

Condensed Consolidated Interim Statements of Financial Position

Stated in thousand of dollars

(Unaudited)

As at	March 31, 2014	December 31, 2013
Assets		
Current Assets		
Accounts receivable	\$ 51,022	\$ 36,036
Prepaid expenses and deposits	3,939	3,258
	54,961	39,294
Investment (note 10)	51,057	—
Exploration and evaluation assets (note 4)	24,836	25,149
Petroleum and natural gas properties (note 5)	1,481,266	1,312,282
	\$ 1,612,120	\$ 1,376,725
Liabilities		
Current liabilities		
Accounts payable and accrued liabilities	\$ 96,219	\$ 57,808
Dividends payable	8,078	7,216
Fair value of financial contracts (note 6)	22,918	12,604
Current portion of other long term obligations	2,279	1,915
	129,494	79,543
Fair value of financial contracts (note 6)	3,129	982
Bank debt (note 7)	358,465	279,619
Decommissioning obligations (note 8)	120,720	85,172
Other long term obligations	4,030	4,303
Deferred income taxes	74,175	72,912
Shareholders' equity		
Share capital	963,377	884,676
Contributed surplus	28,123	27,123
Warrants	6,689	7,284
Accumulated other comprehensive income	8,463	—
Deficit	(84,545)	(64,889)
	922,107	854,194
Subsequent event (note 11)		
	\$ 1,612,120	\$ 1,376,725

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

Condensed Consolidated Interim Statements of Income (Loss) and Comprehensive Income (Loss)

Stated in thousands of dollars, except per share amounts

(Unaudited)

	Three Months Ended March 31,	
	2014	2013
Revenues		
Petroleum and natural gas	\$ 107,567	\$ 53,582
Royalties	(19,033)	(9,483)
Realized loss on financial contracts	(6,841)	(401)
Unrealized loss on financial contracts (note 6)	(12,461)	(9,317)
	69,232	34,381
Expenses		
Operating	19,410	10,911
Transportation	2,595	1,950
General and administrative	2,902	2,775
Bad debt provision	—	317
Transaction costs (note 3)	433	—
Stock-based compensation (note 9)	1,276	892
Depletion and depreciation (note 5)	34,272	15,752
Finance expense	4,035	2,672
Gain on disposal of petroleum and natural gas properties and farm-outs (note 5)	(270)	(150)
	64,653	35,119
Income (loss) before income taxes	4,579	(738)
Deferred income tax expense	1,157	616
Net income (loss) for the period	\$ 3,422	\$ (1,354)
Other comprehensive income:		
Currency translation adjustment	—	654
Gain on investment (net of tax of \$1.2 million) (note 10)	8,463	—
Other comprehensive income for the period	8,463	654
Total comprehensive income (loss) for the period	\$ 11,885	\$ (700)
Income (loss) per share (note 9)		
Basic	\$ 0.02	\$ (0.02)
Diluted	\$ 0.02	\$ (0.02)

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

Condensed Consolidated Interim Statements of Changes in Shareholders' Equity

Stated in thousands of dollars, except share amounts

(Unaudited)

	Number of common shares	Share capital	Contributed surplus	Performance warrants	Accumulated other comprehensive income (loss)	Deficit	Total equity
Balance at December 31, 2012	71,217,345	\$ 351,957	\$ 20,495	\$ 7,059	\$ (43)	\$ (28,469)	\$ 350,999
Net loss for the period	—	—	—	—	—	(1,354)	(1,354)
Other comprehensive loss	—	—	—	—	654	—	654
Stock-based compensation	—	—	2,200	—	—	—	2,200
Balance at March 31, 2013	71,217,345	\$ 351,957	\$ 22,695	\$ 7,059	\$ 611	\$ (29,823)	\$ 352,499
Balance at December 31, 2013	166,543,309	\$ 884,676	\$ 27,123	\$ 7,284	\$ —	\$ (64,889)	\$ 854,194
Net income for the period	—	—	—	—	—	3,422	3,422
Other comprehensive income	—	—	—	—	8,463	—	8,463
Stock-based compensation	—	—	1,005	—	—	—	1,005
Transfer on exercise of options & warrants	—	600	(5)	(595)	—	—	—
Warrants exercised	172,540	901	—	—	—	—	901
Options exercised	6,666	12	—	—	—	—	12
Issued pursuant to short form prospectus	12,778,800	80,506	—	—	—	—	80,506
Share issue costs, net of tax of \$1.1 million	—	(3,318)	—	—	—	—	(3,318)
Dividends	—	—	—	—	—	(23,078)	(23,078)
Balance at March 31, 2014	179,501,315	\$ 963,377	\$ 28,123	\$ 6,689	\$ 8,463	\$ (84,545)	\$ 922,107

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

Condensed Consolidated Interim Statements of Cash Flows

Stated in thousands of dollars

(Unaudited)

	Three Months Ended March 31,	
	2014	2013
Cash provided by (used in)		
Operating		
Net income (loss)	\$ 3,422	\$ (1,354)
Gain on disposal of petroleum and natural gas properties and farm-outs	(270)	(150)
Unrealized loss on financial contracts	12,461	9,317
Finance expense	4,035	2,672
Interest expense	(3,016)	(2,362)
Depletion and depreciation	34,272	15,752
Decommissioning expenditures	(512)	(463)
Bad debt provision	—	317
Stock-based compensation	1,276	892
Deferred income tax recovery	1,157	616
Change in non-cash working capital	2,789	(250)
Cash flow from operating activities	55,614	24,987
Financing		
Bank debt	78,846	18,351
Dividends paid	(22,216)	—
Issue of common shares, net of issue costs	76,998	—
Cash flow from financing activities	133,628	18,351
Investing		
Petroleum and natural gas properties	(58,351)	(39,917)
Exploration and evaluation assets	—	(148)
Disposition of petroleum and natural gas properties	—	807
Acquisition (note 3)	(108,712)	—
Investment (note 10)	(41,385)	—
Change in non-cash working capital	19,206	(4,080)
Cash flow used in investing activities	(189,242)	(43,338)
Change in cash	—	—
Cash, beginning of the period	—	—
Cash, end of the period	\$ —	\$ —

Cash is defined as cash and cash equivalents.

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

NOTES TO CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS

Tabular amounts are in thousands of dollars, except share and per share data

1. REPORTING ENTITY

Surge Energy Inc.'s (the "Corporation" or "Surge") business consists of the exploration, development and production of oil and gas from properties in western Canada. The Corporation transitioned in the third quarter of 2013 to a dividend paying entity. The condensed consolidated interim financial statements include the accounts of the Corporation, its wholly-owned subsidiaries and partnerships.

2. BASIS OF PREPARATION

Statement of compliance

These condensed consolidated interim financial statements have been prepared in accordance with International Accounting Standard 34, "Interim Financial Reporting" and using the accounting policies outlined by the Corporation in its annual consolidated financial statements for the year ended December 31, 2013, except as identified below. These condensed consolidated interim financial statements do not include all of the information required for full annual financial statements.

On January 1, 2014, the Corporation adopted IFRIC 21 which provides guidance with respect to recognition of liabilities resulting from government levies. The Company also adopted IAS 32 that clarifies the requirements for offsetting financial assets and liabilities. The adoption of these standards had no impact on the amounts recorded in the consolidated financial statements as at March 31, 2014 or on the comparative periods.

The condensed consolidated interim financial statements were authorized for issuance by the Board of Directors on May 12, 2014.

3. ACQUISITION

(a) Southeast Saskatchewan

Effective February 14, 2014 the Corporation acquired certain working interests in developed petroleum and natural gas properties in Southeast Saskatchewan for cash of \$108.7 million from a Canadian oil and gas producer. The purpose of the acquisition was to expand the Corporation's exposure to certain light oil plays. The operations from the acquisition have been included in the results of Surge commencing February 14, 2014.

Surge incurred transaction costs of \$0.4 million on the acquisition which were expensed through the statement of income.

The allocation of the purchase price for the above noted acquisition is as follows:

Fair value of net assets acquired	Total
Petroleum and natural gas properties	\$ 137,559
Decommissioning obligations	(28,847)
Net assets acquired	\$ 108,712
Consideration	
Cash	\$ 108,712
Total consideration	\$ 108,712

For the period ended March 31, 2014	As stated	Southeast Saskatchewan prior to February 14, 2014	Pro Forma
Revenue	\$ 107,567	5,363	\$ 112,930
Income	\$ 3,422	1,303	\$ 4,725

Amounts since acquisition	Southeast Saskatchewan
Revenue	\$ 5,607
Income	\$ 1,362

The fair value of petroleum and natural gas properties recognized on an acquisition is based on market values. The market value of petroleum and natural gas properties is the estimated amount for which petroleum and natural gas properties 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 is estimated with reference to the discounted cash flows expected to be derived from oil and natural gas production based on externally prepared reserve reports which apply forward looking price decks as at the date of acquisition. Undeveloped land is valued using recent, third-party landsale prices in corresponding areas.

The market value of other items of petroleum and natural gas properties is based on the quoted market prices for similar items.

4. EXPLORATION AND EVALUATION ASSETS

Exploration and evaluation (E&E) assets consist of the Corporation's exploration projects which are pending the determination of proven or probable reserves. Additions represent the Corporation's share of costs incurred on E&E assets during the period.

Exploration & Evaluation Assets

	Total
Balance at December 31, 2012	\$ 70,726
Additions	8,051
Disposals	(11,831)
Change in foreign exchange rate	391
Transfer to petroleum and natural gas properties	(42,188)
Balance at December 31, 2013	\$ 25,149
Transfer to petroleum and natural gas properties	(313)
Balance at March 31, 2014	\$ 24,836

5. PETROLEUM AND NATURAL GAS PROPERTIES

Petroleum and Natural Gas Properties

	Total
Balance at December 31, 2012	\$ 803,883
Acquisitions	729,719
Additions	117,495
Transfer from exploration and evaluation assets	42,188
Change in decommissioning obligations	6,357
Capitalized stock-based compensation	3,810
Change in foreign exchange rate	968
Dispositions	(35,524)
Balance at December 31, 2013	\$ 1,668,896
Acquisitions	137,559
Additions - including non-monetary exchange value of \$0.3 million	58,621
Transfer from exploration and evaluation assets	313
Change in decommissioning obligations	6,285
Capitalized stock-based compensation	478
Balance at March 31, 2014	\$ 1,872,152

	Total
Accumulated depletion and depreciation	
Balance at December 31, 2012	\$ (228,400)
Depletion and depreciation expense	(82,410)
Impairment	(51,189)
Dispositions	5,385
Balance at December 31, 2013	\$ (356,614)
Depletion and depreciation expense	(34,272)
Balance at March 31, 2014	\$ (390,886)

	Total
Carrying amounts	
At December 31, 2013	\$ 1,312,282
At March 31, 2014	\$ 1,481,266

The calculation of depletion and depreciation expense for the period ended March 31, 2014 included an estimated \$484.7 million (December 31, 2013 - \$453.6 million) for future development costs associated with proved plus probable reserves and deducted \$111.9 million (December 31, 2013 - \$86.4 million) for the estimated salvage value of production equipment and facilities.

During the period ended March 31, 2014 the Company completed a farm-out agreement. In this non-monetary exchange the Company received a well value of \$0.4 million less a value of \$0.1 million that was given up resulting in a gain on the farm-out of \$0.3 million that has been included in petroleum and natural gas properties.

6. RISK MANAGEMENT

As a means of managing commodity price, interest rate, and foreign exchange volatility, the Corporation enters into various derivative financial instrument agreements and physical contracts. The fair value of 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 (based on published government rates). The fair value of options and costless collars is based on option models that use published information with respect to volatility, prices and interest rates. The fair value of interest rate and foreign exchange contracts 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 notional values. Surge's financial derivative contracts are classified as level two in the fair value hierarchy.

The following table outlines the fair value of foreign exchange contracts as at March 31, 2014:

Remaining Term	Type	Notional (\$USD)	Swap Price (Surge receives) (C\$)	Index (Surge pays) (C\$)	As at March 31, 2014
					Fair Value (\$000s CDN)
Apr 1, 2014 to Dec 31, 2014	Swap	\$25,135,000	\$ 1.005	Floating CAD	\$ (2,614)

The following table outlines the fair value of interest rate contracts as at March 31, 2014:

Remaining Term	Type (floating to fixed)	Amount (C\$)	Company Fixed Interest Rate (%) (1)	Counter party Floating Rate Index	As at March 31, 2014
					Fair Value (\$000s CDN)
Apr 1, 2014 to Dec 31, 2014	Swap	\$50,000,000	3.35%	CAD-BA-CDOR	\$ (1,045)

(1) The interest rate contract is comprised of a range, beginning at 1.439% and escalating quarterly to a maximum of 3.952%.

The following table outlines the fair value of natural gas commodity contracts as at March 31, 2014:

					As at March 31, 2014
Remaining Term	Type (floating to fixed)	Volume	Swap Price (Surge receives) (C\$)	Index (Surge pays) (C\$)	Fair Value (\$000s CDN)
Apr 1, 2014 to Dec 31, 2014	Swap	2,000 gj/d	\$ 3.40	AEEO	(662)
Apr 1, 2014 to Dec 31, 2014	Swap	2,000 gj/d	\$ 3.60	AEEO	(544)
Apr 1, 2014 to Dec 31, 2014	Swap	4,000 gj/d	\$ 3.35	AEEO	(1,388)
Jan 1, 2015 to Dec 31, 2015	Swap	2,000 gj/d	\$ 3.68	AEEO	(220)
Jan 1, 2015 to Dec 31, 2015	Swap	2,000 gj/d	\$ 3.66	AEEO	(231)
Jan 1, 2015 to Dec 31, 2015	Swap	1,000 gj/d	\$ 3.86	AEEO	(44)
Total					\$ (3,089)

The following table outlines the fair value of oil commodity contracts as at March 31, 2014:

					As at March 31, 2014
Remaining Term	Type (floating to fixed)	Volume	Swap Price (Surge receives) (C\$)	Index (Surge pays) (C\$)	Fair Value (\$000s CDN)
Apr 1, 2014 to Jun 30, 2014	Swap	500 bbls/d	\$101.45	WTI - NYMEX	(444)
Apr 1, 2014 to Dec 31, 2015	Swap	250 bbls/d	\$98.15	WTI - NYMEX	(905)
Apr 1, 2014 to Jun 30, 2014	Swap	500 bbls/d	\$100.05	WTI - NYMEX	(508)
Apr 1, 2014 to Jun 30, 2014	Swap	200 bbls/d	\$96.00	WTI - NYMEX	(277)
Apr 1, 2014 to Jun 30, 2014	Swap	250 bbls/d	\$105.80	WTI - NYMEX	(124)
Apr 1, 2014 to Dec 31, 2014	Swap	100 bbls/d	\$98.00	WTI - NYMEX	(286)
Apr 1, 2014 to Dec 31, 2014	Swap	200 bbls/d	\$96.45	WTI - NYMEX	(656)
Apr 1, 2014 to Dec 31, 2014	Swap	150 bbls/d	\$100.10	WTI - NYMEX	(343)
Apr 1, 2014 to Dec 31, 2014	Swap	1,000 bbls/d	\$91.40 (USD)	WTI - NYMEX	(1,925)
Apr 1, 2014 to Dec 31, 2014	Swap	500 bbls/d	\$94.50	WTI - NYMEX	(1,899)
Apr 1, 2014 to Dec 31, 2014	Swap	200 bbls/d	\$95.50	WTI - NYMEX	(707)
Apr 1, 2014 to Dec 31, 2014	Swap	500 bbls/d	\$93.80	WTI - NYMEX	(1,997)
Apr 1, 2014 to Dec 31, 2014	Swap	150 bbls/d	\$95.05	WTI - NYMEX	(550)
Jul 1, 2014 to Dec 31, 2014	Swap	200 bbls/d	\$95.05	WTI - NYMEX	(439)
Jul 1, 2014 to Dec 31, 2014	Swap	500 bbls/d	\$100.24	WTI - NYMEX	(618)
Jul 1, 2014 to Dec 31, 2014	Swap	500 bbls/d	\$95.90	WTI - NYMEX	(1,013)
Jul 1, 2014 to Dec 31, 2014	Swap	100 bbls/d	\$100.40	WTI - NYMEX	(122)
Apr 1, 2014 to Dec 31, 2015	Swap	500 bbls/d	\$22.60 (USD)	WCS Basis	(988)
Jan 1, 2015 to Dec 31, 2015	Swap	250 bbls/d	\$91.55	WTI - NYMEX	(796)
Jan 1, 2015 to Dec 31, 2015	Swap	250 bbls/d	\$92.00	WTI - NYMEX	(755)
Jan 1, 2015 to Dec 31, 2015	Swap	250 bbls/d	\$92.29	WTI - NYMEX	(729)
Jan 1, 2015 to Dec 31, 2015	Swap	1,000 bbls/d	\$93.05	WTI - NYMEX	(2,615)
Apr 1, 2014 to Jun 30, 2014	Swap	1,000 bbls/d	\$8.00 (USD)	MSW Basis	(201)
Apr 1, 2014 to Jun 30, 2014	Swap	500 bbls/d	\$18.50 (USD)	WCS Basis	70
Apr 1, 2014 to Dec 31, 2014	Swap	500 bbls/d	\$8.70 (USD)	MSW Basis	(300)
Apr 1, 2014 to Jun 30, 2014	Swap	1,000 bbls/d	\$7.40 (USD)	MSW Basis	(140)
Apr 1, 2014 to Jun 30, 2015	Swap	375 bbls/d	\$106.00	WTI - NYMEX	13
Apr 1, 2014 to Jun 30, 2015	Swap	375 bbls/d	\$105.65	WTI - NYMEX	(45)
Total					\$ (19,299)

The following table summarizes the sensitivity of the fair value of the Corporation's market risk management positions to fluctuations in interest rates, foreign exchange rates, and natural gas and crude oil prices. All such fluctuations were evaluated independently, with all other variables held constant. In assessing the potential impact of these fluctuations, the Corporation believes that the volatilities presented below are reasonable measures. Fluctuations in interest rates, foreign exchange rates, and crude oil and natural gas prices would have had the following impact on the net earnings:

Net earnings impact for the period ended March 31, 2014		
	Price Increase	Price Decrease
Crude Oil - Change of +/- \$1.00	(2,225)	2,225
Natural Gas - Change of +/- \$0.10	(302)	302
Interest rate - Change of +/- 100 points	375	(375)
Foreign Exchange - Change of +/- \$0.01	(189)	189

7. BANK DEBT

The Corporation at March 31, 2014, has a \$470 million extendible, revolving term credit facility with a syndicate of Canadian banks bearing interest at bank rates. The facility is available on a revolving basis until May 31, 2014. On May 31, 2014, at the Corporation's discretion, the facility is available on a non-revolving basis for a one-year period, at the end of which time the facility would be due and payable. Alternatively, the facilities may be extended for a further 364-day period at the request of the Corporation and subject to the approval of the syndicate. As the available lending limits of the facilities are based on the syndicate's interpretation of the Corporation's reserves and future commodity prices, there can be no assurance that the amount of the available facilities will not decrease at the next scheduled review. Interest rates vary depending on the ratio of net debt to cash flow. The facility had an effective interest rate of prime plus 1.75 percent as at March 31, 2014 (December 31, 2013 – prime plus 1.25 percent).

The facility is secured by a general assignment of book debts, debentures of \$1.0 billion with a floating charge over all assets of the Corporation with a negative pledge and undertaking to provide fixed charges on the major producing petroleum and natural gas properties at the request of the bank. Under the terms of the agreement, the Corporation is required to meet certain financial and engineering reporting requirements.

Under the terms of the agreement, the Corporation must maintain an adjusted working capital ratio of not less than 1.00:1.00 at all times. The working capital ratio is defined under the current credit facility as cash-based current assets, including the undrawn portion of the facility, to cash-based current liabilities, excluding any current bank indebtedness. The Corporation is compliant with this covenant at March 31, 2014.

8. DECOMMISSIONING OBLIGATIONS

The Corporation's decommissioning obligations result from net ownership interests in petroleum and natural gas assets including well sites, gathering systems and processing facilities. The Corporation estimates the total undiscounted amount of cash flows required to settle its decommissioning obligations is approximately \$352.5 million (December 31, 2013 – \$277.7 million). A risk free rate of 2.96 percent (December 31, 2013 – 3.24 percent) and an inflation rate of two percent (December 31, 2013 – two percent) was used to calculate the fair value of the decommissioning obligations.

A reconciliation of the decommissioning obligations is provided below:

	March 31, 2014	December 31, 2013
Balance, beginning of period	\$ 85,172	\$ 39,339
Liabilities related to acquisitions (note 3)	28,847	39,965
Liabilities related to dispositions	—	(1,316)
Change in estimate	5,641	4,855
Liabilities incurred	644	1,502
Accretion expense	928	1,793
Decommissioning expenditures	(512)	(966)
Balance, end of period	\$ 120,720	\$ 85,172

9. SHARE CAPITAL

(a) Authorized

Unlimited number of voting common shares.

Unlimited number of preferred shares, issuable in series.

(b) Short Form Prospectus

In February 2014, the Corporation completed a short form prospectus for 12.8 million common shares for gross proceeds of \$80.5 million.

(c) Stock Options

The Company has granted options to certain officers, directors, employees and consultants under the Corporation's stock option plan. The exercise price of each option equals the market price of the Corporation's common shares at the date of grant. Options granted have a term of five years to maturity and vest as to one-third on each of the first, second and third anniversaries from the date of grant.

	March 31, 2014		December 31, 2013	
	Number of Options	Weighted average exercise price	Number of Options	Weighted average exercise price
Stock options outstanding, beginning of period	249,199	\$ 6.49	6,580,701	\$ 7.53
Granted	—	\$ —	74,500	\$ 4.05
Exercised	(6,666)	\$ 1.75	(251,667)	\$ 5.19
Forfeited	—	\$ —	(1,529,608)	\$ 8.00
Cancelled	—	\$ —	(4,624,727)	\$ 7.50
Stock options outstanding, end of period	242,533	\$ 6.62	249,199	\$ 6.49
Exercisable at year-end	198,300	\$ 7.27	159,632	\$ 7.03

The following table summarizes stock options outstanding and exercisable at March 31, 2014:

Range of exercise prices	Options Outstanding			Options Exercisable	
	Number outstanding	Weighted average exercise price	Weighted average contractual life (years)	Number exercisable	Weighted average exercise price
\$3 to \$4.99	52,500	\$3.43	4.07	2,500	\$3.63
\$5 to \$6.99	103,333	\$6.40	1.10	110,667	\$6.34
\$7 to \$8.99	24,500	\$7.34	3.36	35,667	\$7.39
\$9 to \$11.15	62,200	\$9.39	2.24	49,466	\$9.43
\$1 to \$11.15	242,533	\$6.62	2.27	198,300	\$7.27

(d) Warrants

The Corporation has 919,293 performance warrants outstanding (December 31, 2013 – 1,091,833) that expire on April 13, 2015. As at March 31, 2014, all 919,293 outstanding performance warrants were vested and exercisable at a price of \$5.17. During the period ended March 31, 2014 172,540 performance warrants were exercised (December 31, 2013 - 955,439).

The Corporation has 1,400,560 warrants exercisable at a price of \$4.46. The warrants will become exercisable based on certain time based and performance based conditions. Specifically with respect to time they are exercisable up to one third on each anniversary from the date of the grant, and with respect to performance up to one half when the market price of the Corporation reaches \$6.30 and the other half when it reaches \$8.40. The warrants expire in June 2018. There are no warrants exercisable as at March 31, 2014.

(e) Stock Appreciation Rights

For the period ended March 31, 2014, the Corporation had 2.0 million SAR's outstanding exercisable at a price of \$3.24 per SAR. The SARs vest up to one third on each anniversary from the date of grant and expire in June 2018. The exercise price is downward adjusted for dividends paid. As such the exercise price at March 31, 2014 is \$2.92 (December 31, 2013 - \$3.05). The SARs when exercised are to be cash settled based on the difference between the Corporation's common share price on the date of exercise and the adjusted exercise price. The Corporation has valued the SARs using a Black Scholes valuation model and will continue to revalue at each reporting period until ultimate cash settlement. During the period, the Corporation realized an increase to the liability within accounts payable and an offsetting increase to stock-based compensation of \$0.7 million (2013 - \$3.0 million). There is \$3.7 million included in accounts payable at March 31, 2014 (December 31, 2013 - \$3.0 million).

(f) Restricted and Performance Share Award Incentive Plan

The Corporation has a Stock Incentive Plan which authorizes the Board of Directors to grant restricted share awards ("RSAs") and performance share awards ("PSAs") to directors, officers, employees and certain consultants of Surge.

Subject to the terms and conditions of the plan, each RSA entitles the holder to an award value to be typically paid as to one-third on each of the first, second and third anniversaries from the date of grant. Each PSA entitles the holder to an award value to be typically paid on the third anniversary of the date of grant. For the purpose of calculating share-based compensation, the fair value of each award is determined at the grant date using the closing price of the common shares. An estimated forfeiture rate of 15% was used to value all awards granted for the period ended March 31, 2014. The weighted average fair value of awards granted for the period ended March 31, 2014 is \$6.25 per PSA and \$6.23 per RSA. In the case of PSAs, the award value is adjusted for a payout multiplier which can range from 0.0 to 2.0 and is dependent on the performance of the Corporation relative to pre-defined corporate performance measures for a particular period. On the vesting dates, the Corporation has the option of settling the award value in cash or common shares of the Corporation. For purposes of stock-based compensation a payout multiple of 1.0 was assumed for the PSAs.

The total number of RSA and PSA units granted cannot exceed five percent of the issued and outstanding shares of the Corporation.

All share issuances under the plan are subject to receiving approval of the plan from the Toronto Stock Exchange and the Corporation's shareholders, failing which all entitlements under the plan will be cash settled by the Company.

The number of restricted and performance share awards outstanding are as follows:

	Number of restricted share awards	Number of performance share awards
Balance at January 1, 2013	854,425	908,625
Granted	40,025	9,375
Forfeited	(65,700)	(21,000)
Balance at March 31, 2014	828,750	897,000

(g) **Stock-based compensation**

A reconciliation of the stock-based compensation expense is provided below:

	Period ended March 31,	
	2014	2013
Stock-based compensation on options	\$ 24	\$ 2,200
Stock-based compensation on SARs	749	—
Stock-based compensation on PSAs and RSAs	981	—
Capitalized stock-based compensation	(478)	(1,308)
Total stock-based compensation expense	\$ 1,276	\$ 892

The Corporation's stock-based compensation expense for the period ended March 31, 2014 was \$1.3 million (March 31, 2013 - \$0.9 million).

(h) **Per share amounts**

The following table summarizes the shares used in calculating the income (loss) per share:

	Period ended March 31,	
	2014	2013
Weighted average number of shares - basic	173,069,989	71,217,345
Effect of dilutive stock options	828,174	—
Weighted average number of shares - diluted	173,898,163	71,217,345

In computing diluted per share amounts at March 31, 2014, 190,033 options (March 31, 2013 – 6,522,201), nil performance warrants (March 31, 2013 – 2,047,272), nil warrants (March 31, 2013 – nil), 40,025 RSAs (March 31, 2013 – nil) and 9,375 PSAs (March 31, 2013 – nil) were excluded from the calculation as their effect was anti-dilutive.

(i) **Dividends**

The Board of Directors declared for the months of January through March dividends of \$0.13166 per share. Dividends of \$0.045 per share are declared and outstanding at March 31, 2014 and were paid in April 2014. Dividends for the month of April have also been declared at \$0.045 per share per month.

10. INVESTMENT

On February 28, 2014, the Company acquired 9,300,000 common shares of Longview Oil Corp. ("Longview"), representing 19.8 percent of the outstanding common shares, at a purchase price of \$4.45 per Common Share for a total cost of \$41,385,000.

The investment has been accounted for as available for sale, which results in the investment being fair valued at the end of each reporting period, with any gains or losses recorded in accumulated other comprehensive income. This has resulted in a gain of \$8,463,000 net of tax of \$1,209,000 being recorded in accumulated other comprehensive income for the three months ended March 31, 2014. The investment was fair valued using the closing price of Longview shares on March 31, 2014 of \$5.49 per common share for a total fair value of \$51,057,000. The investment is considered a level 1 financial instrument as quoted market prices are available.

11. SUBSEQUENT EVENTS

(a) Business Combination

On March 31, 2014, Surge announced an arrangement agreement, pursuant to which the Company has agreed to acquire all of the issued and outstanding common shares of Longview Oil Corp. ("Longview") by way of a plan of arrangement transaction.

Pursuant to the arrangement agreement, Surge has agreed to acquire all of the remaining Longview common shares at an exchange ratio of 0.975 of a Surge common share for each Longview common share. As a result, Surge anticipates issuing an additional 38.0 million common shares. The arrangement agreement does contemplate under certain circumstances in the event of a failed transaction that Surge or Longview could owe the other party \$7.7 million in non-completion fees.