptance rate plus a stamping fee, based on the Company's debt to trailing cash flow ratio.

The credit facility is secured by a fixed and floating charge debenture on the assets of the Company. The credit facility is available on a revolving basis until April 29, 2014. On or before April 29, 2014, at the request of the Company and subject to the approval of the bank syndicate, the credit facility may be extended for an additional 364 day period. In the event of non-extension, the undrawn portion of the credit facility will be cancelled and the amount outstanding will convert to a 364 day non-revolving term facility with repayment due on April 29, 2015. The borrowing base is primarily based on reserves and commodity prices estimated by the lenders. In the normal course, the Company's next semi-annual credit facility evaluation is due to be completed by April 29, 2014.

The Company has a significant investor, the CPP Investment Board ("CPIB"). For so long as CPIB owns greater than 10% of the outstanding common shares of the Company, it shall have the right to participate in future offerings of securities by the Company, whether by way of public offering or private placement. This includes any offering of common shares and securities convertible or exchangeable into common shares, up to its pro rata ownership interest immediately prior to such offering in the case of a public offering or a private placement to five or more investors, in order to maintain its pro rata percentage ownership interest in the Company, and up to all of the offering in the case of a private placement to less than five investors.

Management is confident that there is sufficient liquidity and capital resources to fund its 2014 capital program and its day-to-day operations.

### Risk Management - Financial Derivatives

From time to time, the Company may enter into commodity price, interest rate and foreign exchange rate derivative contracts (also known as hedges) in order to protect acquisition economics and provide some stability of cash flows for capital spending planning purposes. Commodity prices, interest rates and foreign exchange rates fluctuate due to economic and political events. As well, commodity prices may fluctuate due to weather conditions and changes in supply and demand. The Company's risk management activities are conducted pursuant to the Company's risk management policies approved by the Board of Directors.

At December 31, 2013, the Company had the following commodity contracts outstanding:

Remaining term	Type	Volume (Bbl/d)	Price (per Bbl in Canadian dollars)	Reference
Jan 1, 2014 - Jun 30, 2014	Costless Collar	500	\$100.00 - \$107.00	C\$WTI
Jan 1, 2014 - Jun 30, 2014	Costless Collar	500	\$95.00 - \$109.30	C\$WTI
Jan 1, 2014 - Jun 30, 2014	Oil Swap	500	\$103.75	C\$WTI
Jan 1, 2014 - Jun 30, 2014	Costless Collar	1,000	\$90.00 - \$107.00	C\$WTI
Jan 1, 2014 - Dec 31, 2014	Costless Collar	500	\$95.00 - \$104.60	C\$WTI
Jan 1, 2014 - Dec 31, 2014	Costless Collar	250	\$90.00 - \$107.25	C\$WTI
Jan 1, 2014 - Dec 31, 2014	Costless Collar	250	\$90.00 - \$107.55	C\$WTI
Jan 1, 2014 - Dec 31, 2014	Costless Collar	500	\$95.00 - \$108.50	C\$WTI
Jan 1, 2014 - Dec 31, 2014	Costless Collar	250	\$95.00 - \$105.00	C\$WTI
Jan 1, 2014 - Dec 31, 2014	Costless Collar	250	\$95.00 - \$106.00	C\$WTI
Jul 1, 2014 - Dec 31, 2014	Costless Collar	250	\$90.00 - \$104.03	C\$WTI
Jul 1, 2014 - Dec 31, 2014	Costless Collar	500	\$95.00 - \$105.00	C\$WTI

At December 31, 2013, the mark-to-market value of these commodity contracts totaled a liability of \$0.2 million.

*(continued)*

## MANAGEMENT'S DISCUSSION AND ANALYSIS

Subsequent to December 31, 2013, the Company entered into the following commodity contracts:

Term	Type	Volume (Bbl/d)	Price (per Bbl in Canadian dollars)	Reference
Feb 1, 2014 - Jun 30, 2015	Costless Collar	500	\$95.00 - \$106.25	C\$WTI
Jul 1, 2014 - Dec 31, 2014	Costless Collar	500	\$95.00 - \$105.00	C\$WTI
Jan 1, 2015 - Jun 30, 2015	Costless Collar	250	\$90.00 - \$108.00	C\$WTI
Jan 1, 2015 - Jun 30, 2015	Costless Collar	250	\$90.00 - \$109.55	C\$WTI

### Contractual Obligations

The following table lists the Company's contractual obligations as at December 31, 2013 and the expected timing of these obligations:

<i>(\$ thousands)</i>	Total	Less than 1 year	1-2 years	3-5 years	Thereafter
Trade and other payables	\$ 105,680	\$ 105,680	-	-	-
Dividends payable	4,114	4,114	-	-	-
Operating leases (office rent)	3,247	1,257	1,257	733	-
Farm-in transactions	4,605	4,605	-	-	-
Bank debt	85,000	-	85,000	-	-
<b>Total</b>	<b>\$ 202,646</b>	<b>\$ 115,656</b>	<b>\$ 86,257</b>	<b>\$ 733</b>	<b>-</b>

#### Operating commitments

The Company is, or will be, obligated to pay various costs associated with operations incurred in the normal course of business. These costs include royalties paid to provincial governments, surface lease rentals and mineral rights to various landowners, abandonment and reclamation costs and office leases. These costs are highly dependent on the future operating environment and are subject to changes in commodity prices, ownership, production volumes and government policies.

#### Working capital

The Company manages the pace of its capital spending related to drilling operations by continuously monitoring production, commodity prices and resulting cash flows. Should circumstances affect cash flow in a detrimental way, the Company is capable of reducing its capital spending levels.

The industry has a pre-arranged monthly clearing day for payment of revenues from all buyers of crude oil, NGL and natural gas. This occurs on the 25th day following the month of sale. As a result, the Company's production revenues are collected in an orderly fashion. To the extent that the Company has joint venture partners in its activities it collects the partners' share of capital and operating expenses on a monthly basis. These are subject to normal collection risk.

Accounts payable consist of amounts payable to suppliers relating to capital spending, field operating activities and office expenses. These invoices are processed within the Company's normal payment cycle.

#### Farm-in transactions

The Company has entered into a number of farm-in agreements with third parties to earn interests in additional prospective acreage. At December 31, 2013, the Company's required future commitments are estimated to be \$4.6 million, which form part of the Company's on-going capital program.

#### Flow-through obligation

In November 2012, the Company issued 2,246,340 flow-through shares at a price of \$17.82 per share for gross proceeds of \$40.0 million. As a result, the Company had to incur qualifying resource expenditures amounting to \$40.0 million before December 31, 2013. The qualifying expenditures were renounced to shareholders as at December 31, 2012. As at December 31, 2013, the Company had spent the necessary qualifying resource expenditures and there is no further obligation remaining for this flow-through share issue.

## MANAGEMENT'S DISCUSSION AND ANALYSIS

### Business Conditions and Risks

The Company is engaged in the acquisition, exploration, development and production of crude oil and natural gas assets. TORC's business is inherently risky and there is no assurance that hydrocarbon reserves will be discovered and economically produced. Financial risks associated with the petroleum industry include fluctuations in commodity prices, interest rates, currency exchange rates, and the ability to access debt and equity financing at reasonable cost. Operational risks include competition, environmental factors, reservoir performance uncertainties, a complex regulatory environment and safety concerns.

TORC uses its technical, technological and industry knowledge to evaluate potential hydrocarbon plays in order to pay what it believes are economically sound prices that benefit shareholders. The Company's focus is on areas in which the prospects are understood by management.

The Company minimizes its business risks by operating a large number of its properties. This enables TORC to control the timing, direction and costs related to exploration and development opportunities. TORC's geological focus is on areas in which the prospects are understood by management. Technological tools are regularly used to reduce risk and increase the probability of success.

The Company complies with all government regulations and has an up-to-date emergency response plan that has been communicated to field operations by management. The Company also carries insurance coverage to protect itself against potential losses. Maintaining a highly motivated and talented staff of petroleum and natural gas professionals further minimizes the business risk.

TORC relies on appropriate sources of funding to support the various stages of its business strategy:

- Internally-generated cash flow from production is used to fund business activities;
- New equity, if available on favourable terms, may be utilized to fund acquisitions and to expand capital programs, when appropriate; and
- Debt may be utilized to fund acquisitions and to expand capital programs.

The Company is exposed to commodity price and market risk for its principal products of crude oil and natural gas. Commodity prices are influenced by a wide variety of factors, most of which are beyond TORC's control. To manage this risk, from time to time, the Company may enter into a number of financial derivative contracts for hedging purposes. These derivative contracts may include contracts related to crude oil and natural gas prices, as well as foreign exchange and interest rates. The Company may also, from time to time, enter into fixed physical contracts. The Company monitors the cost and associated benefit of these instruments and contracts as well as any debt levels and utilization rates on bank lines, and utilizes these derivatives and contracts when warranted.

Inflation risks subject the Company to potential erosion of product netbacks. For example, increasing domestic prices for oil and natural gas production equipment and services can inflate the costs of operations. In addition, increasing costs of undeveloped land can inflate costs of both asset and corporate acquisitions.

The supply of service and production equipment at competitive prices is critical to the ability to add reserves at a reasonable cost and produce them in an economic and timely fashion. In periods of increased activity, these services and supplies can become difficult to obtain. The Company attempts to mitigate this risk by developing strong long-term relationships with suppliers and contractors and maintaining an appropriate inventory of production equipment.

Demand for crude oil, NGL and natural gas produced by the Company exists within Canada and the United States; however, crude oil prices are affected by worldwide supply and demand fundamentals while natural gas prices are currently primarily affected by North American supply and demand fundamentals. Demand for natural gas liquids is influenced mainly by the demand for petrochemicals in North American and off-shore markets. TORC mitigates these risks as follows:

- TORC attempts to explore for and produce crude oil that is of high quality, mitigating its exposure to adverse quality differentials;
- Natural gas production will generally be connected to established pipeline infrastructures that operate with minimal interruptions;
- Sale arrangements will vary in term and pricing structure creating a diverse portfolio that minimizes risk of exposure to any one market; and
- Financial derivative contracts may be used where appropriate to manage commodity price volatility.

## MANAGEMENT'S DISCUSSION AND ANALYSIS

### Off Balance Sheet Arrangements

TORC is not involved with any contractual arrangement under which a non-consolidated entity may have an obligation under certain guarantee contracts, a retained or contingent interest in assets transferred to a non-consolidated entity or similar arrangement that serves as credit, liquidity or market risk support to that entity for such assets. TORC has no obligation under financial instruments or a variable interest in an unconsolidated entity that provides financing, liquidity, market risk or credit risk support to the Company.

### Critical Accounting Estimates

The preparation of financial statements in conformity with IFRS requires management to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Estimates and underlying assumptions are reviewed on an ongoing basis. Actual results may differ from these estimates.

#### Reserves

The estimation of reserves is critical to various accounting estimates. It requires judgments based on available geophysical, geological, engineering and economic data. These estimates can change materially as information from ongoing exploratory, development and production activities becomes available. These estimates can also change as economic conditions impacting crude oil and natural gas prices, royalties and operating costs change. Reserve estimates can change net income through depletion expense, accretion expense from decommissioning obligations and the application of impairment tests. Revisions or changes in reserve estimates can have either a positive or a negative impact on net income.

#### Decommissioning obligations

The calculation of decommissioning obligations is based on estimated costs to abandon and reclaim its net ownership in all wells and facilities, the estimated timing of the costs to be incurred and economic inflation and discount rates. These estimates can change due to technological advances, governmental and regulatory laws and regulations or economic conditions and can impact the amount of the decommissioning obligations and net income.

#### Stock-based compensation

The Company's estimate of stock-based compensation is dependent upon estimates of historic volatility, forfeiture rates and an assessment of achieving performance conditions. These estimates can impact net income and contributed surplus.

#### Financial derivatives

By their very nature, the estimated fair value of financial derivative contracts resulting in financial derivative contract assets and liabilities are subject to measurement uncertainty.

#### Deferred income taxes

The calculation of deferred income taxes includes estimates of reversal of temporary differences, tax rates substantively enacted and likelihood of assets being realized. These estimates can impact net income and deferred tax liabilities.

### Environmental Regulation and Risk

The oil and gas industry has various environmental risks subject to regulation by various governmental bodies. Environmental legislation includes, but is not limited to, operational controls, site restoration and abandonment requirements and restrictions on emissions of various substances related to the production of oil and natural gas. Compliance with this legislation may require additional costs and a failure to comply may result in fines and penalties.

TORC is committed to minimizing the environmental impact from its operations through an environmental program which includes stakeholder communication, resource conservation and site restoration.

## MANAGEMENT'S DISCUSSION AND ANALYSIS

### Adopted Accounting Pronouncements

On January 1, 2013, the Company adopted new standards with respect to consolidations (IFRS 10), joint arrangements (IFRS 11), disclosure of interests in other entities (IFRS 12), fair value measurements (IFRS 13) and amendments to financial instrument disclosures (IFRS 7). The adoption of these standards had no impact on the amounts recorded in the financial statements as at January 1, 2013 or on the comparative periods.

### Disclosure Controls and Internal Controls Over Financial Reporting

#### Disclosure controls

Disclosure controls and procedures ("DCP") have been designed to provide reasonable assurance that all relevant information is identified to management to ensure appropriate and timely decisions are made regarding public disclosures. An evaluation of the design and effectiveness of DCP has been conducted by management, under the supervision of the CEO and CFO. Based on this evaluation, the CEO and CFO concluded that the disclosure controls and procedures are appropriately designed and operating effectively to provide reasonable assurance that material information relating to TORC is made known to them and others in the Company.

#### Internal control over financial reporting

Internal controls over financial reporting ("ICFR") have been designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with Canadian GAAP. A control system, no matter how well conceived or operated can only provide reasonable, not absolute assurance that the objective of the control system is met. An evaluation of the design and effectiveness of ICFR has been conducted by management, under the supervision of the CEO and CFO. Based on this evaluation, the CEO and CFO concluded that ICFR were effective as of December 31, 2013. There were no material changes to the internal controls over financial reporting during the three months or year ended December 31, 2013.

### Additional Information

Additional information can be obtained by contacting the Company at TORC Oil & Gas Ltd., Suite 1800, Eighth Avenue Place, 525 - 8th Avenue SW, Calgary, Alberta, Canada T2P 1G1 or by email at [info@torcoil.com](mailto:info@torcoil.com). Additional information is also available on [www.sedar.com](http://www.sedar.com) and on the Company's website [www.torcoil.com](http://www.torcoil.com).



## MANAGEMENT'S DISCUSSION AND ANALYSIS

### Summary of Quarterly and Annual Results

<i>(in \$000's of dollars, except per share amounts)</i>	Q4 2013 <small>(1)</small>	Q3 2013	Q2 2013	Q1 2013	Q4 2012 <small>(1)</small>	Q3 2012 <small>(1)</small>	Q2 2012 <small>(1)</small>	Q1 2012 <small>(1)</small>
Petroleum and natural gas sales	<b>68,206</b>	41,717	28,117	26,034	14,567	6,237	5,350	6,557
Net income (loss)	<b>(17,841)</b>	3,287	3,340	1,130	(13,677)	(1,659)	(840)	(2,591)
Per share – basic <sup>(2)</sup>	<b>(0.20)</b>	0.06	0.09	0.03	(0.47)	(0.08)	(0.04)	(0.12)
Per share – diluted <sup>(2)</sup>	<b>(0.20)</b>	0.06	0.09	0.03	(0.47)	(0.08)	(0.04)	(0.12)
Funds flow from operations, including transaction related costs/recovery <sup>(3)</sup>	<b>41,458</b>	16,223	16,580	15,274	4,241	2,932	2,428	3,794
Per share – basic <sup>(2)</sup>	<b>0.45</b>	0.32	0.43	0.40	0.15	0.14	0.11	0.18
Per share – diluted <sup>(2)</sup>	<b>0.45</b>	0.32	0.42	0.38	0.14	0.14	0.11	0.18
Funds flow from operations, excluding transaction related costs/recovery <sup>(3)</sup>	<b>40,769</b>	24,163	16,397	15,182	8,039	2,932	2,428	3,794
Per share – basic <sup>(2)</sup>	<b>0.45</b>	0.48	0.42	0.39	0.28	0.14	0.11	0.18
Per share – diluted <sup>(2)</sup>	<b>0.44</b>	0.47	0.42	0.38	0.26	0.14	0.11	0.18
Net cash from (used in) operating activities <sup>(4)</sup>	<b>46,912</b>	6,055	16,153	9,665	3,076	(172)	2,550	3,060
Per share – basic <sup>(2)</sup>	<b>0.51</b>	0.12	0.42	0.25	0.11	(0.01)	0.12	0.14
Per share – diluted <sup>(2)</sup>	<b>0.50</b>	0.12	0.41	0.24	0.11	(0.01)	0.12	0.14
Total assets	<b>1,215,153</b>	1,200,628	611,283	627,989	627,457	361,755	356,919	376,184
Total long-term financial liabilities	<b>183,725</b>	194,647	29,006	25,995	20,806	10,865	10,946	10,926
Cash dividends declared per share	<b>0.0428</b>	0.0417	-	-	-	-	-	-
Net working capital (net debt) <sup>(5)</sup>	<b>(145,183)</b>	(121,486)	(2,088)	38	35,077	(3,392)	13,396	35,089

*(footnotes on next page)*

## MANAGEMENT'S DISCUSSION AND ANALYSIS

<i>(in \$000's of dollars, except per share amounts)</i>	Year ended Dec 2013 <sup>(1)</sup>	Year ended Dec 2012 <sup>(1)</sup>	Year ended Dec 2011 <sup>(1)</sup>
Petroleum and natural gas sales	164,074	32,711	3,369
Net loss	(10,084)	(18,767)	(4,667)
Per share – basic <sup>(2)</sup>	(0.18)	(0.81)	(0.28)
Per share – diluted <sup>(2)</sup>	(0.18)	(0.81)	(0.28)
Funds flow from operations, including transaction related costs/recovery <sup>(3)</sup>	89,536	13,396	521
Per share – basic <sup>(2)</sup>	1.63	0.58	0.03
Per share – diluted <sup>(2)</sup>	1.60	0.54	0.03
Funds flow from operations, excluding transaction related costs/recovery <sup>(3)</sup>	96,512	17,193	521
Per share – basic <sup>(2)</sup>	1.76	0.74	0.03
Per share – diluted <sup>(2)</sup>	1.72	0.69	0.03
Net cash from (used in) operating activities <sup>(4)</sup>	78,785	8,514	(600)
Per share – basic <sup>(2)</sup>	1.44	0.37	(0.04)
Per share – diluted <sup>(2)</sup>	1.40	0.34	(0.04)
Total assets	1,215,153	627,457	368,462
Total long-term financial liabilities	183,725	20,806	7,201
Cash dividends declared per share	0.0426	-	-
Net working capital (net debt) <sup>(5)</sup>	(145,183)	35,077	81,138

<sup>(1)</sup> The diluted number of shares is equivalent to the basic number of shares due to stock options, incentive shares, performance and restricted awards, and/or warrants being antidilutive in periods where the Company has a "net loss" or "net cash used in operating activities". Therefore, the diluted per share amounts in these periods are equivalent to the basic per share amounts.

<sup>(2)</sup> The corporate acquisition of Vero in November 2012 has been accounted for as a reverse takeover. As a result, the number of outstanding common shares, stock options, incentive shares and warrants of comparative periods have been reduced by a factor of 0.87 (the arrangement exchange ratio), in order for the comparative common share, stock options, incentive shares, warrants, per share and per diluted share amounts to be equivalent. In addition, in September 2013, the Company consolidated its outstanding common shares, stock options, incentive shares and warrants on a 1 for 5 basis. As a result, the number of outstanding common shares, stock options, incentive shares and warrants of comparative periods have been reduced by a factor of five, in order for the comparative common share, stock options, incentive shares, warrants, per share and per diluted share amounts to be equivalent.

<sup>(3)</sup> "Funds flow from operations, including transaction related costs/recovery" and "funds flow from operations, excluding transaction related costs/recovery" should not be considered an alternative to, or more meaningful than, "net cash from (used in) operating activities" as determined in accordance with International Financial Reporting Standards ("IFRS") as an indicator of TORC's performance. "Funds flow from operations, including transaction related costs/recovery" represents net cash from (used in) operating activities prior to changes in non-cash working capital and settlement of decommissioning obligations. "Funds flow from operations, excluding transaction related costs/recovery" represents net cash from (used in) operating activities prior to changes in non-cash working capital, settlement of decommissioning obligations and transaction related costs. TORC also presents "funds flow from operations, including transaction related costs/recovery" and "funds flow from operations, excluding transaction related costs/recovery" on a per share basis, whereby per share amounts are calculated using weighted average shares outstanding consistent with the calculation of earnings per share.

<sup>(4)</sup> Net cash from (used in) operating activities is determined in accordance with IFRS and includes changes in non-cash working capital.

<sup>(5)</sup> Net working capital (net debt) is calculated as current assets (excluding financial derivative assets) less current liabilities (excluding financial derivative liabilities), bank debt and non-current deferred lease incentives.

Since its incorporation on March 23, 2010, the Company has accumulated light oil resource prone acreage and is delineating and developing its resource base. In November 2012, the Company acquired Vero and completed an equity financing. In September 2013, the Company acquired significant assets in southeast Saskatchewan, along with another equity financing. These events have resulted in an increase in total assets, comprised largely of land and wells, as well as increased petroleum and natural gas sales, influenced by commodity prices and commodity mix.



## **Financial Statements**

As at and for the years ended

December 31, 2013 and 2012

## FINANCIAL STATEMENTS

### MANAGEMENT'S STATEMENT OF RESPONSIBILITY

The accompanying financial statements of TORC Oil & Gas Ltd. were prepared by and are the responsibility of management. They have been prepared in conformity with International Financial Reporting Standards as issued by the International Accounting Standards Board and include certain assessments that reflect management's best estimates and judgments. Management has determined such amounts on a reasonable basis in order to ensure that the financial statements are presented fairly in all material respects. The financial information contained elsewhere in Management's Discussion and Analysis has been reviewed to ensure consistency with the financial statements.

Management has developed and maintains systems of internal controls designed to provide reasonable assurance that all transactions are properly recorded in the Company's financial records, that procedures and policies are adhered to, that the financial statements realistically report the Company's operating and financial results, and that assets are safeguarded from unauthorized use. Management believes that this system of internal controls has operated effectively for the year ended December 31, 2013.

KPMG LLP, an independent firm of chartered accountants, has been engaged to examine the financial statements in accordance with Canadian generally accepted auditing standards and to provide an independent auditors' report thereon.

The Board of Directors, through its Audit Committee, has reviewed the financial statements including notes thereto with management and KPMG LLP. The Audit Committee is composed of three unrelated and independent members of the Board of Directors and meets quarterly with the financial officers of the Company. KPMG LLP has access to the Audit Committee to review the planning and scope of testing and to discuss the results of their audit work. On the recommendation of the Audit Committee, the accompanying financial statements have been approved by the Board of Directors.

*(signed)*

Brett Herman  
President and  
Chief Executive Officer

March 5, 2014  
Calgary, Canada

*(signed)*

Jason Zabinsky  
Vice President, Finance and  
Chief Financial Officer

## FINANCIAL STATEMENTS

### INDEPENDENT AUDITORS' REPORT

*To the Shareholders of TORC Oil & Gas Ltd.*

We have audited the accompanying financial statements of TORC Oil & Gas Ltd., which comprise the statements of financial position as at December 31, 2013 and December 31, 2012, the statements of loss and comprehensive loss, changes in equity and cash flows for the years then ended, and notes, comprising a summary of significant accounting policies and other explanatory information.

#### *Management's Responsibility for the Financial Statements*

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

#### *Auditors' Responsibility*

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

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

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

#### *Opinion*

In our opinion, the financial statements present fairly, in all material respects, the financial position of TORC Oil & Gas Ltd. as at December 31, 2013 and December 31, 2012, and its financial performance and its cash flows for the years then ended in accordance with International Financial Reporting Standards.

*(signed)*

KPMG LLP  
Chartered Accountants

March 5, 2014  
Calgary, Canada

## FINANCIAL STATEMENTS

**TORC Oil & Gas Ltd.**  
**Statements of Financial Position**  
**(in \$000's of Canadian dollars)**

	Note	As at December 31, 2013	As at December 31, 2012
<b>Assets</b>			
Cash and cash equivalents		\$ 13,626	\$ 79,715
Trade and other receivables		34,418	19,096
Deposits and prepaid expenses		2,024	2,369
Financial derivative asset	21	-	1,526
<b>Total current assets</b>		<b>50,068</b>	<b>102,706</b>
Exploration and evaluation assets	11	129,093	151,111
Property, plant and equipment	12	1,035,992	373,640
<b>Total non-current assets</b>		<b>1,165,085</b>	<b>524,751</b>
<b>Total assets</b>		<b>\$ 1,215,153</b>	<b>\$ 627,457</b>
<b>Liabilities</b>			
Trade and other payables		\$ 105,680	\$ 65,470
Dividends payable	17	4,114	-
Deferred lease incentives		177	177
Financial derivative liability	21	220	-
<b>Total current liabilities</b>		<b>110,191</b>	<b>65,647</b>
Bank debt	20	85,000	-
Deferred premium on flow-through shares	22	-	5,233
Deferred lease incentives		280	456
Decommissioning obligations	14	93,045	11,408
Deferred tax liability	15	5,400	3,709
<b>Total non-current liabilities</b>		<b>183,725</b>	<b>20,806</b>
<b>Total liabilities</b>		<b>\$ 293,916</b>	<b>\$ 86,453</b>
<b>Equity</b>			
Share capital	16	\$ 958,754	\$ 558,630
Contributed surplus		11,881	6,165
Deficit		(49,398)	(23,791)
<b>Total equity</b>		<b>921,237</b>	<b>541,004</b>
<b>Total liabilities and equity</b>		<b>\$ 1,215,153</b>	<b>\$ 627,457</b>

Commitments (note 22)  
Subsequent events (note 23)

See accompanying notes to the financial statements.

Approved on behalf of the Board

(signed)

Raymond Chan  
Director

(signed)

Brett Herman  
Director

## FINANCIAL STATEMENTS

### TORC Oil & Gas Ltd.

#### Statements of Loss and Comprehensive Loss

(in \$000's of Canadian dollars, except per share amounts)

Note	Year ended Dec 31, 2013	Year ended Dec 31, 2012
<b>Revenues</b>		
	\$ 164,074	\$ 32,711
	(24,353)	(3,323)
	<b>139,721</b>	<b>29,388</b>
	(163)	287
21	(187)	(890)
	<b>139,371</b>	<b>28,785</b>
<b>Expenses</b>		
	26,431	6,033
	8,156	3,174
	7,072	3,614
6, 7	6,976	3,798
9	2,292	(280)
18	3,395	1,789
12	59,901	18,373
13	(5,000)	-
11	38,355	13,306
	<b>147,578</b>	<b>49,807</b>
	(8,207)	(21,022)
15	1,877	(2,255)
	<b>\$ (10,084)</b>	<b>\$ (18,767)</b>
<b>Loss per share:</b>		
19	\$ (0.18)	\$ (0.81)
19	\$ (0.18)	\$ (0.81)

See accompanying notes to the financial statements.

## FINANCIAL STATEMENTS

### TORC Oil & Gas Ltd.

#### Statements of Changes in Equity

(in \$000's of Canadian dollars, unless otherwise noted)

	Number of common shares	Number of warrants	Share capital	Contributed surplus	Deficit	Total equity
Balance at December 31, 2011	21,129	3,480	\$ 329,836	\$ 3,106	\$ (5,024)	\$ 327,918
Issue of common shares	7,606	-	120,101	-	-	120,101
Common shares issued for corporate acquisition	9,798	-	119,052	-	-	119,052
Stock-based compensation	-	-	-	3,975	-	3,975
Issued on vesting of incentive shares	52	-	-	-	-	-
Transfer of stock-based compensation on vesting of incentive shares	-	-	916	(916)	-	-
Share issue costs, net of tax of \$1.6 million	-	-	(4,820)	-	-	(4,820)
Flow-through share liability	-	-	(6,455)	-	-	(6,455)
Loss for the year	-	-	-	-	(18,767)	(18,767)
<b>Balance at December 31, 2012</b>	<b>38,585</b>	<b>3,480</b>	<b>\$ 558,630</b>	<b>\$ 6,165</b>	<b>\$ (23,791)</b>	<b>\$ 541,004</b>
Issue of common shares (note 16)	52,434	-	411,607	-	-	411,607
Stock-based compensation	-	-	-	6,714	-	6,714
Issued on vesting of incentive shares	54	-	-	-	-	-
Transfer of stock-based compensation on vesting of incentive shares	-	-	998	(998)	-	-
Share issue cost recovery, net of tax of \$5.3 million	-	-	(15,673)	-	-	(15,673)
Dividends to shareholders (note 17)	-	-	-	-	(15,523)	(15,523)
Issued pursuant to the Share Dividend Program (note 17)	350	-	3,192	-	-	3,192
Loss for the year	-	-	-	-	(10,084)	(10,084)
<b>Balance at December 31, 2013</b>	<b>91,423</b>	<b>3,480</b>	<b>\$ 958,754</b>	<b>\$ 11,881</b>	<b>\$ (49,398)</b>	<b>\$ 921,237</b>

See accompanying notes to the financial statements.



## FINANCIAL STATEMENTS

**TORC Oil & Gas Ltd.**  
**Statements of Cash Flows**  
(in \$000's of Canadian dollars)

Note	Year ended Dec 31, 2013	Year ended Dec 31, 2012
<b>Cash flows from (used in) operating activities:</b>		
Loss for the year	\$ (10,084)	\$ (18,767)
Depletion and depreciation	59,901	18,373
Stock-based compensation	3,395	1,789
Deferred income tax (recovery)	1,877	(2,255)
Accretion on decommissioning obligations	905	59
Unrealized loss on financial derivatives	187	890
Gain on disposition of undeveloped land	(5,000)	-
Exploration and evaluation	38,355	13,306
Settlement of decommissioning obligations	(262)	(98)
Change in non-cash working capital	10 (10,489)	(4,783)
Net cash from operating activities	78,785	8,514
<b>Cash flows from (used in) investing activities:</b>		
Additions to exploration and evaluation assets	(43,023)	(93,514)
Additions to property, plant and equipment	(119,690)	(41,150)
Property acquisitions	(488,889)	-
Disposal of exploration and evaluation assets	7,666	1,721
Change in non-cash working capital	10 31,575	15,558
Net cash used in investing activities	(612,361)	(117,385)
<b>Cash flows from (used in) financing activities:</b>		
Proceeds from (repayment of) bank debt	85,000	(36,085)
Proceeds from issue of share capital	411,607	120,101
Share issue costs	(20,903)	(6,427)
Dividends	(8,217)	-
Change in non-cash working capital	10 -	250
Net cash from financing activities	467,487	77,839
Change in cash and cash equivalents	(66,089)	(31,032)
Cash and cash equivalents, beginning of year	79,715	110,747
Cash and cash equivalents, end of year	\$ 13,626	\$ 79,715

See accompanying notes to the financial statements.

## FINANCIAL STATEMENTS

### TORC Oil & Gas Ltd.

#### Notes to the Financial Statements

As at and for the years ended December 31, 2013 and December 31, 2012

(in \$000's of Canadian dollars, unless otherwise noted)

#### 1. Reporting entity

TORC Oil & Gas Ltd. (the "Company" or "TORC") was incorporated pursuant to the Business Corporations Act (Alberta) on March 23, 2010 as 1525893 Alberta Ltd. The Company's name was changed to TORC Oil & Gas Ltd. on December 17, 2010. The Company's principal business activity is the exploration for and production of petroleum and natural gas in the Western Canadian Sedimentary Basin.

The Company's principal place of business is located at Suite 1800, Eighth Avenue Place, 525 - 8th Avenue SW, Calgary, Alberta, Canada T2P 1G1.

#### 2. Basis of preparation

In September 2013, the Company consolidated its outstanding common shares, stock options, incentive shares and warrants on a 1 for 5 basis (the "Share Consolidation"). As a result, the number of outstanding common shares, stock options, incentive shares and warrants of comparative periods have been reduced by a factor of five, in order for the comparative common share, stock options, incentive shares, warrants, per share and per diluted share amounts to be equivalent.

Operating expenses in the statement of income and comprehensive income are presented as a combination of function and nature to conform with industry practice. Depletion and depreciation is presented on a separate line by its nature, while operating expenses and general and administrative expenses are presented on a functional basis. Significant expenses such as key management personnel's short-term employee benefits and stock-based compensation are presented by their nature in the notes to the financial statements.

##### (a) Statement of compliance

The financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") and were authorized for issue by the Board of Directors on March 5, 2014.

##### (b) Basis of measurement

The financial statements have been prepared on the historical cost basis, except for derivative financial instruments which are measured at fair value.

##### (c) Functional and presentation currency

The financial statements are presented in Canadian dollars, which is the Company's functional currency.

##### (d) Use of estimates and judgments

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

Estimates and their underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the year in which the estimates are revised and for any future years affected.

##### *Critical judgments in applying accounting policies:*

The following are critical judgments that management has made in the process of applying accounting policies and that have the most significant effect on the amounts recognized in the financial statements.

The Company's assets are aggregated into cash generating units for the purpose of calculating impairment. Cash generating units ("CGU" or "CGUs") are based on an assessment of the unit's ability to generate independent cash inflows. The determination of these CGUs was based on management's judgment in regards to shared infrastructure, geographical proximity, petroleum type and similar exposure to market risk and materiality.

*(continued)*

## FINANCIAL STATEMENTS

### TORC Oil & Gas Ltd.

#### Notes to the Financial Statements

As at and for the years ended December 31, 2013 and December 31, 2012

(in \$000's of Canadian dollars, unless otherwise noted)

Judgments are required to assess when impairment indicators exist and impairment testing is required. In determining the recoverable amount of assets, in the absence of quoted market prices, impairment tests are based on estimates of reserves, production rates, future oil and natural gas prices, future costs, discount rates, market value of land and other relevant assumptions.

The application of the Company's accounting policy for exploration and evaluation assets requires management to make certain judgments as to future events and circumstances as to whether economic quantities of reserves will be found so as to assess if technical feasibility and commercial viability has been achieved.

Judgments are made by management to determine the likelihood of whether deferred income tax assets at the end of the reporting period will be realized from future taxable earnings.

#### *Key sources of estimation uncertainty:*

The following are key estimates and their assumptions made by management affecting the measurement of balances and transactions in these financial statements.

Estimation of recoverable quantities of proven and probable reserves include estimates and assumptions regarding future commodity prices, exchange rates, discount rates and production and transportation costs for future cash flows as well as the interpretation of complex geological and geophysical models and data. Changes in reported reserves can affect the impairment of assets, the decommissioning obligations, the economic feasibility of exploration and evaluation assets and the amounts reported for depletion, depreciation and amortization of property, plant and equipment. These reserve estimates are verified by third party professional engineers, who work with information provided by the Company to establish reserve determinations in accordance with National Instrument 51-101.

The Company estimates the decommissioning obligations for oil and natural gas wells and their associated production facilities and pipelines. In most instances, removal of assets and remediation occurs many years into the future. Amounts recorded for the decommissioning obligations and related accretion expense require assumptions regarding removal date, future environmental legislation, the extent of reclamation activities required, the engineering methodology for estimating cost, inflation estimates, future removal technologies in determining the removal cost, and the estimate of the liability specific discount rates to determine the present value of these cash flows.

In a business combination, management makes estimates of the fair value of assets acquired and liabilities assumed which includes assessing the value of oil and gas properties based upon the estimation of recoverable quantities of proven and probable reserves being acquired.

The Company's estimate of stock-based compensation is dependent upon estimates of historic volatility, forfeiture rates and an assessment of achieving performance conditions.

The Company's estimate of the fair value of derivative financial instruments is dependent on estimated forward prices and volatility in those prices.

The deferred tax liability is based on estimates as to the timing of the reversal of temporary differences, substantively enacted tax rates and the likelihood of assets being realized.

#### (e) Adoption of new accounting policies

On January 1, 2013, the Company adopted new standards with respect to consolidations (IFRS 10), joint arrangements (IFRS 11), disclosure of interests in other entities (IFRS 12), fair value measurements (IFRS 13) and amendments to financial instrument disclosures (IFRS 7). The adoption of these standards had no impact on the amounts recorded in the financial statements as at January 1, 2013 or on the comparative periods.

## FINANCIAL STATEMENTS

### TORC Oil & Gas Ltd.

#### Notes to the Financial Statements

As at and for the years ended December 31, 2013 and December 31, 2012

(in \$000's of Canadian dollars, unless otherwise noted)

### 3. Significant accounting policies

The accounting policies set out below have been applied consistently to the years presented in the financial statements by the Company.

#### (a) Basis of consolidation

##### (i) Subsidiaries

Subsidiaries are entities controlled by the Company. Control exists when the Company has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. In assessing control, substantive potential voting rights are taken into consideration. The financial statements of subsidiaries are included in consolidated financial statements from the date that control commences until the date that control ceases.

The purchase method of accounting is used to account for acquisitions of subsidiaries and assets that meet the definition of a business under IFRS. The cost of an acquisition is measured as the fair value of assets given, equity instruments issued and liabilities incurred or assumed at the date of exchange. Identifiable assets acquired and liabilities assumed in a business combination are measured initially at their fair values at the acquisition date. The excess of the cost of acquisition over the fair value of the identifiable assets and liabilities acquired is recorded as goodwill. If the cost of acquisition is less than the fair value of the net assets of the subsidiary acquired, the difference is recognized immediately in the statement of income and comprehensive income.

##### (ii) Jointly controlled assets

Many of the Company's oil and natural gas activities involve jointly controlled assets. The financial statements include the Company's share of these jointly controlled assets and a proportionate share of the relevant revenue and related costs.

##### (iii) Transactions eliminated on consolidation

Intercompany balances and transactions, and any unrealized income and expenses arising from intercompany transactions, are eliminated in preparing consolidated financial statements.

#### (b) Foreign currency

Transactions in foreign currencies are translated to Canadian dollars at exchange rates at the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies are translated to Canadian dollars at the period end exchange rate. Non-monetary assets and liabilities denominated in foreign currencies that are measured at fair value are translated to Canadian dollars at the exchange rate at the date that the fair value was determined. Foreign currency differences arising on translation are recognized in the statement of income and comprehensive income.

#### (c) Financial instruments

##### Non-derivative financial instruments

Non-derivative financial instruments are comprised of cash and cash equivalents including bank overdrafts, trade and other receivables, trade and other payables, dividends payable and bank debt. Non-derivative financial instruments are recognized initially at fair value plus any directly attributable transaction costs. Subsequent to initial recognition, non-derivative financial instruments are measured as described below.

##### *Cash and cash equivalents:*

Cash and short term deposits on the statement of financial position comprise cash at banks and on hand and short term deposits with an original maturity of three months or less.

(continued)

## FINANCIAL STATEMENTS

### TORC Oil & Gas Ltd.

#### Notes to the Financial Statements

As at and for the years ended December 31, 2013 and December 31, 2012

(in \$000's of Canadian dollars, unless otherwise noted)

For the purpose of the statement of cash flows, cash and cash equivalents consist of cash and cash equivalents defined above, net of outstanding bank overdrafts.

#### *Other:*

Other non-derivative financial instruments, such as bank debt, trade and other receivables, trade and other payables and dividends payable, are measured at amortized cost using the effective interest method, less any impairment losses.

#### Derivative financial instruments

The Company may enter into certain financial derivative contracts (often known as "hedges") in order to manage the exposure to market risks from fluctuations in commodity prices, interest rates and foreign exchange rates. These instruments are not used for trading or speculative purposes. The Company has not designated its financial derivative contracts as effective accounting hedges, and thus has not applied hedge accounting, even though the Company considers all commodity contracts to be economic hedges. As a result, all financial derivative contracts are classified at fair value through profit and loss and are recorded on the statement of financial position at fair value. Related transaction costs such as trading commissions are recognized in the statement of income and comprehensive income when incurred.

Forward physical delivery and sales contracts of oil and natural gas products are entered into under normal course of business and therefore not recorded at fair value on the statement of financial position. These physical delivery contracts are not considered to be derivative financial instruments or hedges. Settlements on these physical delivery contracts are recognized in oil and natural gas revenue on the statement of income and comprehensive income.

#### Share capital

Common shares are classified as equity. Incremental costs directly attributable to the issue of common shares, warrants and share options are recognized as a deduction from equity, net of any tax effects.

#### (d) Exploration and evaluation assets ("E&E")

Costs incurred prior to the ownership of licenses and rights to drill on properties are expensed in the statement of income and comprehensive income as incurred, if the related licenses and rights are not subsequently acquired.

The costs incurred to acquire licenses and rights to drill, including seismic costs, and the subsequent drilling and completing costs related to these licenses (including employee remuneration, materials and fuel used, rig costs and payments made to contractors) are capitalized as E&E assets until the drilling of the well is complete and the results have been evaluated.

E&E assets are accumulated in cost centers pending the determination of technical feasibility and commercial viability of the drilling project. Technical feasibility and commercial viability is considered to be achieved when proven reserves are determined to exist. Upon determination of proven reserves, the related E&E assets are typically reclassified to a different long-term asset category, Property, Plant and Equipment ("PP&E"), where the assets may be subject to depletion expense.

E&E assets are measured at cost less accumulated impairment losses and not subject to depletion expense until after these assets are reclassified to PP&E.

As facts and circumstances suggest, E&E assets are tested for impairment. The Company compares the carrying amount of its total E&E assets to the assets' recoverable amount, which, for E&E assets, is generally the fair market value of undeveloped land at the time of impairment testing. In addition, E&E assets related to specific technically feasible and commercially viable cost centers are tested for impairment if and when they are reclassified to PP&E. E&E assets are aggregated with the associated cash generating units for the purposes of impairment testing.

*(continued)*

## FINANCIAL STATEMENTS

### TORC Oil & Gas Ltd.

#### Notes to the Financial Statements

As at and for the years ended December 31, 2013 and December 31, 2012

(in \$000's of Canadian dollars, unless otherwise noted)

Impairment losses recognized in prior periods are assessed as facts and circumstances suggest to evaluate if those losses have decreased or no longer exist. If those impairment losses have decreased or no longer exist (recovered), they are reversed accordingly. Previously recognized impairment losses may be recovered in future reporting periods due to changes in estimates used to determine the recoverable amount. An impairment loss recovery is recorded only to the extent that the E&E asset's carrying amount does not exceed the carrying amount that would have been determined if no impairment loss had been recognized. Impairment losses and recoveries are recorded in the statement of income and comprehensive income.

(e) Property, plant and equipment ("PP&E")

There are two categories of PP&E: Developed and Producing ("D&P") assets and Other PP&E assets.

D&P assets include capital costs (i) related to drilling projects where the drilling location is already determined to hold proven reserves, (ii) that have been reclassified from E&E assets because proven reserves have been determined, and (iii) incurred to improve an already technically feasible and commercially viable well.

Other PP&E typically includes furniture, fixtures, leasehold improvements and office equipment.

For statement of financial position presentation, both D&P assets and Other PP&E are included in the PP&E category.

(i) Recognition and measurement

PP&E is measured at cost less accumulated depletion and depreciation and accumulated impairment losses. For the purposes of depletion and depreciation, when significant parts of PP&E have different useful lives, they are accounted for separately so that depletion and depreciation rates appropriately reflect useful lives.

Gains and losses on disposal of PP&E, property swaps and farm-outs, including oil and natural gas interests, are determined by comparing the proceeds from disposal of fair value of the asset received or given up, with the carrying amount of the PP&E sold, and are recognized on a net basis in profit or loss.

For the purposes of impairment testing, assets are grouped into the smallest group of assets that generate independent cash inflows from continuing use that are largely independent of the cash inflows of other assets or groups of assets. These groups of assets are called cash generating units ("CGU's").

Impairment testing of PP&E is performed as facts and circumstances suggest by comparing the carrying amount of each CGU to each CGU's recoverable amount. The recoverable amount of a CGU is the greater of (i) its value in use, and (ii) its fair value less selling costs. In assessing value in use for D&P assets, the estimated future cash flows from the production of proven and probable reserves are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. Value in use is generally computed by reference to the present value of the future cash flows expected to be derived from proved and probable reserves.

Impairment losses recognized in prior periods are assessed at each reporting date to evaluate if those losses have decreased or no longer exist. If those impairment losses have decreased or no longer exist (recovered), they are reversed accordingly. Previously recognized impairment losses may be recovered in future reporting periods due to changes in estimates used to determine the recoverable amount. An impairment loss recovery is recorded only to the extent that the PP&E carrying amount does not exceed the carrying amount that would have been determined, net of depletion and depreciation, if no impairment loss had been recognized. Impairment losses and recoveries are recorded in the statement of income and comprehensive income.

*(continued)*

## FINANCIAL STATEMENTS

### TORC Oil & Gas Ltd.

#### Notes to the Financial Statements

As at and for the years ended December 31, 2013 and December 31, 2012

(in \$000's of Canadian dollars, unless otherwise noted)

#### (ii) Proven and probable reserves

Proven and probable reserves represent the estimated quantities of crude oil, natural gas and natural gas liquids which geological, geophysical and engineering data demonstrate with a specified degree of certainty to be recoverable in future years from known reservoirs and which are considered commercially producible. There should be a 50 percent statistical probability that the actual quantity of recoverable reserves will be more than the amount estimated as proven and probable and a 50 percent statistical probability that it will be less. At least annually, reserves are evaluated by independent reserve evaluators.

Such reserves may be considered commercially producible if management has the intention of developing and producing them and such intention is based upon:

- a reasonable assessment of the future economics of such production;
- a reasonable expectation that there is a market for all or substantially all the expected oil and natural gas production; and
- evidence that the necessary production, transmission and transportation facilities are available or can be made available.

Where amounts are expressed on a barrel of oil equivalent ("Boe") basis, natural gas volumes have been converted to Boe using a ratio of 6,000 cubic feet of natural gas to one barrel of oil equivalent. This conversion ratio is based upon an energy equivalent conversion method primarily applicable at the burner tip and does not represent value equivalence at the wellhead. Boe figures may be misleading, particularly if used in isolation.

#### (iii) Subsequent costs

Subsequent costs are capital costs incurred to improve an existing D&P asset (such as a well) that is technically feasible and commercially viable. These costs are capitalized as D&P assets only if they increase the future economic benefits of the asset. All other expenditures are expensed in the statement of income and comprehensive income as incurred. These improvement costs include capital costs of further developing proven reserves or enhancing production. The costs of routine maintenance of D&P assets are recognized in the statement of income and comprehensive income as incurred. The carrying value of any replaced or sold component is derecognized.

#### (iv) Depletion and depreciation

The net carrying value of D&P assets is depleted using the unit-of-production method by calculating the ratio of production in the period to the related proven and probable reserves. The carrying value to be depleted includes estimated future development costs necessary to produce proven and probable reserves. Future development costs are estimated by considering the level of development required to produce the proven and probable reserves and are reviewed by independent reserve engineers at least annually.

For Other PP&E, depreciation is recognized in the statement of income and comprehensive income on a straight-line basis over their estimated useful lives. Finance lease assets are depreciated over the shorter of the lease term and their useful lives unless it is reasonably certain that the Company will obtain ownership by the end of the lease term. Depreciation methods, useful lives and residual values are reviewed at each reporting date.

#### (f) Goodwill

The Company records goodwill relating to corporate acquisitions when the purchase price exceeds the fair value of the net identifiable assets and liabilities acquired by the Company. When goodwill is negative, it is recognized immediately in the statement of income and comprehensive income. The goodwill balance is assessed for impairment annually or as events occur that could result in an impairment. Goodwill is measured at cost less accumulated impairment losses.

For the purposes of impairment testing, goodwill is allocated to CGU's that are expected to economically benefit from the business combination from which the goodwill arose. An impairment loss is recognized if the carrying amount of a CGU exceeds its estimated recoverable amount. Impairment losses are recognized in the statement of income and comprehensive income. Impairment losses identified in a CGU are first charged against any goodwill related to that CGU, with any remaining impairment losses charged against E&E or PP&E assets remaining in that CGU. Impairment losses of goodwill cannot be reversed.

*(continued)*

## FINANCIAL STATEMENTS

### TORC Oil & Gas Ltd.

#### Notes to the Financial Statements

As at and for the years ended December 31, 2013 and December 31, 2012

(in \$000's of Canadian dollars, unless otherwise noted)

(g) Leased assets

Leases where the Company assumes substantially all the risks and rewards of ownership are classified as finance leases. Upon initial recognition the leased asset is measured at an amount equal to the lower of its fair value and the present value of minimum lease payments. Subsequent to initial recognition, the asset is accounted for in accordance with the accounting policy applicable to that asset.

Minimum lease payments made under finance leases are apportioned between the finance expenses and the reduction of the outstanding liability. The finance expenses are allocated to each year during the lease term so as to produce a constant periodic rate of interest on the remaining balance of the liability.

Other leases are operating leases, which are not recognized on the Company's statement of financial position.

Payments made under operating leases are recognized in the statement of income and comprehensive income on a straight-line basis over the term of the lease and not recognized as a liability on the Company's statement of financial position. Lease incentives received are recognized as an integral part of the total lease expense, over the term of the lease.

(h) Stock-based compensation

The grant date fair value of stock-based compensation on equity instruments, such as stock options, incentive shares and restricted and performance awards granted to employees, is recognized as stock-based compensation expense, with a corresponding increase in contributed surplus over the vesting period. A forfeiture rate is estimated at the grant date and is adjusted to reflect the actual number of stock-based compensation equity instruments that vest including adjustments for performance conditions. The inputs used in the calculation of the fair value of stock-based compensation are estimated on the grant date.

(i) Flow-through shares

The Company may finance a portion of its exploration activities through the issuance of flow-through common shares. Under the terms of the flow-through share agreements, the resource expenditure deductions for income tax purposes are renounced to investors in accordance with the appropriate income tax legislation.

The proceeds from the sale of flow-through shares are allocated between the offering of shares and the sale of tax benefits. The allocation is made based on the difference between the fair market price of the existing shares and the amount the investor pays for the flow-through shares (given no other differences between the securities). A flow-through share liability is recognized for this difference. On a pro-rata basis, the previously recorded flow-through share liability is reversed and a corresponding deferred tax liability (equal to the Company's effective tax rate multiplied by the flow-through commitment) is recognized as qualifying expenditures are incurred. Any difference between the reversal of the flow-through share liability and corresponding deferred tax liability is recognized as deferred tax expense in the statement of income and comprehensive income.

(j) Provisions

A provision is recognized if, as a result of a past event, the Company has a present legal or constructive obligation that can be estimated reliably, and it is probable that an outflow of economic benefits will be required to settle the obligation. Provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the liability. Provisions are not recognized for future operating losses.

*(continued)*



## FINANCIAL STATEMENTS

### TORC Oil & Gas Ltd.

#### Notes to the Financial Statements

As at and for the years ended December 31, 2013 and December 31, 2012

(in \$000's of Canadian dollars, unless otherwise noted)

Examples of provisions include dismantling, decommissioning and site disturbance remediation activities, and anticipated losses from lawsuits. Provision is made for the estimated cost of these activities and capitalized in the relevant asset category or expensed in the statement of income and comprehensive income.

#### Decommissioning obligations

Decommissioning obligations (also called asset retirement obligations) are measured at the present value of management's best estimate of expenditure required to settle the present obligation at the statement of financial position date. Subsequent to initial measurement, the obligation is adjusted at the end of each reporting period to reflect the passage of time and changes in the estimated future cash flows underlying the obligation. The increase in the provision due to the passage of time, known as accretion, is recognized in the statement of income and comprehensive income as finance costs whereas increases/decreases due to changes in the estimated future cash flows are capitalized. Actual costs incurred upon settlement of the decommissioning obligations are charged against the provision to the extent the provision was established.

#### (k) Revenue

Revenue from the sale of oil and natural gas is recorded when the significant risks and rewards of ownership of the product are transferred to the buyer which is usually when legal title passes to the external party. This is generally at the time product enters a third party pipeline or facility. Revenue is measured net of discounts, customs duties and royalties. With respect to the latter, the entity is acting as a collection agent on behalf of others.

Tariffs and tolls charged to other entities for use of pipelines and facilities owned by the Company are recognized as revenue as they accrue in accordance with the terms of the service or tariff and tolling agreements.

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

#### (l) Finance income and costs

Finance costs comprise of interest expense on bank debt, accretion of the discount on decommissioning obligations, and impairment losses recognized on financial assets.

Interest income is recognized as it accrues in the statement of income and comprehensive income, using the effective interest method.

#### (m) Income tax

Income tax expense comprises current and deferred tax. Income tax expense is recognized in the statement of income and comprehensive income except to the extent that it relates to items recognized directly in equity, such as share issue costs, in which case it is recognized in equity.

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

Deferred tax is recognized using the balance sheet method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is not recognized on the initial recognition of assets or liabilities in a transaction that is not a business combination. Deferred tax is measured at the tax rates that are expected to be applied to temporary differences when they reverse, based on the laws that have been enacted or substantively enacted at the reporting date. Deferred tax assets and liabilities are offset if there is a legally enforceable right to offset, and they relate to income taxes levied by the same tax authority on the same taxable entity, or on different tax entities, but they intend to settle current tax liabilities and assets on a net basis or their tax assets and liabilities will be realized simultaneously.

A deferred tax asset is recognized to the extent that it is probable that future taxable profits will be available against which the temporary difference can be utilized. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realized.

*(continued)*

## FINANCIAL STATEMENTS

### TORC Oil & Gas Ltd.

#### Notes to the Financial Statements

As at and for the years ended December 31, 2013 and December 31, 2012

(in \$000's of Canadian dollars, unless otherwise noted)

(n) Earnings per share

Basic earnings per share is calculated by dividing the net income or loss attributable to common shareholders of the Company by the weighted average number of common shares outstanding during the period. Diluted earnings per share is determined by adjusting the net income or loss attributable to common shareholders and the weighted average number of common shares outstanding for the effects of dilutive instruments such as options, incentive shares, and restricted and performance awards granted to employees.

#### 4. Determination of fair values

A number of the Company's accounting policies and disclosures require the determination of fair value for both financial and non-financial assets and liabilities. Fair values have been determined for measurement and/or disclosure purposes based on the following methods. When applicable, further information about the assumptions made in determining fair values is disclosed in the notes specific to that asset or liability.

The Company classifies the fair value of financial instruments according to the following hierarchy based on the amount of observable inputs used to value the instruments:

- Level 1: Values based on unadjusted quoted prices in active markets that are accessible at the measurement date for identical assets or liabilities.
- Level 2: Values based on quoted prices in markets that are not active or model inputs that are observable either directly or indirectly for substantially the full term of the asset or liability.
- Level 3: Values based on prices or valuation techniques that require inputs that are both unobservable and significant to the overall fair value measurement.

#### Exploration and evaluation assets, and property, plant and equipment

The fair value of exploration and evaluation assets and property, plant and equipment recognized in a business combination, is based on market value. The market value of E&E assets and PP&E is the estimated amount for which E&E assets and PP&E could be exchanged on the acquisition date between a willing buyer and a willing seller in an arm's length transaction after proper marketing wherein the parties had each acted knowledgeably, prudently and without compulsion. The market value of oil and natural gas interests included in E&E assets and PP&E is estimated with reference to the discounted cash flows expected to be derived from oil and natural gas production based on internally and externally prepared reserve reports. The risk-adjusted discount rate is specific to the asset with reference to general market conditions.

#### Cash and cash equivalents, bank overdrafts, trade and other receivables, trade and other payables, dividends payable and bank debt

The fair value of cash and cash equivalents, bank overdrafts, trade and other receivables, trade and other payables, dividends payable and bank debt is estimated as the present value of future cash flows, discounted at the market rate of interest at the reporting date. As at December 31, 2013 and 2012, the fair value of cash and cash equivalents, trade and other receivables, trade and other payables and dividends payable approximated their carrying value due to their short term to maturity. The fair value of bank debt approximates its carrying value as it bears a floating rate of interest and the margin charged by the lenders are indicative of current credit spreads.

#### Derivatives

The fair value of financial forward contracts and swaps is determined by discounting the difference between the contracted prices and published forward price curves as at the statement of financial position date, using the remaining contracted oil and natural gas volumes and a risk-free interest rate. The fair value of costless collars is based on option models that use published information with respect to volatility, prices and interest rates. The Company classifies its derivatives as Level 2. Level 2 values are based on quoted prices in markets that are not active or model inputs that are observable either directly or indirectly for substantially the full term of the asset or liability.

(continued)

## FINANCIAL STATEMENTS

### TORC Oil & Gas Ltd.

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#### Stock-based compensation

The fair value of employee stock options is measured using a Black-Scholes option pricing model. Measurement inputs include share price on measurement date, exercise price of the option, expected volatility, weighted average expected life of the instruments (based on historical experience and general option holder behaviour), expected dividends, forfeiture rate and the risk-free interest rate (based on government bonds). Incentive shares and restricted and performance awards are fair valued based on the share price on the measurement date with a forfeiture rate applied.

### 5. Financial risk management

#### (a) Overview

The Company's activities expose it to a variety of financial risks such as credit risk, liquidity risk and market risk that arise as a result of its exploration, development, production and financing activities.

This note presents information about the Company's exposure to each of the above risks, the Company's objectives, policies and processes for measuring and managing risk and the Company's management of capital. Further quantitative disclosures are included throughout these financial statements.

The Board of Directors oversees management's establishment and execution of the Company's risk management framework. Management has implemented and monitors compliance with risk management policies. The Company's risk management policies are established to identify and analyze the risks faced by the Company, to set appropriate risk limits and controls and to monitor risks and market conditions.

#### (b) Credit risk

Credit risk is the risk of financial loss to the Company if a customer or counterparty to a financial instrument fails to meet its contractual obligations.

The carrying amount of the Company's cash and cash equivalents, trade and other receivables, and financial derivative contract assets represents the maximum credit exposure.

With respect to trade and other receivables, the Company's exposure to credit risk is influenced mainly by the individual characteristics of each customer.

Receivables from petroleum and natural gas marketers are collected on the 25th day of each month following production. The Company's policy to mitigate credit risk associated with these balances is to establish relationships with credit-worthy marketers, as well as to carefully assess the extent of credit granted to these parties.

Joint venture receivables are normally collected within one to three months of the joint venture bill being issued to the partner. The Company attempts to mitigate the risk from joint venture receivables by obtaining partner approval of capital expenditures prior to expenditure. However, the receivables are from participants in the petroleum and natural gas sector and collection of the outstanding balances is dependent on industry factors such as commodity price fluctuations, escalating costs and the risk of unsuccessful drilling. Further risks exist with joint venture partners as disagreements occasionally arise, increasing the risk of non-collection.

The Company does not typically obtain collateral from petroleum and natural gas marketers or joint venture partners. However, the Company does have the ability to withhold production from joint venture partners in the event of non-payment, as well as requiring prepayment (cash calls) for significant expenditures.

The Company does not anticipate any default as it transacts with credit-worthy customers and management does not expect any losses from non-performance by these customers. As such, a provision for doubtful accounts has not been recorded at December 31, 2013 and 2012.

*(continued)*

## FINANCIAL STATEMENTS

### TORC Oil & Gas Ltd.

#### Notes to the Financial Statements

As at and for the years ended December 31, 2013 and December 31, 2012

(in \$000's of Canadian dollars, unless otherwise noted)

The maximum exposure to credit risk for trade and other receivables at the reporting date by type of customer was:

	December 31, 2013	December 31, 2012
Petroleum and natural gas marketing companies	\$ 23,874	\$ 6,805
Joint venture partners	9,913	11,244
Other parties <sup>(1)</sup>	432	760
Bank <sup>(2)</sup>	199	287
<b>Total trade and other receivables</b>	<b>\$ 34,418</b>	<b>\$ 19,096</b>

<sup>(1)</sup> Other parties is comprised of goods and services tax ("GST") receivable from the federal government.

<sup>(2)</sup> Bank is comprised of commodity derivative contract settlements receivable from certain members of the Company's bank syndicate.

As at December 31, 2013, the Company's trade and other receivables are aged as follows:

	December 31, 2013	December 31, 2012
Current (less than 90 days)	\$ 34,013	\$ 18,114
Past due (greater than 90 days)	405	982
<b>Total</b>	<b>\$ 34,418</b>	<b>\$ 19,096</b>

#### (c) Liquidity risk

Liquidity risk relates to the risk that the Company will encounter difficulty in meeting its obligations associated with financial liabilities. The financial liabilities on the statement of financial position consist of trade and other payables, dividends payable and bank debt. Trade and other payables and dividends payable are considered due within one year. The terms for bank debt are outlined in note 20. The Company anticipates it will continue to have adequate liquidity to fund its financial liabilities. The Company has had no defaults or breaches on its financial liabilities.

#### (d) Market risk

Market risk is the risk that changes in market prices relating to currency, commodity prices and interest rates will affect the Company's net earnings, future cash flows, the value of financial instruments, or the fair value of its assets and liabilities. The objective of market risk management is to manage and control market risk exposure within acceptable parameters.

Although the Company generally does not sell or transact in foreign currency, the United States dollar influences the price of petroleum and natural gas sold in Canada. Furthermore, exchange rate fluctuations can affect the fair value and cash flow from derivative contracts. For the years ended December 31, 2013 and 2012, the Company did not enter into any foreign currency derivative contracts.

Commodity prices for crude oil, natural gas liquids and natural gas are also impacted by political events, meteorological conditions and changes in supply and demand. The Company may enter into commodity derivative contracts that provide downside price protection in order to provide some stability of cash flows for capital spending and planning purposes. The Company's risk management activities are conducted pursuant to its risk management policies approved by the Board of Directors.

Interest rate risk is the risk that future cash flows will fluctuate as a result of changes in interest rates. The Company's interest rate risk arises from its floating rate credit facility. For the years ended December 31, 2013 and 2012, the Company did not enter into any interest rate derivative contracts. Assuming all other variables remain constant, an increase or decrease of one percent in market interest rates in the year ended December 31, 2013 would have decreased or increased shareholders' equity and net income by \$0.1 million.

*(continued)*

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### TORC Oil & Gas Ltd.

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(e) Capital management

The Company's policy is to maintain a strong capital base in order to maintain financial flexibility and to sustain the future development of the business. The Company manages its capital structure and makes adjustments relative to changes in economic conditions and the Company's risk profile. In order to maintain the capital structure, the Company may from time to time issue shares and adjust its capital spending to manage current and projected debt levels. The Company considers its capital structure to include working capital, bank debt and shareholders' equity.

The same as in the prior year, in order to optimize capital and operating efficiency, the Company monitors its net debt. Net debt is calculated as current assets (excluding financial derivative assets) less current liabilities (excluding financial derivative liabilities), bank debt and non-current deferred lease incentives. In times of net debt, the Company monitors debt levels based on a ratio of net debt to annualized funds flow from operations. The Company defines funds flow from operations as cash flow from operating activities prior to changes in non-cash working capital and settlement of decommissioning obligations.

#### 6. Southeast Saskatchewan asset acquisition

On September 9, 2013, the Company closed an acquisition of assets (the "Acquired Assets") located in southeast Saskatchewan (the "SE Saskatchewan Acquisition").

The Company believes the low decline, high netback, light oil producing characteristics of the Acquired Assets are complementary to TORC's light oil focused strategy.

Transaction costs incurred by the Company totaling \$7.0 million related to the SE Saskatchewan Acquisition were expensed in the statement of loss and comprehensive loss.

The SE Saskatchewan Acquisition has been accounted for using the acquisition method of accounting, with the results of the Acquired Assets' operations included in the Company's financial and operating results beginning September 9, 2013.

Consideration paid <sup>(1)</sup>	\$	493,889
Net assets acquired, at estimated fair value		
Property, plant and equipment	\$	571,910
Working capital		1,029
Derivative contracts		(1,559)
Decommissioning obligations		(77,491)
	\$	493,889

<sup>(1)</sup> Consideration paid includes \$488.9 million of cash paid and an additional \$5.0 million of expected purchase price adjustments.

The above amounts are estimates, which were made by management at the time of the preparation of these financial statements based on information then available. Amendments may be made to these amounts as values subject to estimate are finalized.

The fair value of property, plant and equipment has been determined with reference to an independent reserve report with consideration also given for land and seismic values that have been included based on estimated market value.

(continued)

## FINANCIAL STATEMENTS

### TORC Oil & Gas Ltd.

#### Notes to the Financial Statements

As at and for the years ended December 31, 2013 and December 31, 2012

(in \$000's of Canadian dollars, unless otherwise noted)

Included in the statement of loss and comprehensive loss for the year ended December 31, 2013 are the following amounts relating to the Acquired Assets from September 9, 2013 to December 31, 2013:

Petroleum and natural gas sales	\$	52,938
Net income and comprehensive income	\$	31,795

If the SE Saskatchewan Acquisition had occurred on January 1, 2013, the Company's pro forma results of petroleum and natural gas sales and net income and comprehensive income for the year ended December 31, 2013 would have been as follows:

Year ended December 31, 2013	Acquired Assets		(Unaudited)
	As stated	Jan 1 to Sep 8, 2013	
Petroleum and natural gas sales	\$ 164,074	\$ 121,140	\$ 285,214
Net income and comprehensive income	\$ (10,084)	\$ 34,763	\$ 24,679

#### 7. Corporate acquisition

On September 13, 2012, TORC and Vero Energy Inc. ("Vero") jointly announced that they had entered into a plan of arrangement (the "Arrangement") under the Business Corporation's Act (Alberta) to form a new light oil focused company. Under the terms of the Arrangement, each previous TORC (hereinafter "Old TORC") shareholder received 0.87 shares of TORC for each share of Old TORC held and each Vero shareholder exchanged their shares for one share of TORC for each share of Vero held. The Arrangement closed on November 19, 2012. Total consideration paid was \$119.1 million through the issuance of 9,798,496 common shares valued at \$12.15 per share based on Vero's trading price on November 19, 2012, the date the Arrangement closed.

Transaction costs incurred by the Company totaling \$3.8 million related to this Arrangement were expensed in the statement of loss and comprehensive loss.

This Arrangement complemented TORC's existing petroleum and natural gas assets, provided a solid base of lower risk development opportunities, and accelerated TORC's production growth phase.

The Old TORC shareholders held 75% of the outstanding shares of the new combined entity at the time the Arrangement closed. As well, the management team and board of directors of Old TORC continued their roles into TORC. Accordingly, the transaction is accounted for as a reverse takeover whereby Old TORC is deemed to be the acquirer of Vero, using the acquisition method of accounting, with the results of Vero's operations included in the Company's financial and operating results beginning November 19, 2012.

Consideration paid		
9,798,496 common shares issued	\$	119,052
Net assets acquired, at estimated fair value		
Property, plant and equipment	\$	164,726
Bank debt		(36,085)
Working capital deficiency		(4,004)
Derivative contracts		2,416
Decommissioning obligations		(7,345)
Deferred tax liability		(656)
	\$	119,052

*(continued)*

## FINANCIAL STATEMENTS

### TORC Oil & Gas Ltd.

#### Notes to the Financial Statements

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Included in the statement of loss and comprehensive loss for the year ended December 31, 2012 are the following amounts relating to Vero from November 19, 2012 to December 31, 2012:

Petroleum and natural gas sales	\$	5,713
Net income and comprehensive income	\$	3,343

If the Arrangement had occurred on January 1, 2012, the pro forma results of petroleum and natural gas sales and net loss and comprehensive loss for the two combined entities for the year ended December 31, 2012 would have been as follows:

Year ended December 31, 2012	As stated	Vero Jan 1 to Nov 18, 2012	(Unaudited)
Petroleum and natural gas sales	\$ 32,711	\$ 50,078	\$ 82,789
Net income (loss) and comprehensive income (loss)	\$ (18,767)	3,363	\$ (15,404)

#### 8. Key management personnel compensation

	Year ended Dec 31, 2013	Year ended Dec 31, 2012
Remuneration and short-term benefits	\$ 2,605	\$ 1,640
Stock-based compensation	3,596	2,128
	<b>6,201</b>	3,768
Capitalized portion of total compensation	<b>(3,101)</b>	(2,072)
	<b>\$ 3,100</b>	\$ 1,696

Key management personnel includes the officers and directors of the Company.

Short-term employee benefits and stock-based compensation include both the capitalized and non-capitalized portion of these expenditures. Stock-based compensation reflects amounts amortized during the respective periods.

#### 9. Finance costs (income)

	Year ended Dec 31, 2013	Year ended Dec 31, 2012
Interest expense (income) and financing charges	\$ 1,387	\$ (339)
Accretion on decommissioning obligations	905	59
	<b>\$ 2,292</b>	\$ (280)

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### TORC Oil & Gas Ltd.

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#### 10. Supplemental cash flow information

Changes in non-cash working capital is comprised of:

	Year ended Dec 31, 2013	Year ended Dec 31, 2012
Source/(use) of cash:		
Trade and other receivables	\$ (15,322)	\$ (15,034)
Deposits and prepaid expenses	345	(2,064)
Trade and other payables	40,210	32,304
Deferred lease incentives	(176)	(177)
Non-cash working capital acquired	(3,971)	(4,004)
	<b>\$ 21,086</b>	<b>\$ 11,025</b>
Related to operating activities	\$ (10,489)	\$ (4,783)
Related to investing activities	31,575	15,558
Related to financing activities	-	250
	<b>\$ 21,086</b>	<b>\$ 11,025</b>

The following table summarizes interest and taxes paid/(received):

	Year ended Dec 31, 2013	Year ended Dec 31, 2012
Interest paid/(received)	\$ 1,135	\$ (553)
Taxes paid	-	-
	<b>\$ 1,135</b>	<b>\$ (553)</b>

Cash and cash equivalents at December 31, 2013 and 2012 is cash in bank. There are no short-term investments.

#### 11. Exploration and evaluation assets

Balance at December 31, 2011	\$ 120,708
Property acquisitions	5,496
Property dispositions	(1,721)
Capital expenditures	90,205
Exploration and evaluation assets expensed, previously capitalized	(13,306)
Transferred to property, plant and equipment	(50,271)
Balance at December 31, 2012	\$ 151,111
Property acquisitions	2,097
Property dispositions	(2,666)
Capital expenditures	40,926
Exploration and evaluation assets expensed, previously capitalized	(38,355)
Transferred to property, plant and equipment	(24,020)
<b>Balance at December 31, 2013</b>	<b>\$ 129,093</b>

Exploration and evaluation assets ("E&E assets") consist of the Company's exploration projects, including undeveloped land and development costs which are pending the determination of proven reserves. Property acquisitions and capital expenditures represent the Company's share of costs incurred on E&E assets during the period.

For the year ended December 31, 2013, the Company expensed \$38.4 million (year ended December 31, 2012: \$13.3 million) of exploration and evaluation costs related to projects with a carrying value greater than the current market value estimate.



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### TORC Oil & Gas Ltd.

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#### 12. Property, plant and equipment

Cost:	
Balance at December 31, 2011	\$ 134,619
Property acquisitions	4,289
Capital expenditures	38,279
Corporate acquisition (note 7)	164,726
Change in decommissioning obligations	1,808
Transferred from exploration and evaluation assets	50,271
Balance at December 31, 2012	393,992
Property acquisitions (note 6)	571,910
Capital expenditures	122,820
Change in decommissioning obligations	3,503
Transferred from exploration and evaluation assets	24,020
<b>Balance at December 31, 2013</b>	<b>\$ 1,116,245</b>
Accumulated depletion and depreciation:	
Balance at December 31, 2011	\$ 1,979
Depletion and depreciation for the year	18,373
Balance at December 31, 2012	20,352
Depletion and depreciation for the year	59,901
<b>Balance at December 31, 2013</b>	<b>\$ 80,253</b>
Net amount:	
As at December 31, 2012	\$ 373,640
<b>As at December 31, 2013</b>	<b>\$ 1,035,992</b>

Included in the net amount of property, plant and equipment at December 31, 2013 is office equipment of \$0.3 million, net of accumulated depreciation of \$0.2 million (December 31, 2012: \$0.2 million, net of accumulated depreciation of \$0.1 million).

At December 31, 2013, the Company had \$106.5 million of property, plant and equipment which was excluded from depletion at the time and largely related to undeveloped land (December 31, 2012: \$117.8 million). Estimated future development costs of \$307.4 million were included in the depletion calculation (December 31, 2012: \$199.6 million).

For the year ended December 31, 2013, the Company has capitalized \$4.0 million of general and administrative expenses and \$3.4 million of stock-based compensation, which are directly attributable to the acquisition or exploration activities of the Company (for the year ended December 31, 2012: \$2.2 million and \$1.9 million, respectively).

Based on the facts and circumstances in place at December 31, 2013, there was no impairment of the Company's property, plant and equipment.

#### 13. Gain on disposition of undeveloped land

In October 2013, the Company disposed of certain non-core undeveloped land for cash proceeds of \$5.0 million. The Company's carrying cost of this undeveloped land was nominal.

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#### 14. Decommissioning obligations

	As at December 31, 2013	As at December 31, 2012
Balance, beginning of year	\$ 11,408	\$ 877
Obligations incurred	2,699	1,808
Obligations acquired	77,491	8,762
Obligations settled	(262)	(98)
Change in estimated future cash outflows	804	-
Accretion	905	59
<b>Balance, end of year</b>	<b>\$ 93,045</b>	<b>\$ 11,408</b>

The total future decommissioning obligations are based on the Company's net ownership in wells and facilities, estimated costs to reclaim and abandon the wells and facilities, and the estimated timing of the costs to be incurred in future periods. The Company has estimated an undiscounted total future liability of \$118.4 million as at December 31, 2013 (at December 31, 2012: \$15.3 million) to be incurred over an average of the next 25 years. For the period ended December 31, 2013, the Company's risk-free rate of 2.85 percent and an inflation rate of 1.8 percent per annum were used to calculate the net present value of the decommissioning obligations (year ended December 31, 2012: risk-free rate of 2.4 percent and inflation rate of 2.0 percent per annum). Actual costs may differ from estimated costs due to changes in laws and regulations, timing of costs, changes in technology and market conditions.

In 2013, the Company recorded a change in estimated future cash outflows totaling \$0.8 million relating to a change in the Company's well abandonment and reclamation cost estimates. These estimates were revised using management expectations, with reference to industry parameters established by regulatory organizations that estimate regional abandonment and reclamation costs, as well as prevailing economic conditions.

#### 15. Taxes

##### Tax expense (recovery)

The combined provision for taxes in the statement of loss and comprehensive loss reflects an effective tax rate which differs from the expected statutory rate. The reasons for the difference are as follows:

	Year ended Dec 31, 2013	Year ended Dec 31, 2012
Loss before taxes	\$ (8,207)	\$ (21,022)
Statutory income tax rate	25.3%	25.0%
Expected income tax (recovery)	(2,078)	(5,256)
Add (deduct):		
Non-deductible stock-based compensation	859	449
Flow-through share liability	2,878	2,539
Permanent depletion	132	-
Rate adjustments	86	-
Other non-deductible items	-	13
<b>Deferred income tax (recovery)</b>	<b>\$ 1,877</b>	<b>\$ (2,255)</b>

As a result of the Company's new operations in the province of Saskatchewan (in connection with the SE Saskatchewan Acquisition), the corporate Provincial statutory income tax rate increased slightly in 2013, such that the combined Federal and Provincial statutory income tax rate increased from 25.0% in 2012 to 25.3% in 2013.

*(continued)*

## FINANCIAL STATEMENTS

### TORC Oil & Gas Ltd.

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#### Deferred tax liability/(asset)

The components of the deferred tax liability are as follows:

	As at December 31, 2013	As at December 31, 2012
E&E and PP&E	80,494	\$ 39,762
Decommissioning obligations	(23,554)	(2,852)
Loss carryforwards	(44,316)	(29,486)
Financial derivative asset (liability)	(56)	381
Deferred lease incentives	(116)	(158)
Share issue costs	(7,052)	(3,938)
	<b>\$ 5,400</b>	<b>\$ 3,709</b>

The following table summarizes the continuity of the deferred tax liability/(asset):

	As at Dec 31, 2011	Recognized in profit or loss	Recognized in equity	Corporate acquisition (note 7)	Flow-through share premium	As at Dec 31, 2012
E&E and PP&E	\$ 14,112	\$ 11,641	\$ -	\$ 9,052	\$ 4,957	\$ 39,762
Decommissioning obligations	(219)	(797)	-	(1,836)	-	(2,852)
Loss carryforwards	(8,948)	(13,819)	-	(6,719)	-	(29,486)
Financial derivatives	-	(223)	-	604	-	381
Deferred lease incentives	-	(158)	-	-	-	(158)
Share issue costs	(2,987)	1,101	(1,607)	(445)	-	(3,938)
	<b>\$ 1,958</b>	<b>\$ (2,255)</b>	<b>\$ (1,607)</b>	<b>\$ 656</b>	<b>\$ 4,957</b>	<b>\$ 3,709</b>

	As at Dec 31, 2012	Recognized in profit or loss	Recognized in equity	Asset acquisition (note 6)	Flow-through share premium	As at Dec 31, 2013
E&E and PP&E	\$ 39,762	\$ 15,596	\$ -	\$ 20,011	\$ 5,125	\$ 80,494
Decommissioning obligations	(2,852)	(1,086)	-	(19,616)	-	(23,554)
Loss carryforwards	(29,486)	(14,830)	-	-	-	(44,316)
Financial derivatives	381	(42)	-	(395)	-	(56)
Deferred lease incentives	(158)	42	-	-	-	(116)
Share issue costs	(3,938)	2,197	(5,311)	-	-	(7,052)
	<b>\$ 3,709</b>	<b>\$ 1,877</b>	<b>\$ (5,311)</b>	<b>\$ -</b>	<b>\$ 5,125</b>	<b>\$ 5,400</b>

As at December 31, 2013, the Company has tax deductions of approximately \$1.0 billion (2012: \$480 million) available to shelter future taxable income.

	As at December 31, 2013	As at December 31, 2012
CEE	\$ 98,753	\$ 84,330
CDE	151,975	109,931
COGPE	455,824	133,220
UCC	117,916	18,356
Share issue costs	27,859	15,753
Loss carry forwards (expiring between 2026 to 2033)	174,804	117,945
	<b>\$ 1,027,131</b>	<b>\$ 479,535</b>

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### TORC Oil & Gas Ltd.

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#### 16. Share capital

In September 2013, the Company consolidated its outstanding common shares, stock options, incentive shares and warrants on a 1 for 5 basis (the "Share Consolidation"). As a result, the number of outstanding common shares, stock options, incentive shares and warrants of comparative periods have been reduced by a factor of five, in order for the comparative common share, stock options, incentive shares, warrants, per share and per diluted share amounts to be equivalent.

The Company has a significant investor, the CPP Investment Board ("CPPIB"). For so long as CPPIB owns greater than 10% of the outstanding common shares of the Company, it shall have the right to participate in future offerings of securities by the Company, whether by way of public offering or private placement. This includes any offering of common shares and securities convertible or exchangeable into common shares, up to its pro rata ownership interest immediately prior to such offering in the case of a public offering or a private placement to five or more investors, in order to maintain its pro rata percentage ownership interest in the Company, and up to all of the offering in the case of a private placement to less than five investors.

##### Share capital - authorized

At December 31, 2013, the Company was authorized to issue an unlimited number of Class A voting common shares, an unlimited number of Class B non-voting common shares and an unlimited number of preferred shares. The Company has not issued any Class B non-voting common shares nor any preferred shares.

##### Share capital - issued

On November 19, 2012, the Company completed an equity financing by issuing 5,359,200 Common Shares at \$14.94 per Common Share for gross proceeds of \$80.1 million, before share issue costs.

On November 19, 2012, the Company completed an equity financing by issuing 2,246,340 Common Shares on a flow-through basis at \$17.82 per Common Share for gross proceeds of \$40.0 million, before share issue costs.

On November 19, 2012, the Company issued 9,798,496 Common Shares valued at a deemed price of \$12.15 per share as consideration for the Arrangement with Vero.

In August 2013, in connection with the SE Saskatchewan Acquisition described in note 6, the Company completed two equity financings by issuing 52,434,000 subscription receipts at \$7.85 per subscription receipt for gross proceeds of \$411.6 million, before share issue costs. In September 2013, these subscription receipts were converted into common shares of TORC on a one-for-one basis.

##### Warrants

On December 17, 2010, the Company closed a private placement to insiders and service providers whereby 5 million units ("Units") were issued at \$4.00 per Unit, for gross proceeds of \$20.0 million. Each Unit is comprised of 0.52 common shares, 0.17 common shares issued on a flow-through basis and 0.7 common share purchase warrants ("Warrants"). Each Warrant entitles the holder to acquire one common share at a price of \$7.18, subject to the following conditions:

- one-third of the Warrants may be exercised after the Company's stock price (the "Stock Price") exceeds \$11.49;
- one-third of the Warrants may be exercised after the Company's Stock Price exceeds \$14.37;
- one-third of the Warrants may be exercised after the Company's Stock Price exceeds \$17.24; and
- the Stock Price is defined as the weighted average price per share for the 20 consecutive trading days ending immediately before such date on the Toronto Stock Exchange on which the Company's shares are listed.

At December 31, 2013, there were 3.5 million Warrants outstanding of which 1.2 million of the Warrants were exercisable. The Warrants expire on December 17, 2015, which is five years from the date of grant.

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### TORC Oil & Gas Ltd.

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(in \$000's of Canadian dollars, unless otherwise noted)

#### 17. Dividends

In September 2013, the Company's shareholders approved TORC's plan to transition its business model to an intermediate dividend plus growth company. Pursuant to this transition, TORC declared a monthly dividend of \$0.0417 per common share (or \$0.50 per year), paid on October 15, 2013 to shareholders on record at September 30, 2013. On December 10, 2013, TORC announced a dividend increase to \$0.045 per common share (or \$0.54 per year), paid on January 15, 2014 to shareholders on record at December 31, 2013. A total of \$15.5 million (or weighted average of \$0.0426 per common share) was declared between September 30, 2013 and December 31, 2013.

The Company's dividend plan enables common shareholders to elect to receive dividends in common shares rather than cash, calculated at 95% of the weighted average trading price for the five days immediately prior to the payment date (the "Share Dividend Program").

For the period between January 1, 2014 and March 5, 2014, \$8.2 million of dividends (or \$0.09 per common share) were declared, as follows:

- On January 15, 2014, the Company confirmed that a dividend of \$0.045 per Common Share will be paid on February 18, 2014 to common shareholders of record on January 31, 2014. The total amount declared was \$4.1 million, of which \$2.8 million was paid in cash and the remaining \$1.3 million participated in the Company's Share Dividend Program.
- On February 18, 2014, the Company confirmed that a dividend of \$0.045 per Common Share will be paid on March 17, 2014 to common shareholders of record on February 28, 2014. The total amount declared was \$4.1 million, of which \$2.8 million was paid in cash and the remaining \$1.3 million participated in the Company's Share Dividend Program.

#### 18. Stock-based compensation

In September 2013, the Company consolidated its outstanding common shares, stock options, incentive shares and warrants on a 1 for 5 basis (the "Share Consolidation"). As a result, the number of outstanding common shares, stock options, incentive shares and warrants of comparative periods have been reduced by a factor of five, in order for the comparative common share, stock options, incentive shares and warrants to be equivalent.

In September 2013, the Company's shareholders approved an award plan (the "Share Award Plan") whereby restricted awards and performance awards (collectively, "Share Awards") may be granted to the directors, officers and employees of the Company. The maximum number of common shares issuable under the Share Award Plan, combined with the Company's existing stock option and incentive share plans, cannot exceed ten percent of the outstanding Common Shares. In addition, the combined number of restricted and performance awards cannot exceed 6.5 percent of the outstanding Common Shares. Share Awards are earned over various periods, up to three years from the date of grant. Upon being earned, the restricted awards are converted into Common Shares and issued from treasury at no cost to the recipient. The performance awards are converted into Common Shares using a multiplier between zero and two, dependent on the Company's performance on a set criteria as determined by the Board of Directors. In the case of both restricted and performance awards, the number of Common Shares to be issued on the applicable issue date is adjusted to account for the payment of dividends from the grant date to the applicable issue date.

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### TORC Oil & Gas Ltd.

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#### Stock options

Stock options granted have a term of five years to expiry and have various vesting periods up to three years. The following table summarizes the Company's stock option activity:

<i>(thousands, except exercise prices)</i>	Number of stock options	Weighted average exercise price
Balance at December 31, 2011	1,096	\$ 17.60
Granted	495	14.95
Forfeited	(10)	17.25
Balance at December 31, 2012	1,581	\$ 16.75
Granted	119	10.64
Forfeited	(60)	14.56
<b>Balance at December 31, 2013</b>	<b>1,640</b>	<b>\$ 16.38</b>
<b>Exercisable at December 31, 2013</b>	<b>896</b>	<b>\$ 17.09</b>

The following table summarizes stock options outstanding and exercisable at December 31, 2013:

<i>(thousands, unless otherwise noted)</i>	Number outstanding	Number exercisable	Weighted average remaining term (years)
Exercise price:			
\$7.15 to \$9.85	39	-	4.4
\$11.65 to \$13.05	155	37	3.8
\$14.94 to \$22.99	1,446	859	2.6
\$7.15 to \$22.99	1,640	896	2.8

The fair value of each stock option granted was estimated on the date of the grant using the Black-Scholes option pricing model with the following weighted average assumptions:

	Year ended Dec 31, 2013	Year ended Dec 31, 2012
Risk free interest rate	1.4%	1.7%
Expected life (years)	3.0	3.9
Expected volatility (%)	40.0%	40.0%
Forfeiture rate (%)	0.0%	0.0%
Weighted average fair value of stock options	\$3.02	\$4.79

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### TORC Oil & Gas Ltd.

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(in \$000's of Canadian dollars, unless otherwise noted)

#### Incentive shares

The following table summarizes incentive share activity:

<i>(thousands)</i>	Number of incentive shares
Balance at December 31, 2011	157
Granted	73
Forfeited	(1)
Common shares issued upon vesting	(52)
Balance at December 31, 2012	177
Granted	17
Forfeited	(11)
Common shares issued upon vesting	(54)
<b>Balance at December 31, 2013</b>	<b>129</b>
<b>Convertible into Common Shares at December 31, 2013</b>	<b>-</b>

Incentive shares are earned over various periods, up to three years from the date of grant. Upon being earned, the incentive shares are converted into Common Shares and issued from treasury at no cost to the incentive shareholder. The fair value of incentive shares is deemed to equal the stock price on the date of grant. For the year ended December 31, 2013, the weighted average fair value of incentive shares granted was \$10.57 per incentive share (year ended December 31, 2012: \$14.89 per incentive share).

#### Restricted awards

The following table summarizes restricted award activity:

<i>(thousands)</i>	Number of restricted awards
Balance at December 31, 2012	-
Granted	1,249
<b>Balance at December 31, 2013</b>	<b>1,249</b>
<b>Convertible into Common Shares at December 31, 2013</b>	<b>-</b>

Restricted awards are earned over various periods, up to three years from the date of grant. Upon being earned, the restricted awards are converted into Common Shares and issued from treasury at no cost to the restricted award holder. The fair value of restricted awards is deemed to equal the stock price on the date of grant. For the year ended December 31, 2013, the weighted average fair value of restricted awards granted was \$9.27 per restricted award.

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### TORC Oil & Gas Ltd.

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#### Performance awards

The following table summarizes performance award activity:

<i>(thousands)</i>	Number of performance awards
Balance at December 31, 2012	-
Granted	1,818
<b>Balance at December 31, 2013</b>	<b>1,818</b>
<b>Convertible into Common Shares at December 31, 2013</b>	<b>-</b>

Performance awards are earned over various periods, up to three years from the date of grant. Upon being earned, the performance awards are converted into Common Shares and issued from treasury at no cost to the performance award holder. The performance awards are converted into Common Shares using a multiplier between zero and two, dependent on the Company's relative performance on a set criteria as determined by the Board of Directors. The fair value of performance awards is deemed to equal the stock price on the date of grant. For the year ended December 31, 2013, the weighted average fair value of performance awards granted was \$9.26 per performance award. For purposes of the fair value calculation for the year ended December 31, 2013, a multiplier of 1.0 has been assumed.

#### 19. Earnings per share

Earnings per share amounts are calculated by dividing the net loss for the period attributable to common shareholders of the Company by the weighted average number of common shares outstanding during the period.

<i>(thousands, except number of Common Shares and per share amounts)</i>	Year ended Dec 31, 2013	Year ended Dec 31, 2012
Loss for the year	\$ (10,084)	\$ (18,767)
Weighted average number of Common Shares	54,900,265	23,160,504
Basic and diluted loss per Common Share	\$ (0.18)	\$ (0.81)

For the year ended December 31, 2013, the diluted number of shares is equivalent to the basic number of shares due to 1,640,195 stock options, 129,183 incentive shares, 3,480,000 warrants, 1,818,018 performance awards and 1,249,373 restricted awards, all of which are outstanding and antidilutive. Therefore, the diluted per share amounts for net loss are equivalent to the basic per share amounts.

For the year ended December 31, 2012, the diluted number of shares is equivalent to the basic number of shares due to 1,580,803 stock options, 175,940 incentive shares and 3,480,000 warrants, all of which are outstanding and antidilutive. Therefore, the diluted per share amounts for net loss are equivalent to the basic per share amounts.



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### TORC Oil & Gas Ltd.

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#### 20. Credit facility

The Company has a reserves-based revolving credit facility of \$350 million with a syndicate of banks. The credit facility provides that advances may be made by way of direct advances, bankers' acceptances, or standby letters of credit/guarantees. Direct advances bear interest at the agent bank's prime lending rate plus an applicable margin for Canadian dollar advances and at the agent bank's U.S. base rate plus an applicable margin for U.S. dollar advances. The applicable margin charged by the banks is dependent on the Company's debt to trailing cash flow ratio. The bankers' acceptances bear interest at the applicable bankers' acceptance rate plus a stamping fee, based on the Company's debt to trailing cash flow ratio.

The credit facility is secured by a fixed and floating charge debenture on the assets of the Company. The credit facility is available on a revolving basis until April 29, 2014. On or before April 29, 2014, at the request of the Company and subject to the approval of the bank syndicate, the credit facility may be extended for an additional 364 day period. In the event of non-extension, the undrawn portion of the credit facility will be cancelled and the amount outstanding will convert to a 364 day non-revolving term facility with repayment due on April 29, 2015. The borrowing base is primarily based on reserves and commodity prices estimated by the lenders. In the normal course, the Company's next semi-annual credit facility evaluation is due to be completed by April 29, 2014.

#### 21. Financial derivatives

The following table presents a reconciliation of the change in the unrealized amounts for the year ended December 31, 2013:

	Fair value
Balance at December 31, 2011	\$ -
Additions (note 7)	2,416
Unrealized loss on financial derivatives	(890)
Balance at December 31, 2012	\$ 1,526
Additions (note 6)	(1,559)
Unrealized loss on financial derivatives	(187)
Balance at December 31, 2013	\$ (220)

Commodity contracts outstanding as at December 31, 2013:

Remaining term	Reference	Type	Volume (Bbl/d)	Price (per Bbl in Canadian dollars)	Fair value at Dec 31, 2013 (\$000s)
Jan 1, 2014 - Jun 30, 2014	C\$WTI	Costless Collar	500	\$100.00 - \$107.00	-
Jan 1, 2014 - Jun 30, 2014	C\$WTI	Costless Collar	500	\$95.00 - \$109.30	(11)
Jan 1, 2014 - Jun 30, 2014	C\$WTI	Oil Swap	500	\$103.75	(36)
Jan 1, 2014 - Jun 30, 2014	C\$WTI	Costless Collar	1,000	\$90.00 - \$107.00	(204)
Jan 1, 2014 - Dec 31, 2014	C\$WTI	Costless Collar	500	\$95.00 - \$104.60	(135)
Jan 1, 2014 - Dec 31, 2014	C\$WTI	Costless Collar	250	\$90.00 - \$107.25	(46)
Jan 1, 2014 - Dec 31, 2014	C\$WTI	Costless Collar	250	\$90.00 - \$107.55	(37)
Jan 1, 2014 - Dec 31, 2014	C\$WTI	Costless Collar	500	\$95.00 - \$108.50	117
Jan 1, 2014 - Dec 31, 2014	C\$WTI	Costless Collar	250	\$95.00 - \$105.00	47
Jan 1, 2014 - Dec 31, 2014	C\$WTI	Costless Collar	250	\$95.00 - \$106.00	(19)
Jul 1, 2014 - Dec 31, 2014	C\$WTI	Costless Collar	250	\$90.00 - \$104.03	64
Jul 1, 2014 - Dec 31, 2014	C\$WTI	Costless Collar	500	\$95.00 - \$105.00	40
					\$ (220)

As at December 31, 2013, a 10% decrease in the market price detailed in the commodity contracts above would result in a \$6.2 million increase in income.

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#### 22. Commitments

##### Flow-through shares issued in November 2012

In November 2012, the Company issued 2,246,340 flow-through shares at a price of \$17.82 per share for gross proceeds of \$40.0 million. As a result, the Company had to incur qualifying resource expenditures amounting to \$40.0 million before December 31, 2013. The qualifying expenditures were renounced to shareholders as at December 31, 2012. As at December 31, 2013, the Company had spent the necessary qualifying resource expenditures and there is no further obligation remaining for this flow-through share issue.

A flow-through share liability of \$6.5 million was recorded to reflect the opening fair value of the liability associated with these flow-through shares at that date. This flow-through share liability was reduced on a pro-rata basis as the Company incurred qualifying expenditures. Since the Company had spent the necessary qualifying resource expenditures as at December 31, 2013, there is no remaining flow-through share liability.

##### Farm-in transactions

The Company has entered into a number of farm-in agreements with third parties to earn interests in additional prospective acreage. At December 31, 2013, the Company's required future commitments are estimated to be \$4.6 million, which form part of the Company's on-going capital program.

##### Operating lease commitment

###### (a) Deferred lease incentives

The Company has entered into a lease commitment for office space. The term of the lease is 64 months commencing April 1, 2011, totaling \$5.8 million. Under the terms of the lease, the period from April 1, 2011 until December 31, 2011 did not require any payments. However, the total expenditure will be amortized over the full term. This resulted in a liability being recorded and accumulated during the rent free period, which will then reverse and be amortized to income over the remaining term of the office space lease when payments are made. The short-term and long-term components of the deferred rent expense liability represent those portions of the accumulated liability that will be amortized within 12 months and beyond that, respectively.

###### (b) Future lease payments

Future minimum lease payments for the Company's office space as at December 31, 2013 are as follows:

2014	\$	1,257
2015		1,257
2016		733
	\$	3,247

#### 23. Subsequent events

Subsequent to December 31, 2013, the Company entered into the following commodity contracts:

Term	Type	Volume (Bbl/d)	Price (per Bbl in Canadian dollars)	Reference
Feb 1, 2014 - Jun 30, 2015	Costless Collar	500	\$95.00 - \$106.25	C\$WTI
Jul 1, 2014 - Dec 31, 2014	Costless Collar	500	\$95.00 - \$105.00	C\$WTI
Jan 1, 2015 - Jun 30, 2015	Costless Collar	250	\$90.00 - \$108.00	C\$WTI
Jan 1, 2015 - Jun 30, 2015	Costless Collar	250	\$90.00 - \$109.55	C\$WTI