November 10, 2016

HAND DELIVERED

TIMOTHY PINOS

Certified as a Specialist
in Civil Litigation

tpinos@casselsbrock.com
tel (416) 869-5784
fax (416) 350-6903

The Honourable Justice A.D. Macleod
Court of Queen's Bench
Calgary Courts Centre
601 - 5 Street S.W.
Calgary Alberta T2P 5P7

Re: Court File No. 1601-12571: In the Matter of the *Companies Creditors Arrangement Act, RSC 1985,* c C-36, as amended and in the matter of a Plan of Compromise or Arrangement of Lightstream Resources Ltd., 1863359 Alberta Ltd, LTS Resources Partnership, 1863360 Alberta Ltd and Bakken Resources Partnership

My Lord:

In advance of the hearing scheduled for November 15 and 16, Mudrick and FrontFour have enclosed *InterOil Corporation v Mulacek*, 2016 YKCA 14. Although the date of the decision is November 4, 2016, the printed reasons were not released until early this week and were not included in our Book of Authorities. We intend to rely on this case at the hearing.

We have also enclosed Lightstream's Second Quarter Results dated August 5, 2015, which we refer to in our factum on page 17, and which we inadvertently omitted from our Record.

We trust that the foregoing is satisfactory but please advise whether further information is needed.

Yours very truly,

Timothy Pinos
TP/SV/gmc

cc: Service list

COURT OF APPEAL OF YUKON

Citation: *InterOil Corporation v. Mulacek*, 2016 YKCA 14

Date: 20161104
Docket: 16-YU795

Between:

InterOil Corporation

Respondent
(Petitioner)

And

Philippe E. Mulacek

Appellant
(Respondent)

And

Exxon Mobil Corporation

Respondent
(Respondent)

Before: The Honourable Madam Justice Newbury
The Honourable Madam Justice Saunders
The Honourable Mr. Justice Groberman

On appeal from: An order of the Supreme Court of Yukon, dated October 7, 2016 (*Re: Interoil Corporation*, 2016 YKSC 54, Whitehorse Registry No. 16-A0082)

Oral Reasons for Judgment

Counsel for the Appellant: W. Berman
M. Hannam
L. Jackson

Counsel for the Respondent, InterOil Corporation: T. Friedland
M. Ouanounou
G.A. Fekete

Counsel for the Respondent, Exxon Mobil Corporation	G. Macdonald, Q.C. D. Tupper M. Dixon M.P. Good
Place and Date of Hearing:	Vancouver, British Columbia October 31, 2016
Place and Date of Judgment:	Vancouver, British Columbia November 4, 2016

Summary:

Appeal from a ruling under s. 195 of Yukon Business Corporations Act that proposed "arrangement" (acquisition of company by share exchange) was fair and reasonable. Appeal allowed. The court below had erred in principle in setting aside various deficiencies in information provided to shareholders, and other 'red flags' as irrelevant to whether the arrangement was fair and reasonable, and instead relied mainly on the fact a majority of shareholders had voted to approve it. Considering the correct factors, court could not be satisfied the arrangement was fair and reasonable.

[1] **NEWBURY J.A.**: By reasons for judgment dated October 7 of this year, a chambers judge of the Yukon Supreme Court granted an application under s. 195 of the *Business Corporations Act*, R.S.Y. 2002, c. 20 for the approval of an "arrangement" (as defined by s. 195(1)(f)) whereby all the shares of InterOil Corporation ("InterOil") would be exchanged for shares of Exxon Mobil Corporation ("Exxon") valued at $45 per share, plus a capped "contingent resource payment" ("CRP"). InterOil is a Yukon corporation the shares of which are traded on the NYSE. Its primary asset is a 36.5% joint venture interest in an oil and gas field ("PRL15" or the Elk-Antelope fields) in Papua New Guinea that is still in the development stage. As counsel noted in this court, the proposed arrangement is "transformational" in that it will require shareholders to surrender their shares and will result in InterOil's becoming a wholly-owned subsidiary of Exxon.

[2] Yukon's Act, which has counterparts in the corporate legislation of most of the provinces of Canada, contemplates in s. 195(9) that the Supreme Court shall hear applications for approval of an arrangement and may in its discretion:

> (a) approve the arrangement as proposed by the applicant or as amended by the Supreme Court; or
>
> (b) refuse to approve the arrangement, and make any further order it thinks fit.

A copy of the order of the Supreme Court approving the arrangement is one of the documents required to be filed with the Registrar, who is then required by s. 195(11) of the Act to issue a certificate giving effect to the arrangement.

[3] In Canada, the leading case dealing with the approval of corporate arrangements is *BCE Inc. v. 1976 Debentureholders*, 2008 SCC 69. As the chambers judge noted, *BCE* formulated three "tests" for approval. The first two – that the statutory requirements and any court-mandated requirements have been complied with, and that the application has been put forward in good faith – were met in this case; the third is that the court be satisfied the proposed arrangement is "fair and reasonable". (This phrase does not appear in the Act but may be traced back at least to the decision of Romer L.J. in *Re Alabama*, *New Orleans, Texas and Pacific Junction Ry. Co*. [1891] 1 Ch. 231 (C.A.).)

[4] The chambers judge ruled that the arrangement in this case was fair and reasonable. His ruling is challenged by the appellant Mr. Mulacek, a founder and former chairman and director of InterOil. He holds a 5.5% interest in the company. He has extensive experience in petroleum and related exploration and development. He dissented from the shareholders' resolution adopting the arrangement, but as the chambers judge stated at the end of his reasons, Mr. Mulacek "failed to persuade the 80%" who voted in favour. If the arrangement proceeds, Mr. Mulacek will be required to surrender his shares in return for their "fair value" as determined in accordance with s. 193 of the Act.

[5] At paras. 6–19 of his reasons, the chambers judge set forth the "background" of Exxon's offer, beginning with the fact that a previous offer had been made by a company called Oil Search in May 2016. In fact, InterOil had been exploring the possible sale of *some* assets, and then a "Whole Company Transaction" since mid-2015. Immediately before the Oil Search offer was announced on May 20, InterOil's shares were trading at $31.65 U.S. per share. InterOil first agreed to enter into an arrangement, also structured as a share exchange, with Oil Search that valued InterOil's equity at about $2.1 billion or $40.25 per share, plus a "Contingent Value Right" ("CVR") tied to the volume of PRL15. As the chambers judge stated:

> The CVR would have delivered a contingent cash payment of approximately $6.044 for each 1 tcfe (1 trillion cubic feet equivalent) of PRL15 2C Resources above 6.2 tcfe without a cap. All figures are in US dollars. (At para. 9.)

[6] This arrangement was to be voted on at a special meeting of securityholders on July 28, but on June 30, Exxon made an unsolicited offer to buy all the shares of InterOil for *$45* per share plus a contingent payment ("CRP") of approximately "$7.07 for each one tcfe of PRL15 2C Resources above 6.2 tcfe, up to a maximum of 10.0 tcfe". (My emphasis.) Exxon paid the "break fee" of $60 million required under the Oil Search agreement so that InterOil could proceed with the Exxon deal.

[7] The chambers judge described the implications of the capped CRP and the financial implications of the deal for InterOil's CEO and directors in the following terms:

> … the Exxon Arrangement provides an additional $5 per Interoil share and an increased CRP relative to the CVR in the Oil Search Arrangement, but capped at 10 tcfe. It is also important to note that certain Restricted Share Units ("RSU") were granted pursuant to Company Incentive Plans. As of August 2016, the directors of Interoil owned an aggregate of 404,302 RSUs representing 51.9% of the issued and outstanding RSUs. The CEO owns 329,825 of these RSUs. It is estimated that the CEO stands to earn approximately $35 million if the Exxon Arrangement proceeds. The RSUs are accelerated, thereby not required to satisfy certain performance metrics normally necessary for the issuance of common shares to the RSU holders. Each director has entered into a Voting Agreement requiring him or her to vote the common shares issued pursuant to the RSUs in favour of the Exxon Arrangement.
>
> If all CRP payments were made up to the cap of 10 tcfe, the value of the Exxon Arrangement is approximately $72 per Interoil share. The Oil Search Arrangement would have provided a similar value at 11.5 tcfe. Interoil indicates it is possible that the CRP could be 0, although Mr. Mulacek would disagree. He expresses the opinion that the CRP could account for up to 37% of the compensation to shareholders under the Exxon Arrangement. I make no finding of fact in that regard. [At paras. 13–14.]

[8] Once it had become clear that Oil Search would not be revising its bid, the Board met with Morgan Stanley (which had already prepared an opinion in respect of the Oil Search bid) and requested that it prepare a fairness opinion for the Exxon arrangement. Morgan Stanley is to receive a fee for providing the opinion, which fee is largely contingent on the arrangement taking place. The amount of the fee has not been disclosed. A general meeting to approve the arrangement was called for September 21, 2016 in New York City.

[9] Management's Information Circular sent to shareholders in connection with the general meeting summarized the Oil Search and Exxon arrangements respectively, and the reasons for the Board's determination that the new proposal was in the best interests of InterOil, and that the consideration to be received by shareholders was fair to them. The chambers judge summarized these reasons at para. 19:

> 1. The Exxon Arrangement valued the equity of Interoil at $45 per share which represents a premium of 42.2% on the closing share price of Interoil on May 19. 2016, without considering the potential value of the CRP.
> 2. It provided Shareholders the ability to participate in the potential upside of the resource volume of the PRL15 Fields. If the CRP is paid, the aggregate consideration for a common share is approximately $72.
> 3. The Exxon shares provide immediate liquidity to those shareholders who wish to sell them.
> 4. The Exxon Arrangement provides certainty of value at $45 per common share.
> 5. Exxon agreed to pay the Oil Search termination fee of $60 million.
> 6. Under the heading "Review of Strategic Alternatives" the Board said that it "considered and actively pursued a wide range of potential strategic alternatives available to Interoil, including the potential shareholder value as assessed by Interoil and its financial advisors that could be expected to be generated by remaining an independent company, as well as potential benefits, risks and uncertainties associated with such alternatives". No details were given.
> 7. Under the heading "Probe of Strategic Alternatives" the Board directed management to contact third parties to gauge their interest in a variety of different transactions involving Interoil and its assets. No details were given.
> 8. The Board also cited the benefits of participation in Exxon shares and their future growth.
> 9. The Board also found support in the Interior Resource Certification ("IRC") for the CRP to ensure that the PLR15 2C Resource Antelope well 7 would be drilled and tested before the IRC. However, this recommendation was tempered by the risk that the CRP payout, if any, will not be known for some time.
> 10. The Board relied on the Fairness Opinion and stated that "it did not constitute a recommendation as to how any Shareholder should

vote" but nevertheless stated "Shareholders are urged to read the Fairness Opinion carefully and in its entirety".

11. The Rights of Dissent were carefully set out.
12. The interests of certain directors and officers were set out in their entirety and specifically the value of the CEO's RSUs at $32,252,855 and his termination payment of $2,646,000.
13. The Circular also set out a variety of risks that could influence the market value of shares and the risk that the $67 million termination fee would discourage other bids.

[10] I note that the Circular informed shareholders resident in the U.S. that under s. 3(a)(10) of the U.S. Securities Act, the exchange of their shares for Exxon shares would be exempt from registration, provided that *inter alia* the terms and conditions of the exchange were approved after a fairness hearing before a court or other competent authority at which all recipients of Exxon shares would be entitled to appear. Accordingly, the final order of the Yukon Court would "constitute a basis for the exemption from the registration requirements of the U.S. Securities Act with respect to the Exxon… shares issued in accordance with the arrangement."

[11] The Circular was accompanied by Morgan Stanley's fairness opinion dated July 21, 2016 addressed to the Board. A copy of that letter will be attached to these reasons. Its contents were summarized by the chambers judge at para. 21 of his reasons. He also noted that the Board had consulted other financial experts in addition to Morgan Stanley, but that none of them had provided opinions on fairness. (At para. 24.)

[12] The special meeting was duly held on September 21, 2016. The statutory voting thresholds required by s. 195 of the Act were met by shareholders, security holders, and shareholders of InterOil other than those required to be excluded under MI 61-101, respectively. Mr. Mulacek and others holding approximately 10% of the common outstanding shares voted against the resolution.

[13] In the court below, Mr. Mulacek submitted that the fairness opinion was seriously deficient. In support, he adduced opinion evidence of Mr. Peter Dey, the chairman of an independent investment dealer and a person qualified as an expert

on corporate governance issues. In addition to his legal practice in the securities area, Mr. Dey was Chair of the Ontario Securities Commission between 1993 and 1995 and author of the *Dey Report on Corporate Governance* prepared for the TSE. He is also a former chairman of Morgan Stanley.

[14] For reasons summarized by the chambers judge at para. 26, Mr. Dey opined that the "process undertaken by this board in considering and recommending the Transaction … was deficient, and failed to meet current governance best practice and to ensure adequate safeguards of shareholder interests." (At para. 27.) He contrasted the fairness opinion of Morgan Stanley with three others with which he was familiar, each of which provided a great deal more information – and one might say, substance – than the opinion in this case.

[15] In addition, Mr. Mulacek filed an affidavit of a Mr. Booth, of the investment banking department of Paradigm Capital, opining as to the adequacy of the consideration to be received by InterOil shareholders. Mr. Booth was found to be an expert in the "valuation of reserves and resource estimates for the oil and gas industry." His report is summarized at para. 30 of the chambers judge's reasons, which I will not recount here, except to note his conclusion that the consideration contemplated by the arrangement was "<u>inadequate, from a financial point of view</u>, to the shareholders of InterOil." (My emphasis.) No contrary opinions were adduced into evidence, directly or indirectly, by InterOil or Exxon.

[16] The chambers judge reviewed the law applicable to corporate arrangements of this kind. He noted *Magna International Inc. (Re)* 2010 ONSC 4123, where the Court had approved an arrangement under which certain "super-voting" shares representing control of the company were bought back at a huge premium in comparison to the value of non-voting shares. The chambers judge observed that the Court in *Magna* had "placed significance on the shareholder vote" and he quoted from the Court's reasons:

> ….the position of the Opposing Shareholders disregards entirely the significance of the shareholder vote from the perspective of the implicit contract among shareholders of a public corporation. <u>It is an</u>

> important principle of corporate democracy that a shareholder is bound by an informed vote of all shareholders. It is relevant that, in acquiring shares in a public corporation, a shareholder must expect that the majority vote will prevail, except in circumstances of oppressive behavior by shareholder groups. Moreover, ratification of actions of directors by a vote of the affected shareholders is a recognized means of addressing controversial transactions. [At para. 38; emphasis added.]

[17] The chambers judge summarized the parties' respective positions at paras. 39–46 and many of those arguments have been advanced before us on this appeal. Under the heading "Analysis", he then proceeded to address two questions – first, whether the board of InterOil had provided "improper corporate governance and deficient disclosure", and second, whether the Exxon arrangement was fair and reasonable.

[18] In connection with the first issue, the judge agreed with Mr. Dey that the process undertaken by the InterOil's board in connection with the Exxon arrangement had demonstrated "deficient corporate governance and inadequate disclosure." In particular, the judge wrote:

> The Fairness Opinion obtained by the Board was deficient and indicative of a failure to discharge its fiduciary obligations in the following ways:
>
> 1. it failed to address the value of the Elk-Antelope asset and the impact of the cap on the CRP so that shareholders could consider whether the Exxon Arrangement reflected that value;
> 2. it failed to disclose the details of Morgan Stanley's success compensation so that shareholders could evaluate whether the Fairness Opinion is influenced by the terms of the compensation;
> 3. it failed to provide the shareholders with an independent financial fairness opinion on a flat fee basis, particularly in the situation where the CEO had a financial incentive for the Exxon Arrangement to proceed.
>
> The Fairness Opinion was also remarkably deficient in the following ways:
>
> 1. it contained no reference to the specific documents that it reviewed;
> 2. it contained no facts or information to indicate what the opinion was based on; and

> 3. it contained no analysis of the facts or information so that a shareholder could fairly consider the merits of the Exxon Arrangement. [At paras. 50–51.]

[19] The judge described the Morgan Stanley fairness letter as "devoid of facts or analysis" and contrasted it with examples provided from other cases by counsel for Mr. Mulacek. Those opinions had, he noted, provided "offer facts and figures, analysis and comparative data" not found in this instance. In fact, the judge noted, the Morgan Stanley opinion provided "less information than a residential real estate appraisal commonly filed in this Court." (At para. 53.)

[20] In the chambers judge's analysis, however, the "real question" was whether fairness opinions should be regarded as independent opinions or "simply comfort letters that a board of directors enlists to support their decision." He referred to *Royal Host Inc. (Re)* 2014 ONSC 3323, which was decided after the well-known case of *Champion Iron Mines Ltd. (Re)* (2014) 119 O.R. (3d) 339. In *Champion*, the company seeking court approval had not been permitted to put its fairness opinion into evidence as an expert report because the applicant had not complied with the Court's rules governing the adducing of expert opinions into evidence. (The transaction was approved on the basis of "ample other admissible evidence" that supported it.) Relying on *Champion*, the Court in *Royal Host* commented that:

> The purpose of a fairness opinion is a commercial one. It is an opinion to be considered by the board of directors and the shareholders in a commercial context. It is not an expert report in a litigation context. If the board or the shareholders are not satisfied with the report, they can vote with their feet and not proceed with or approve the arrangement. [At para. 8; emphasis added.]

The chambers judge agreed that a "third party financial advisor does not need to meet the requirements of an expert pursuant to the *Rules of Court",* although he acknowledged that the question of whether a fairness report should meet the standard of an expert report under the *Rules of Court* had not been argued before him.

[21] More importantly, the judge expressed the view that there should be an independent "flat fee Fairness Opinion to assist shareholders and the court if [the Board] wishes to comply with best practice corporate governance". (My emphasis.) Thus, he said, an opinion that "simply follows the direction of the Board and is based on a success fee does not meet the standard of good corporate governance." (See also *HudBay Minerals Inc. (Re)* 2009 CarswellOnt 2219 at para. 264, cited at para. 60.)

[22] The point, the chambers judge said, is that although a fairness opinion is only one indicator of fairness, it should be "robust, rigorous and independent", prepared by "reputable experts" and intended to help discharge the fiduciary duty of special committees of independent boards and to assist the shareholders in their evaluation of the fairness of a proposed arrangement. Thus an opinion obtained from an independent financial advisor "retained on a flat fee" is an important factor in assisting the court to scrutinize the arrangement before it. (At para. 61.)

[23] Turning, however, to the second question – whether the proposed arrangement had been shown to be fair and reasonable – the chambers judge found the deficiencies he had identified to be less important – or perhaps unimportant – in comparison to the fact that a substantial majority of the shareholders of InterOil had voted in favour of the arrangement. (The purpose of the arrangement was said to be to "sell the assets of InterOil for the highest price available rather than continue to be involved in the long game in the Elk–Antelope gas fields.")

[24] The material portions of the judge's analysis of the "fair and reasonable" issue was as follows:

> Mr. Mulacek had his opportunity to persuade shareholders that the $45 plus the potential of $7.07 for each 1 tcfe of PRL15 2C Resources above 6.2 tcfe to a maximum of 10 tcfe, was not a reasonable or fair price for Interoil shares. He failed to persuade the 80% who voted in favour of the Exxon Arrangement.
>
> This Court should speak freely and independently about matters of corporate governance but at the end of the day it is the shareholders that have spoken in favour of the Exxon Arrangement. Judges are not business people and are not in a good position to judge these investments....

> …
>
> Any shareholder reading the Circular can discern the lack of detail regarding valuations and analysis as well as the interest of the CEO in voting for the Arrangement.
>
> While that may draw criticism from this Court in terms of corporate governance, it should not prevent shareholders from realizing substantive increases in value.
>
> From the shareholders' perspective, they can realize their gain and Mr. Mulacek can pursue his Dissent Rights.
>
> Further, the Exxon Arrangement has clear advantages in receiving Exxon shares with immediate liquidity at $45 per share value.
>
> The CRP provides a higher rate of return than the Oil Search Arrangement but is capped. While the Board did not provide detail on the value of Interoil's Elk-Antelope field nor the strategic alternatives, it reduced the speculative nature of the Interoil shares and provided a solid return.
>
> For these reasons, I approve the Exxon Arrangement as fair and reasonable. [At paras. 62–63 and 65–70; emphasis added.]

In the result, the arrangement was approved.

[25] On October 19, 2016, Mr. Justice Frankel of this court stayed the order of the chambers judge pending the hearing of this appeal by Mr. Mulacek. At the end of the hearing we extended the stay until the disposition of the appeal.

On Appeal

[26] The appellant raises the following grounds of appeal:

a) The Application Judge erred in relying on the shareholder vote as proxy for the determination of the fairness of the Exxon Arrangement. This is an error because the Application Judge failed to consider the reliability of the vote given the deficiencies in information provided to shareholders and the Application Judge failed to give appropriate consideration to other indicia of unfairness;

b) The Application Judge failed to properly consider the following factors in his fairness analysis: (i) the lack of a robust fairness opinion; (ii) the evidence of the negative impact of the Exxon Arrangement on shareholders; (iii) the lack of any detailed information or analysis from InterOil as to the value of the Elk-Antelope Fields and the financial impact of the structure and terms of the Exxon Arrangement; (iv) the absence of an independent committee of directors' approval of the transaction; and (v) the compromised endorsement of the Exxon Arrangement by the CEO and Morgan Stanley;

c) The Application Judge erred in deferring to the business judgment of the Board instead of scrutinizing the Exxon Arrangement as required under the BCA and the BCE test;

d) The Application Judge erred in considering the reasonableness of the consideration offered by Exxon as an indicator of fairness when there is no evidence to support these factors;

e) The Application Judge erred by reversing the onus in the test for approval of the Exxon Arrangement and holding that it was Mr. Mulacek who had the obligation to convince shareholders that the Exxon Arrangement was unfair; and

f) The Application Judge erred in holding that the Appellant's dissent rights were sufficient.

[27] The respondents take issue with all of these grounds and emphasize the deference that is to be given to a court's exercise of statutory discretion. In this regard, counsel referred us to *Dhillon v. Pannu* 2008 BCCA 514 at paras. 26–8, where it was noted that the standard of review for discretionary decisions has been expressed in "slightly varying ways" in recent years. The leading cases on this point were said to be *Friends of the Oldman River Society v. Canada (Minister of Transport)* [1992] 1 S.C.R. 3 and *Named Person v. Vancouver Sun* 2007 SCC 43. They instruct that an appellate court should not interfere unless the court below misdirected itself, gave no weight or insufficient weight to a relevant consideration, or made an error in principle.

[28] Turning to the substantive law, counsel are in agreement that the leading authority is *BCE, supra*. That case of course involved a group of debentureholders of a corporation in fairly dire straits. Their debt instruments were likely to be adversely affected, in terms of *value*, by the proposed transaction, but the *legal* rights attached to the debentures would remain unchanged. Thus the Court emphasized that a judge faced with an application under s. 192 of the *Canada Business Corporations Act* (the equivalent of s. 195 of the *Yukon Business Corporations Act*) must be satisfied the arrangement achieves a "fair balancing" of conflicting interests – in *BCE*, those of the debentureholders as opposed to those of the shareholders.

[29] The case at bar does not involve competing classes of shares or securities; but the Court in *BCE* also gave some general guidance as to a judge's task in

considering an arrangement. The following comments are most relevant to the case at bar:

a) The court should consider whether the arrangement, objectively viewed, is fair and reasonable and "looks primarily to the interests of the parties whose legal rights are being arranged". (Para. 119);

b) The court should focus on the "terms and impact of the arrangement itself, rather than on the process by which it was reached. What is required is that the arrangement itself, viewed substantively and objectively, be suitable for approval." (Para. 136);

c) The "business judgment test" – whether an intelligent and honest business person, as a member of the voting class concerned and acting in his or her own interest would reasonably approve the arrangement – does *not* constitute "a useful or complete statement of what must be considered". (Para. 139);

d) The reviewing judge must "delve beyond whether a reasonable business person would approve of [the] plan." (Para. 141);

e) There must be a "positive value to the corporation to offset the fact that rights are being altered". In other words, the court must be satisfied the "burden imposed by the arrangement on security holders is justified by the interests of the corporation… as an ongoing concern." (Para. 145);

f) The "valid purpose inquiry" is fact-specific. One important factor is the "necessity" of the arrangement to the continued operation of the corporation. Indicia of necessity include the existence of alternatives and market reaction to the plan. (Para. 146);

g) If the arrangement is not mandated by the corporation's financial or commercial situation, courts will be more cautious and strive to ensure that it is not in the sole interest of a particular stakeholder. (Para. 146);

h) Generally, the arrangement must strike a "fair balance, having regard to the ongoing interests of the corporation and the circumstances of the case. Often this will involve complex balancing, whereby courts determine whether appropriate accommodations and protections have been afforded to the concerned parties." (Para. 148);

i) Other indicia include whether a majority of securityholders have voted to approve the arrangement; whether an intelligent businessperson might reasonably approve of the plan; the "proportionality of the compromise" between various security holders; the securityholders' positions before and after the arrangement; whether the plan was approved by a special committee of independent directors; the presence of a fairness opinion from a reputable expert; and the access of shareholders to dissent and appraisal remedies. (Para. 152);

j) The foregoing list is not exhaustive and the court should not insist on a "perfect arrangement." As stated at para. 155:

> The court on a s. 192 application should refrain from substituting their views of what they consider the "best" arrangement. At the same time, the court should not surrender their duty to scrutinize the arrangement. Because s. 192 facilitates the alteration of legal rights, the Court must conduct a careful review of the proposed transactions. As Lax J. stated in *UPM-Kymmene Corp. v. UPM-Kymmene Miramichi Inc.* (2002), 214 D.L.R. (4th) 496 (Ont. S.C.J.), at para. 153: "Although Board decisions are not subject to microscopic examination with the perfect vision of hindsight, they are subject to examination."
> [Emphasis added.]

[30] As mentioned, the case at bar does not involve a conflict between different classes of securityholders or the 'balancing' of conflicting legal rights. Rather, it involves conflicting views as to the financial situation and prospects of InterOil and the degree of risk to which shareholders wish their investments to be subject going forward. (One assumes the shares were acquired with the understanding they were "speculative" in the first place.) On the one hand, Mr. Mulacek sees the company as "well-positioned" to develop its share in the Elk-Antelope fields with its joint venture partners. He deposed:

> The project development timeline anticipates completion of appraisal drilling in 2016, resource confirmation in 2017, and commercial production in 2022.
>
> The terms and structure of the ExxonMobil Transaction unfairly and inappropriately deny Interoil shareholders any reasonable retained participation in, or compensation for, the vast upside of potential value of the resource. This is particularly egregious given the fact that I believe a development decision on this gas field asset is imminent, which will materially de-risk the project and unlock additional value. In my view, the terms and structure of the ExxonMobil Transaction fail to provide fair consideration to Interoil shareholders.
>
> Under the … Transaction, Interoil shareholders will receive for each common share of Interoil (a) a fixed component comprised of ExxonMobil shares worth $45; and (b) a capped contingent component based on a one-time interim resource estimate. The absence of any subsequent contingent payments tied to future growth in resource estimates based on recertification after production is underway unfairly denies Interoil's shareholders any participation in the value upside created through commercialization of this key gas resource asset. This Transaction structure effectively shifts the entire upside potential value of this gas resource to ExxonMobil after the initial recertification payment.
>
> In addition, the … Transaction fails to ensure that the interim resource certification process for the contingent payment calculation is fair, transparent, and focused on accurately assessing the potential resource. Among other things, ExxonMobil will run the interim resource certification process without the participation of Interoil's long-time independent resource appraiser and with no effective oversight or involvement of any Interoil shareholder nominee. The structure and terms of the Transaction in respect of the interim resource certification for the contingent payment unfairly favours ExxonMobil, who is incentivized to achieve a low contingent payment.
>
> [Emphasis added.]

[31] Mr. Mulacek takes the view that InterOil failed to provide sufficient information to its shareholders to make a "fully informed decision" in determining whether to approve or reject the bid and in particular that it:

> … failed to provide any meaningful disclosure of the potential value of the gas field asset, the financial impact of the cap on the contingent payment, the range of value of the gas field asset shareholders will forego in the event the resource certification exceeded the cap, and the risk factors associated with the determination of the contingent payment.

[32] On the other hand, InterOil's directors are of the view that it is in the interests of shareholders to reap the advantages of "certainty of value" with *some* participation in the 'upside" of the development of the PRL15 gasfields. Thus the Board set forth

in the Information Circular various reasons for its recommendation of the arrangement, including:

- **Significant Premium to Shareholders.** The Arrangement values the equity of InterOil at approximately $2.3 billion or $45.00 per Common Share, plus the potential value of the CRP. Without giving effect to the potential value of the CRP, this represents a premium of approximately 42.2% to the closing price of the Common Shares on the NYSE on May 19, 2016 (Eastern time), the last trading day prior to the public announcement by InterOil and Oil Search of the Oil Search Arrangement.
- **Shareholder Participation in Future Potential of the PRL 15 Fields.** The CRPs and the transactions contemplated in the CRP Agreement provide Shareholders the ability to participate in potential upside of the resource volume of the PRL 15 Fields under the Total Sale Agreement. This upside will also include the results and information gained from the drilling of the Antelope 7 appraisal well which is expected to spud in September 2016.
- **Liquidity of the ExxonMobil Shares.** The ExxonMobil Shares have historically been, and are expected to be at the Effective Time, highly liquid securities. The consideration to be paid to Shareholders pursuant to the Arrangement is comprised in part of ExxonMobil Shares, which should provide immediate liquidity to Shareholders should they wish to sell the ExxonMobil Shares they receive.
- **Certainty of Value.** The portion of the consideration comprised of ExxonMobil Shares to be paid to Shareholders pursuant to the Arrangement is fixed at $45.00 per Common Share and will be satisfied by issuing, in exchange for each Common Share, a number of ExxonMobil Shares equal to (i) $45.00, divided by (ii) the volume weighted average price of the ExxonMobil shares on the NYSE for the 10 consecutive trading days ending on (and including) the second trading date immediately prior to the Effective Date. The fixed value (or floating exchange) nature of the consideration to be issued pursuant to the Arrangement provides certainty of value to the Shareholders.

  …

- **Review of Strategic Alternatives.** The Board considered and actively pursued a wide range of potential strategic alternatives available to InterOil, including the potential shareholder value as assessed by InterOil and its financial advisors that could be expected to be generated by remaining an independent company, as well as the potential benefits, risks and uncertainties associated with such alternatives. As an independent standalone entity and depending on the size of further payments under the Total Sale Agreement, InterOil may have been required to raise additional funds through the capital markets in order to fund its share of project development costs in respect of the PRL 15 Fields – a step that is no longer expected to be

necessary under ExxonMobil ownership. See "The Arrangement – Background to the Arrangement".

- **Participation in ExxonMobil Base.** Shareholders who retain the ExxonMobil Shares they receive in connection with the Arrangement will have the opportunity to participate in ExxonMobil's diverse asset base and operations. ExxonMobil's asset base includes an operating interest in the world-class PNG LNG Project.

  …

- **Participation by Shareholders in Future Growth**. Shareholders who retain the ExxonMobil Shares they receive in connection with the Arrangement will have the opportunity to participate in any future increase in the value of ExxonMobil.
- **Participation in ExxonMobil's Dividend.** Shareholders who retain the ExxonMobil Shares they receive in connection with the Arrangement will have the opportunity to participate in any future ExxonMobil dividends.
- **Terms of the Arrangement Agreement are Reasonable.** The Arrangement Agreement is a result of arm's-length negotiations between InterOil and ExxonMobil. The Board believes that the terms and conditions of the Arrangement Agreement, including the fact that InterOil's and ExxonMobil's representations, warranties and covenants and the conditions to completion of the Arrangement are, after consultation with InterOil's legal advisors, reasonable in light of all applicable circumstances.
- **Negotiations with ExxonMobil**. Based on the fact that the negotiations between InterOil and ExxonMobil were extensive, lasted for several months (see "The Arrangement – Background to the Arrangement"), and resulted in a significant increase from ExxonMobil's previous offers and from the consideration contemplated by the Oil Search Agreement, the Board believes that the Arrangement represents ExxonMobil's highest price and the highest price reasonably attainable for the Shareholders in the near future.
- **InterOil's Financial Condition and Prospects.** The Board reviewed InterOil's current and historical financial condition, results of operations, business, competitive position and prospects as well as InterOil's future business and potential long-term value taking into account its future prospects and risks if it were to remain an independent company.
- **Fairness Opinion of Morgan Stanley**. In the opinion of Morgan Stanley, as of June 21, 2016, and based upon and subject to the assumptions, limitations, qualifications and other matters contained therein, the consideration to be received by Shareholders under the Arrangement was fair, from a financial point of view, to such Shareholders. See "The Arrangement – Fairness Opinion" and Schedule C.

…

- **Court Approval is Required.** The Arrangement must be approved by the Court, which will consider, among other things, the fairness, procedurally and substantively, of the Arrangement to Shareholders.
- **Dissent Rights.** The availability of Dissent Rights to the registered Shareholders with respect to the Arrangement.

[33] It is of course for the shareholders, not the court, to decide between the conflicting views of the prospects of InterOil and its joint venture interest in the Elk-Antelope gasfields. It *is* the court's task to decide whether the proposed arrangement has been shown to be fair and reasonable. In the circumstances of this case, that requires, in my respectful view, that the court be satisfied the shareholders were in a position to make an *informed choice*, both as to the value they would be giving up, and the value they would be receiving. It is in connection with the values of the PRL 15 gas fields – the primary asset of the company – and the capped CRP that, in my opinion, difficulties arise in this case.

[34] Most obviously, there is the fact that the Morgan Stanley opinion expressly stated that it had not attributed any "specific value to the CRP for purposes of arriving at the conclusion expressed in this letter." This fact, together with the contingent nature of Morgan Stanley's fee, clearly undermines the utility of the opinion to the directors, the shareholders and the Court. It is difficult to disagree with Mr. Dey's observation that:

> The Board did not obtain advice on the value of the CRP. The Board seems to have concluded that by including the CRP in the consideration to be received for the sale of the company, it had satisfactorily addressed the need for the company to be compensated for the Elk-Antelope asset without actually obtaining advice as to the value of the asset. In my view, a board engaged in a proper and robust review and consideration of a proposed transformative transaction should have obtained independent advice on the value of the CRP, the Elk-Antelope asset, and the 101 CFE's impact on the CRP. Moreover, those estimates of value should have been disclosed to shareholders so that shareholders could decide whether the US$45 plus the capped CRP adequately reflected the value of the company. In the absence of this guidance, shareholders would not know the value of the Elk-Antelope asset, what they gave up by agreeing to capped the CRP at 101 CFE, and whether the terms of the Transaction fairly reflected the value of the Elk-Antelope asset.

> In circumstances where a financial expert's compensation depends in part on the success or failure of a transaction, shareholders must be in a position to evaluate whether the advice is influenced by these terms of payment. In the circumstances of this transaction, it is my view that the Board should have disclosed the details of the compensation payable to Morgan Stanley. It should also have engaged a second financial advisor whose compensation would not be dependent upon the success or failure of the transaction….
>
> [Emphasis added.]

[35] There is another reason why the Board should have engaged a second financial advisor on a 'flat fee' basis, i.e., for a fee not dependent upon the success or failure of the transaction. Although the Board constituted a committee to oversee the negotiation of the transaction, the committee appears to have been fairly passive, merely receiving reports from management who led the negotiations. As we have seen, if the transaction proceeded, the CEO stood to realize significant compensation through the change of control provision in his employment contract and through the acceleration of his RSU's (restricted share units). Other members of the Board also stood to reap significant benefits.

[36] In these circumstances, it was incumbent on the Board to ensure that the arrangement negotiated by management did indeed reflect the fair value of the company (and of course its assets) and its issued shares. For this purpose, the Board should have sought independent advice as to the financial fairness of the transaction.

[37] As we have seen, however, the only independent opinion in evidence on this point was provided by Mr. Booth of Paradigm Capital, who found in part that:

> When examining the resource estimates summarized in the Company's AIFs from 2008 to 2015, it is evident that there has been a history of positive estimate revisions, with GLJ consistently increasing its 1C, 2C and 3C volumes. Indeed, from 2008 to 2015, the 2C volumes were increased from 631 mmboe gross (3.79 Tcfe) to 1,663 mmboe gross (9.98 Tcfe). In our opinion, this indicates an increasing confidence in the resource estimate due to a lack of negative revisions over time. It reflected new developments and information, such as the availability of seismic data and the completion of five Antelope wells and three Elk wells. Based on this historical trend, it is reasonable to expect further positive estimate revisions with the scheduled completion of two new Antelope wells and the resulting test data.

His conclusion was that the “Consideration pursuant to the Transaction [was] inadequate, from a financial point of view, to the shareholders of InterOil.” (My emphasis.) Again, InterOil did not respond to or provide expert opinions that were contrary to those of either Mr. Dey or Mr. Booth.

[38] The chambers judge in his discussion of “best practice corporate governance” agreed that a board in the position of InterOil’s board “must ensure that there will be an independent flat fee Fairness Opinion to assist shareholders and the Court” and that “a fairness opinion prepared by a financial advisor who is being paid a signing fee or success fee does not assist directors comprising a special committee of independent directors in demonstrating the due care they have taken in complying with their fiduciary duties in approving a transaction.” (At paras. 59–60.)

[39] The judge seemed to take the view, however, that the deficiencies in the fairness opinion and disclosure generally were nevertheless not relevant to the question of whether the arrangement was fair and reasonable. I repeat here the crucial part of his reasoning:

> This Court should speak freely and independently about matters of corporate governance but at the end of the day it is the shareholders that have spoken in favour of the Exxon Arrangement. Judges are not business people and are not in a good position to judge these investments. See Edward Iacobucci, “Making Sense of Magna”, (2011) 49 Osgoode Hall L.J. 237-275 at para. 47.
>
> The shareholders of Interoil saw their share price increase at a premium of 42.2% after the Oil Search Arrangement, and, considering the price increase to $45 per share from Exxon, plus a CRP potential for a total value of $72 per share, they are entitled to make the decision approving the Exxon Arrangement.
>
> Any shareholder reading the Circular can discern the lack of detail regarding valuations and analysis as well as the interest of the CEO in voting for the Arrangement.
>
> While that may draw criticism from this Court in terms of corporate governance, it should not prevent shareholders from realizing substantive increases in value. (At paras. 63-66)

[40] With respect, it seems to me that the chambers judge erred in principle in setting aside the identified deficiencies when he came to consider the fairness and reasonableness of the proposed arrangement. Instead of ‘delving into’ the question

of value (see *BCE* at para. 141), he relied on the truism that the shareholders were “entitled to make the decision”. Clearly, it *was* the shareholders’ decision to make, but court approval was *also* required by the Act to ensure the decision was fair and reasonable in the sense of being based on information and advice that was adequate, objective and not undermined by conflicts of interest. Given the ‘red flags’ in this case – the absence of a fairness opinion from an independent expert, the failure of Morgan Stanley to assess the value of the CRP as compared with the value of the PRL prospects (again, the company’s primary asset); the deficiencies pointed out by Mr. Dey; the unchallenged report of Mr. Booth; the fact the CEO was in a position of conflict; the probability the “independent” special committee was not independent of management; and the lack of “necessity” for the deal – the Court was required to do more than accept the vote of the majority as a “proxy” for fairness, or the cash amount of Exxon’s offer as a proxy for reasonableness. As I say, this was an error of principle, if not law, in the sense that the correct ‘legal test’ was not brought to bear.

[41] The respondents acknowledged that the onus was on InterOil to satisfy the Court that the transaction was fair and reasonable. Counsel urged this court not to substitute its own opinion for that of the chambers judge under the “guise” that he failed to give sufficient weight to one or more relevant factors. Counsel also emphasized the Supreme Court’s comment in *BCE* that courts should focus on the terms and impact of the arrangement itself rather than the process by which it was reached. (At para. 136.)

[42] More particularly, Mr. Friedland submitted that Exxon’s offer had been the result of a “competitive bidding process.” He invited us to review the Oil Search bid (to which Exxon’s bid was of course “superior”), and to consider the various negative possibilities or “risks” which may face InterOil in the future as it becomes necessary to contribute its share of funds required for the development of the Elk-Antelope fields. He submitted that past assessments of the project disclosed in various information circulars and financial statements of InterOil have been “all over the map”. In his submission, the recent increase in the trading price of InterOil shares is

an indicator that the arrangement is regarded by the market as a 'good deal' for shareholders. In the end, the respondents contend the chambers judge recognized that the best alternative for shareholders was to "sell the assets of InterOil for the highest price available rather than continue to be involved in the long game in the Elk-Antelope gas fields." (At para. 62.)

[43] Again, I acknowledge that (adequately informed) shareholders are perfectly entitled to make a decision to "de-risk" their investments. I also acknowledge that in general, "judges are not business people" and may not be in the best position to assess investments like the InterOil shares. Nevertheless, it was not open to the Court to set to one side the deficiencies it had identified, and simply accept the verdict of the market or the majority shareholders. It will almost always be the case in applications under s. 195 that the arrangement in question has been approved by a substantial majority of shareholders, who are obviously voting in what they see to be their own interests. The Court must be satisfied, however, that the arrangement is objectively fair and reasonable in a more general sense. The evidence before the judge contained many deficiencies that were not answered by the fact that the arrangement was approved by a majority or that Mr. Mulacek had dissent rights available to him.

[44] In all the circumstances, we are not able to say that the arrangement has been shown to be fair and reasonable.

[45] It follows that I would allow the appeal, set aside the chambers judge's order, and dismiss the application under s. 195 of the *Business Corporations Act*.

[46] We are indebted to counsel for their able arguments.

[47] **SAUNDERS J.A.**: I agree.

[48] **GROBERMAN J.A.**: I agree.

[49] **NEWBURY J.A.**: The appeal is allowed.

"The Honourable Madam Justice Newbury"

MANAGEMENT'S DISCUSSION AND ANALYSIS:

The following Management's Discussion and Analysis ("MD&A") is dated August 5, 2015 and should be read in conjunction with the unaudited interim consolidated financial statements and accompanying notes of Lightstream Resources Ltd. ("Lightstream", "we" or "our" or the "Company") as at and for the three and six months ended June 30, 2015 and 2014, MD&A for the year ended December 31, 2014, and the audited consolidated financial statements for the years ended December 31, 2014 and 2013. All amounts are in Canadian dollars, unless otherwise stated and all tabular amounts are in thousands of Canadian dollars, except per share amounts or as otherwise noted. Natural gas volumes have been converted to barrels of oil equivalent ("boe"). Six thousand cubic feet ("Mcf") of natural gas is equal to one barrel of oil equivalent based on an energy equivalency conversion method primarily attributable at the burner tip and does not represent a value equivalency at the wellhead. Boes may be misleading, especially if used in isolation.

This MD&A contains financial measures that have no standardized meaning under International Financial Reporting Standards ("IFRS") and forward-looking statements. As such, the MD&A should be read in conjunction with Lightstream's disclosure under the headings "Non-GAAP Measures" and "Forward-Looking Information" at the end of this MD&A.

SUMMARY SECOND QUARTER HIGHLIGHTS:

- Second quarter average production was 31,966 boepd (72% light oil and liquids weighted), a decrease of 9% from the first quarter of 2015 attributed to a reduced capital program and higher downtime associated with third party facility maintenance and spring break up. Second quarter 2015 production was 25% lower than second quarter 2014 production of 42,513 boepd, primarily reflecting dispositions throughout 2014 combined with the reduction in our capital program since early 2014, which has resulted in natural well declines exceeding new well production.
- Our operating netback was $29.18/boe, a 40% increase over the first quarter of 2015 primarily due to higher realized oil prices. Our operating netback decreased 49% from the second quarter of 2014, attributed to lower commodity prices, partially offset by lower royalties and production expenses. Benchmark oil prices have declined approximately 40% from Q2 2014, resulting in a realized oil price of $64.24/bbl in Q2 2015 down from $102.87/bbl in Q2 2014.
- Funds flow from operations was $67 million ($0.34 per basic share), a 29% increase over the first quarter of 2015 due to higher commodity prices. Funds flow from operations decreased 62% from the second quarter of 2014, primarily due to lower commodity prices and lower production.
- Capital expenditures of $20 million (before asset acquisitions and dispositions) in second quarter 2015 were 67% lower than first quarter 2015 expenditures of $60 million and second quarter 2014 expenditures of $61 million. Lower spending levels are consistent with our reduced capital program and commitment in 2015 to spend within cash flow. In the quarter, we drilled one non-operated well, brought six wells on production and exited the quarter with two wells in inventory.
- Subsequent to June 30, 2015, we issued a total of US$650 million in second lien notes ("Secured Notes"). US$450 million of the Secured Notes were issued in exchange for US$546 million of senior unsecured notes, which were cancelled. A further US$200 million of Secured Notes were issued for cash proceeds, which we used to reduce the outstanding borrowing under our secured termed credit facility. As a result of these transactions, we have reduced our overall debt by approximately $125 million and increased credit capacity by approximately $250 million.

SELECTED QUARTERLY RESULTS

	Three months ended June 30,			Six months ended June 30,		
	2015	2014	% Change	**2015**	2014	% Change
Financial ($000s, except where noted)						
Oil and natural gas sales	**136,265**	326,552	(58)	**257,396**	651,786	(61)
Funds flow from operations [1]	**66,966**	177,034	(62)	**118,894**	352,004	(66)
Per share - basic ($)[1]	**0.34**	0.88	(61)	**0.60**	1.76	(66)
- diluted ($)[1] [2]	**0.34**	0.87	(61)	**0.60**	1.73	(65)
Adjusted Net Income (loss)[1]	**(51,533)**	68,202	(176)	**(178,695)**	82,601	(316)
Per share - basic ($)[1]	**(0.26)**	0.34	(176)	**(0.90)**	0.41	(320)
- diluted ($)[1] [2]	**(0.26)**	0.34	(176)	**(0.90)**	0.41	(320)
Dividends[1]	**—**	24,351	(100)	**—**	48,649	(100)
Per share ($)[1]	**—**	0.12	(100)	**—**	0.24	(100)
Capital expenditures [3]	**20,175**	61,249	(67)	**80,429**	260,532	(69)
Net capital expenditures[1]	**18,324**	(77,174)	(124)	**67,255**	8,429	698
Total debt[1] [4]				**1,668,123**	1,985,342	(16)
Basic common shares, end of period (000)				**197,565**	200,150	(1)
Operations						
Operating netback ($/boe except where noted) [1] [5]						
Oil, NGL and natural gas revenue [6]	**46.54**	83.92	(45)	**42.07**	82.84	(49)
Royalties	**4.47**	12.12	(63)	**4.54**	11.93	(62)
Production expenses	**12.89**	14.31	(10)	**12.68**	14.10	(10)
Operating netback	**29.18**	57.49	(49)	**24.85**	56.81	(56)
Average daily production (boe/d)						
Oil and NGL (bbl/d)	**23,066**	34,128	(32)	**24,827**	34,665	(28)
Natural gas (mcf/d)	**53,399**	50,309	6	**52,419**	51,400	2
Total (boe/d) [5]	**31,966**	42,513	(25)	**33,563**	43,232	(22)

(1) Non-GAAP measure. See "*Non-GAAP Measures*" section within this document.

(2) Consists of common shares, stock options, deferred common shares, incentive shares and convertible debentures as at the period end date.

(3) Prior to asset acquisitions and dispositions.

(4) Total debt is calculated as secured termed credit facility outstanding plus accounts payable less accounts receivable, prepaid expense and long-term investments plus the full value outstanding on the senior unsecured notes and convertible debentures converted to Canadian dollars at the exchange rate on the period end date.

(5) Six Mcf of natural gas is equivalent to one barrel of oil equivalent ("boe").

(6) Net of transportation expenses.

MANAGEMENT'S DISCUSSION AND ANALYSIS

2015 GUIDANCE

($000s, except where noted and per share amounts)	2015 Guidance (Mar 6, 2015)	2015 Revised Guidance (Aug 5, 2015)	2015 Actual (to June 30, 2015)
Production (annual average)			
Total (boe/d)	**30,500 - 32,500**	**30,500 - 32,500**	**33,563**
Natural Gas Weighting	**26%**	**27%**	**26%**
Exit Production (boe/d)	**26,500 - 28,500**	**26,500 - 28,500**	**-**
EBITDA	**$255,000 - $275,000**	**$295,000 - $315,000**	**$174,202**
Funds Flow from Operations[1]	**$145,000 - $165,000**	**$175,000 - $195,000**	**$118,894**
Funds Flow per share[1]	**$0.74 - $0.84**	**$0.89 - $0.99**	**$0.60**
Dividends per share	**$0.00**	**$0.00**	**$0.00**
Capital Expenditures[2]	**$100,000 - $120,000**	**$100,000 - $120,000**	**$80,429**
Pricing Assumptions:			
Crude oil - WTI (US$/bbl)	**52.50[3]**	**50.00**	**53.29**
Crude oil - WTI (Cdn$/bbl)	**65.63**	**64.94**	**65.70**
Corporate oil differential (%)	**15**	**15**	**15**
Natural gas - AECO (Cdn$/mcf)	**3.00**	**3.00**	**2.74**
Exchange rate (US$/Cdn$)	**0.80**	**0.77**	**0.81**

(1) Funds flow per share calculation based on 197 million weighted average basic shares outstanding.
(2) Projected capital expenditures exclude acquisitions and divestitures, which are evaluated separately.
(3) Oil pricing assumption was $50/bbl WTI for first half of 2015 and $55/bbl WTI for second half.

Production for the first six months of 2015 was above our annual average guidance and in line with our expectations. We anticipate that production levels will decrease over the remainder of the year as we restrict the amount of capital being invested into new operated wells given the current low commodity price environment, aside from one Falher liquids-rich well planned for the second half of 2015, which will help maximize the use of our facility infrastructure in the area.

Funds flow from operations of $119 million in the first half of 2015 is above our expectations as realized prices were higher during the second quarter than our annual average oil price assumption. Capital expenditures of $80 million over the first six months of 2015, representing approximately 75% of anticipated spending for the year, are in line with our expectations. Capital spending is expected to be significantly lower during the second half of the year as we remain focused on preserving our long term asset value until we are in a more positive economic environment with higher commodity prices and/or lower capital costs.

We are increasing the mid-point of our 2015 funds flow from operations guidance by 19% to $185 million, which incorporates our strong first half results and a lower WTI price assumption of US$50.00/bbl for the second half of the year. We continue to expect to generate funds flow well above our capital spending in 2015 and based on the mid-point of our guidance, we expect surplus cash of approximately $75 million to be applied to reduce our debt.

FINANCIAL AND OPERATING REVIEW

(Comparisons presented in this MD&A are second quarter of 2015 compared to the second quarter of 2014 unless otherwise noted. All references to well counts are on a net basis unless otherwise noted.)

Average Daily Production

	Three months ended June 30,			Six months ended June 30,		
	2015	2014	Change	**2015**	2014	Change
Oil and NGL (bbls)	**23,066**	34,128	(32%)	**24,827**	34,665	(28%)
Natural gas (Mcf)	**53,399**	50,309	6%	**52,419**	51,400	2%
Total (boe)	**31,966**	42,513	(25%)	**33,563**	43,232	(22%)

Total production for the three and six months ended June 30, 2015 decreased 25% and 22% respectively from 2014, due primarily to the disposition of assets representing approximately 6,315 boepd of production during 2014 combined with the reduction in our capital program since early 2014, which has resulted in natural well declines exceeding new well production. Second quarter 2015 production decreased 9% from Q1 2015 primarily due to higher downtime associated with third party facility maintenance and spring break up. Natural gas production increased over the prior year due to favorable results from two Falher liquids-rich gas wells brought on-stream in 2015 within the Cardium business unit. During the second quarter of 2015, we brought six wells on production compared to 29 wells during the same period a year ago. For the first six months of 2015, we brought 26 wells on production compared to 54 wells during the same period a year ago. At June 30, 2015, there were two wells in inventory that are scheduled to be completed and/or brought on production during the third quarter.

In southeast Saskatchewan, our Bakken business unit averaged 11,720 boepd of production during the second quarter of 2015, representing a 15% decrease from Q1 2015 production of 13,811 boepd, due to a facility turnaround and lower seasonal field activity levels. Second quarter 2015 production decreased 22% from Q2 2014 volumes of 14,990 boepd, due to continued attenuation of investment in the Bakken as we continued to maximize the free cash flow generated from this resource play. During the second quarter of 2015, we brought one well on production in the Bakken, leaving two wells remaining in inventory at June 30, 2015.

In the Cardium business unit, production for the second quarter of 2015 averaged 17,455 boepd, which was relatively unchanged from Q1 2015 production of 17,661 boepd. Second quarter 2015 production decreased 9% from Q2 2014 volumes of 19,277 boepd, due to a reduction in new well program spending compared to 2014. During the second quarter, we brought five wells on-stream in the Cardium, including one liquids-rich Falher well. We have seen encouraging results from the Falher gas wells and we continue to evaluate further development drilling opportunities in this play to efficiently utilize our existing gas infrastructure.

In our Alberta/BC business unit, production in the second quarter of 2015 averaged 2,791 boepd, representing a 25% decrease from Q1 2015 production of 3,707 boepd, due to higher downtime resulting from a third party facility turnaround. Second quarter 2015 production decreased 21% from Q2 2014 as a result of limited new well activity in the area.

Average Benchmark and Realized Prices

	Three months ended June 30,			Six months ended June 30,		
	2015	2014	Change	**2015**	2014	Change
WTI (US$/bbl)	**57.94**	102.99	(44%)	**53.29**	100.84	(47%)
WTI ($/bbl)	**71.05**	112.31	(37%)	**65.70**	110.61	(41%)
Edmonton Par	**67.55**	105.77	(36%)	**59.74**	102.80	(42%)
Differential % of WTI	**(5%)**	(6%)	—	**(9%)**	(7%)	—
AECO natural gas ($/Mcf)	**2.69**	4.76	(43%)	**2.74**	5.28	(48%)
US$ per Cdn$1	**0.82**	0.92	(11%)	**0.81**	0.91	(11%)
Oil and NGL						
Realized price per bbl ($/bbl)	**58.71**	97.76	(40%)	**51.50**	95.80	(46%)
Differential % of Edm. Par	**(13%)**	(8%)	—	**(14%)**	(7%)	—
Differential % of WTI	**(17%)**	(13%)	—	**(22%)**	(13%)	—
Natural gas						
Realized price per Mcf ($/Mcf)	**2.68**	5.01	(47%)	**2.74**	5.45	(50%)

Realized oil and NGL prices decreased for the three and six months ended June 30, 2015, due to lower WTI oil prices, which have significantly declined from the same period a year ago. A weaker Canadian dollar relative to the U.S. dollar has partially offset the impact of lower WTI oil prices. Light oil differentials are consistent with the prior year but remain volatile due to changes in demand for Canadian sourced light crude oil. NGL pricing, particularly propane, was lower in Q2 2015, due to growth in supply in North America and the lack of storage or export facilities to accommodate the increased production. The reduced pricing has widened our overall liquids differential. The decrease in realized natural gas prices from the prior year is due to lower AECO spot pricing as a result of higher natural gas supply and storage levels.

Revenue

	Three months ended June 30,			Six months ended June 30,		
	2015	2014	Change	**2015**	2014	Change
Oil and natural gas sales	**136,265**	326,552	(58%)	**257,396**	651,786	(61%)
Royalties	**(13,002)**	(46,873)	(72%)	**(27,588)**	(93,390)	(70%)
Revenue	**123,263**	279,679	(56%)	**229,808**	558,396	(59%)

The decrease in sales for the three and six months ended June 30, 2015 is primarily due to lower realized commodity prices and the decrease in sales volumes. The table below summarizes these changes:

Reconciliation of Changes in Sales

Three months ended June 30, 2014	326,552
Sales volumes	(44,959)
Realized prices	(145,328)
Three months ended June 30, 2015	**136,265**
$ change in sales	(190,287)
% change in sales	(58%)

Reconciliation of Changes in Sales

Six months ended June 30, 2014	651,786
Sales volumes	(74,152)
Realized prices	(320,238)
Three months ended June 30, 2015	**257,396**
$ change in sales	(394,390)
% change in sales	(61%)

Net Realized Prices

	Three months ended June 30,			Six months ended June 30,		
	2015	2014	Change	**2015**	2014	Change
Oil and natural gas sales	**136,265**	326,552	(58%)	**257,396**	651,786	(61%)
Transportation expense	**872**	1,891	(54%)	**1,806**	3,636	(50%)
Total sales, net of transportation expense	**135,393**	324,661	(58%)	**255,590**	648,150	(61%)
Gross sales ($/boe)	**46.84**	84.41	(45%)	**42.37**	83.30	(49%)
Transportation expense ($/boe)	**0.30**	0.49	(39%)	**0.30**	0.46	(35%)
Realized price, net of transportation expense ($/boe)	**46.54**	83.92	(45%)	**42.07**	82.84	(49%)

Net realized price decreased for the three and six months ended June 30, 2015 primarily due to lower liquids pricing. Transportation expense decreased for the three and six months ended June 30, 2015, both on a unit of production and total basis, as a result of lower oil production and the disposition of southeast Saskatchewan conventional oil producing assets in Q3 2014.

Royalties

	Three months ended June 30,			Six months ended June 30,		
	2015	2014	Change	**2015**	2014	Change
Royalties [(1)]	**13,002**	46,873	(72%)	**27,588**	93,390	(70%)
$ per boe	**4.47**	12.12	(63%)	**4.54**	11.93	(62%)
Royalties % [(2)]	**10%**	14%	—	**11%**	14%	—

(1) Royalties include the Saskatchewan Resource Surcharge determined as a percentage of sales from our Saskatchewan lands.

(2) Royalties % is shown as a % of our realized price, net of transportation costs.

Royalties decreased for the three and six months ended June 30, 2015, on both a total and unit of production basis, commensurate with the decrease in revenues and a lower royalty rate. The decrease in royalty rate is primarily driven by lower pricing offset somewhat by the expiry of royalty incentives on Cardium wells that have exceeded the number of new wells qualifying for the royalty incentive. On Crown lands in Saskatchewan, the first 37,740 boe of production from horizontal wells receive a royalty incentive but incur the Saskatchewan Resource Surcharge of 1.7%. On Crown lands in Alberta, horizontal oil wells are subject to a maximum 5% royalty rate for 12 to 48 months or 50,000 to 100,000 boe of production, whichever comes first, depending on well length.

Gain (Loss) on Risk Management Contracts

Lightstream enters into commodity price derivative contracts to limit exposure to declining commodity prices, thereby protecting project economics and providing increased stability of cash flows and capital expenditure programs. Commodity prices fluctuate for a number of reasons, including changes in economic conditions, political events, weather conditions and changes in supply or demand. The Company's risk management activities are conducted pursuant to the Company's risk management policies that have been approved by the Board of Directors.

Lightstream enters into foreign exchange contracts to limit exposure to variability in exchange rates on U.S. dollar interest payments on the senior unsecured notes and convertible debentures, thereby providing increased stability of cash flows.

Our financial commodity derivative contracts that are option-based contracts have their fair value, at a particular point in time, impacted by underlying commodity prices, expected commodity price volatility and the duration of the contract. The fair value of our fixed price derivative contracts at a particular point in time is determined by the expected future settlements of the underlying commodity. The fair value of these contracts represents the estimated amount that would be received for settling Lightstream's outstanding contracts on June 30, 2015, and will be different than what will eventually be realized.

The gain or loss on risk management contracts is comprised of two components; the realized component reflects actual settlements that occurred during the period, and the unrealized component represents the change in the fair value of contracts during the period. The realized gain on risk management contracts for the three and six months ended June 30, 2015 was primarily driven by settlements on our WTI oil derivative contracts. The unrealized loss on risk management contracts for the three and six months ended June 30, 2015 resulted primarily from an increase in expected future WTI oil prices as compared to March 31, 2015 or December 31, 2014.

	Three months ended June 30,			Six months ended June 30,		
	2015	2014	Change	**2015**	2014	Change
Realized gain (loss):						
Crude oil derivative contracts	**19,457**	(2,159)	—	**47,810**	(2,579)	—
Natural gas derivative contracts	**12**	(607)	—	**12**	(2,005)	—
Foreign exchange contracts	**(2)**	72	—	**1,487**	995	49%
	19,467	(2,694)	—	**49,309**	(3,589)	—
Unrealized gain (loss):						
Crude oil derivative contracts	**(37,074)**	(9,874)	275%	**(45,576)**	(14,830)	207%
Natural gas derivative contracts	**62**	1,296	(95%)	**62**	(977)	—
Foreign exchange contracts	**262**	(889)	—	**295**	(1,057)	—
	(36,750)	(9,467)	288%	**(45,219)**	(16,864)	168%
Gain (loss) on risk management contracts	**(17,283)**	(12,161)	42%	**4,090**	(20,453)	—

Commodity Contracts

At June 30, 2015, Lightstream recorded a $21.2 million asset (December 31, 2014 - $66.7 million asset) related to its commodity price risk management contracts. The following is a summary of crude oil derivatives as of the date of this MD&A:

Crude Oil Price Risk Management Contracts – WTI(1)

Remaining Term	Volume (bopd)	Average Price ($/bbl) (1)	Type
Jul. 2015 – Dec. 2015	4,796	US$80.52 floor/US$103.35 ceiling	Costless Collar
Jul. 2015 - Dec. 2015	1,500	US$56.45	Fixed Price Swap

(1) Prices are the volume weighted average prices for the period.

The following is a summary of natural gas derivatives as of the date of this MD&A:

Remaining Term	Volume (GJ/d)	Average Price ($/GJ) (1)	Type
Jul. 2015 - Dec. 2015	1,000	$2.86	Fixed Price Swap
Jan. 2016 - Dec. 2016	4,000	$2.92	Fixed Price Swap

(1) Prices are the volume weighted average prices for the period.

Foreign Exchange Contracts

At June 30, 2015, Lightstream recorded a $0.3 million asset (December 31, 2014 - $nil) related to foreign exchange risk management contracts. The following is a summary of foreign exchange contracts entered into as of the date of this MD&A:

Foreign Exchange Risk Management Contracts

Settlement	Type	Amount (US$)	Rate (US$/CDN$)
Jul. 2015	Forward	$222,548	$0.79(1)

(1) Weighted average exchange rate of multiple contracts.

Production Expenses

	Three months ended June 30,			Six months ended June 30,		
	2015	2014	Change	**2015**	2014	Change
Production expenses	**37,497**	55,352	(32%)	**77,020**	110,335	(30%)
$ per boe	**12.89**	14.31	(10%)	**12.68**	14.10	(10%)

Production expenses decreased on a total basis for the three and six months ended June 30, 2015 due primarily to lower variable production costs associated with decreased production levels. The decrease in production expenses per boe was due to lower costs related to repairs and maintenance, trucking, electricity/power and chemicals in addition to the disposition of relatively higher cost production in our southeast Saskatchewan Conventional business unit that was sold in Q3 2014.

Netbacks ($/boe)

	Three months ended June 30,			Six months ended June 30,		
	2015	2014	Change	**2015**	2014	Change
Oil, NGL and natural gas sales [1]	**46.54**	83.92	(45%)	**42.07**	82.84	(49%)
Royalties	**4.47**	12.12	(63%)	**4.54**	11.93	(62%)
Production expenses	**12.89**	14.31	(10%)	**12.68**	14.10	(10%)
Operating netback [2]	**29.18**	57.49	(49%)	**24.85**	56.81	(56%)

[1] Net of transportation expenses.

[2] Non-GAAP measure. See “Non-GAAP Measures” section within this document.

The decrease in operating netback for the three and six months ended June 30, 2015 was primarily due to lower realized oil prices, partially offset by lower royalties and production expenses.

General and Administrative Expenses

	Three months ended June 30,			Six months ended June 30,		
	2015	2014	Change	**2015**	2014	Change
General and administrative expenses	**9,491**	11,465	(17%)	**22,438**	23,107	(3%)
$ per boe	**3.26**	2.96	10%	**3.69**	2.95	25%

General and administrative expenses decreased for the three and six months ended June 30, 2015, on a total basis, due to staff reductions in the first quarter of 2015. General and administrative expenses increased for the three and six months ended June 30, 2015, on a unit of production basis, due to lower production levels.

Share-based Compensation

	Three months ended June 30,			Six months ended June 30,		
	2015	2014	Change	**2015**	2014	Change
Share-based compensation	**2,083**	3,877	(46%)	**3,494**	8,529	(59%)

Share-based compensation expense relates to stock options, deferred common shares and incentive shares granted. The calculation of this non-cash expense is based on the fair value of the share-based compensation issued, amortized over the vesting period of the option and incentive share or immediately upon grant of the deferred common share.

The decrease in share-based compensation for the three and six months ended June 30, 2015 is due to fewer new option, incentive share and deferred common share grants, an increased number of older share-based awards that have fully vested and the reversal of previously recognized compensation expense upon cancellation of share-based awards as a result of staff reductions.

Gain (Loss) on Dispositions

	Three months ended June 30,			Six months ended June 30,		
	2015	2014	Change	**2015**	2014	Change
Gain (loss) on dispositions	**556**	13,141	(96%)	**(1,332)**	40,919	—

The gain on dispositions for the three months ended June 30, 2015 includes $0.2 million from the disposal of non-core assets in our Alberta/BC business unit during Q2 2015 and $0.4 million of adjustments to other non-core asset dispositions, including $0.3 million from the royalty and fee title asset disposition that occurred in Q1 2015. The loss on dispositions for the six months ended June 30, 2015 includes $0.7 million from the disposition of royalty and fee title assets in our Alberta/BC business unit in Q1 2015 for gross proceeds of $12.4 million and $0.6 million of net adjustments to other non-core asset dispositions that occurred in 2014 and 2015. The gain on dispositions for both the three and six months ended June 30, 2014 related to the sale of non-core properties for total gross proceeds of $253 million.

Gain (Loss) on Long-term Investments

	Three months ended June 30,			Six months ended June 30,		
	2015	2014	Change	**2015**	2014	Change
Gain (loss) on long-term investments	**(250)**	1,162	—	**(416)**	(83)	401%

Long-term investments are held at fair value and the loss represents the change in value based on the quoted market share price. The loss on long-term investments for the three and six months ended June 30, 2015 reflects a lower average market closing price of the investments at June 30, 2015 as compared to December 31, 2014.

Interest and Other Expense

	Three months ended June 30,			Six months ended June 30,		
	2015	2014	Change	**2015**	2014	Change
Interest on unsecured termed debt	**21,309**	21,219	—	**42,790**	42,332	1%
Interest on secured termed credit facility and other	**6,474**	9,655	(33%)	**11,979**	20,306	(41%)
Cash Interest and other	**27,783**	30,874	(10%)	**54,769**	62,638	(13%)
Accretion on unsecured termed debt	**850**	789	8%	**1,698**	1,561	9%
Accretion of decommissioning liability	**1,317**	1,488	(11%)	**2,465**	3,193	(23%)
Amortization of deferred financing costs	**459**	403	14%	**852**	814	5%
Other	**—**	7	(100%)	**(421)**	4	—
Interest and other expense	**30,409**	33,561	(9%)	**59,363**	68,210	(13%)

Unsecured termed debt includes the senior unsecured notes and convertible debentures which are denominated in U.S. dollars. Interest and accretion are translated to Canadian dollars using the average foreign exchange rate for the period. Interest expense on unsecured termed debt was essentially unchanged for the three and six months ended June 30, 2015 as the reduction in interest costs from the repurchase of US$100 million principal amount of senior unsecured notes during the second half of 2014 was offset by the impact of a weaker Canadian dollar relative to the U.S. dollar.

Interest expense on the secured termed credit facility ("Credit Facility") includes interest on debt, stand-by fees, and fees on letters of credit. Interest expense on the Credit Facility decreased for the three and six months ended June 30, 2015 as the Credit Facility was paid down throughout 2014 using proceeds from our 2014 asset disposition program. The average Credit Facility balance outstanding for Q2 2015 was $640 million compared to $1,009 million in Q2 2014, and $629 million for the first six months of 2015 compared to $1,078 million for the first six months of 2014.

Foreign Exchange Gain (Loss)

	Three months ended June 30,			Six months ended June 30,		
	2015	2014	Change	**2015**	2014	Change
Unrealized foreign exchange gain (loss)	**16,474**	33,415	(51%)	**(69,005)**	(3,499)	1,872%
Realized foreign exchange gain (loss)	**(123)**	(227)	(46%)	**(3,651)**	(2,657)	37%
Foreign exchange gain (loss)	**16,351**	33,188	(51%)	**(72,656)**	(6,156)	1,080%

The Company recognizes foreign exchange gains/losses primarily due to the appreciation/depreciation of the Canadian dollar relative to the U.S. dollar. Our senior unsecured notes and convertible debentures are denominated in U.S. dollars and, as a result, the majority of unrealized foreign exchange gains or losses relate to the change in the foreign exchange rate compared to the rate at the end of the previous period. A stronger Canadian dollar at June 30, 2015 compared to March 31, 2015 resulted in a foreign exchange gain for Q2 2015. A weaker Canadian dollar at June 30, 2015 compared to December 31, 2014 resulted in an unrealized foreign exchange loss during the first six months of 2015. The realized foreign exchange loss in the first six months of 2015 resulted from settlement of the U.S. denominated interest obligations on the senior unsecured notes and convertible debentures and was partially mitigated by a $1.5 million realized gain on foreign exchange hedges.

Depletion and Depreciation ("D&D")

	Three months ended June 30,			Six months ended June 30,		
	2015	2014	Change	**2015**	2014	Change
Depletion and depreciation	**87,008**	121,408	(28%)	**180,334**	243,159	(26%)
$ per boe	**29.91**	31.38	(5%)	**29.69**	31.07	(4%)

D&D expense decreased for the three and six months ended June 30, 2015, on both a total and unit of production basis, due to lower production volumes and a lower cost base from asset dispositions and impairment in the fourth quarter of 2014.

Income Tax Expense (Recovery)

	Three months ended June 30,			Six months ended June 30,		
	2015	2014	Change	**2015**	2014	Change
Income tax expense (recovery)	**6,810**	19,260	(65%)	**(6,687)**	33,050	—

Income tax expense (recovery) for the three and six months ended June 30, 2015 relates to the non-cash change in the Company's deferred tax liabilities. The income tax recovery for the six months ended June 30, 2015 resulted from a net loss compared to an income tax expense on net income in the comparative period and the

increased impact of non-deductible unrealized foreign exchange gains/losses. The income tax expense for the three months ended June 30, 2015 arises from the increase in the Alberta provincial corporate tax rate from 10% to 12% effective July 1, 2015, resulting in an increase in the Company's deferred tax liability. The Company's normalized effective tax rate for the second quarter of 2015 is 26% (Q2 2014 - 26%), after excluding non-deductible permanent differences such as unrealized foreign exchange gains/losses and share based compensation.

Net Income (Loss)

As summarized in the table below, the net loss in Q2 2015 compared to net income in Q2 2014 is primarily due to lower realized prices, lower sales volumes, a smaller foreign exchange gain and a smaller gain on asset dispositions, partially offset by lower royalties, lower production expenses, lower depletion and depreciation and lower income tax expense.

The net loss in the first six months of 2015 compared to net income in the first six months of 2014 is primarily due to lower realized prices, lower sales volumes, a larger unrealized foreign exchange loss and a loss on dispositions compared to a gain previously, partially offset by lower royalties, lower production expenses, a gain on risk management contracts compared to a loss previously, an income tax recovery and lower depletion and depreciation.

Reconciliation of Changes in Net Loss

	Three months ended June 30,	Six months ended June 30,
Net income: June 30, 2014	68,195	82,597
Increase (decrease) due to:		
Sales volumes	(44,959)	(74,152)
Realized prices	(145,328)	(320,238)
Royalties	33,871	65,802
Gain (loss) on risk management contracts	(5,122)	24,543
Production expenses	17,855	33,315
Gain (loss) on disposition of assets	(12,585)	(42,251)
Interest and other	3,152	8,847
Foreign exchange (gain) loss	(16,837)	(66,500)
Depletion and depreciation	34,400	62,825
Income taxes	12,450	39,737
Other [1]	3,375	7,201
Net loss: June 30, 2015	**(51,533)**	**(178,274)**

(1) Includes transportation expense, share-based compensation, general and administrative expense, gain (loss) on long-term investments, and gain (loss) on derivative financial liability.

Funds Flow from Operations

The decrease in funds flow from operations for Q2 2015 from Q2 2014 and for the first six months of 2015 compared to the same period in 2014 is due to lower realized prices and sales volumes, partially offset by a gain on realized risk management contracts, lower royalties and production expenses.

Reconciliation of Changes in Funds Flow From Operations

	Three months ended June 30,	Six months ended June 30,
Funds flow from operations: June 30, 2014	177,034	352,004
Increase (decrease) due to:		
Sales volumes	(44,959)	(74,152)
Realized prices	(145,328)	(320,238)
Royalties	33,871	65,802
Production expenses	17,855	33,315
Cash interest expense	3,091	7,869
Realized gain on risk management contracts	22,161	52,898
Other [1]	3,241	1,396
Funds flow from operations: June 30, 2015	**66,966**	**118,894**

(1) Includes transportation expenses, cash general and administrative expense, realized FX gain (loss), and decommissioning liabilities settled.

Capital Expenditures

	Three months ended June 30,			Six months ended June 30,		
	2015	2014	Change	**2015**	2014	Change
Drilling, completions, equipping and recompletions	**8,237**	38,533	(79%)	**59,426**	208,040	(71%)
Land	**589**	1,744	(66%)	**1,111**	2,951	(62%)
Facilities	**8,176**	16,921	(52%)	**15,365**	39,697	(61%)
Seismic	**53**	233	(77%)	**(991)**	604	(264%)
Other	**3,120**	3,818	(18%)	**5,518**	9,240	(40%)
Capital expenditures before acquisitions[1]	**20,175**	61,249	(67%)	**80,429**	260,532	(69%)
Asset acquisitions[2] [3]	**84**	390	(78%)	**84**	3,851	(98%)
Proceeds from dispositions[3]	**(1,935)**	(138,813)	(99%)	**(13,258)**	(255,954)	(95%)
Net capital expenditures	**18,324**	(77,174)	(124%)	**67,255**	8,429	698%

(1) Includes exploration and evaluation expenditures for the three and six months ended June 30, 2015 of $nil (2014 - $0.7 million) and $0.1 million (2014 - $1.2 million) respectively.

(2) Includes exploration and evaluation expenditures for the three and six months ended June 30, 2015 of $nil (2014 - $nil) and $nil (2014 - $1.2 million) respectively.

(3) Includes non-cash acquisitions/dispositions for the three and six months ended June 30, 2015 of $nil (2014 - $0.4 million) and $nil (2014 - $3.8 million) respectively.

Drilling Activity (Net), for the three months ended June 30,

	Net wells drilled		Net wells pending completion and/or tie-in		Dry and abandoned wells		Success Rate	
Business Unit	**2015**	2014	**2015**	2014	**2015**	2014	**2015**	2014
Bakken	**1**	—	**2**	2	**—**	—	**100%**	—
Cardium	**—**	1	**—**	1	**—**	—	**—**	100%
Alberta/BC	**—**	—	**—**	—	**—**	—	**—**	—
Total	**1**	1	**2**	3	**—**	—	**100%**	100%

Drilling Activity (Net), for the six months ended June 30,

	Net wells drilled		Net wells pending completion and/or tie-in		Dry and abandoned wells		Success Rate	
Business Unit	**2015**	2014	**2015**	2014	**2015**	2014	**2015**	2014
Bakken	**7**	14	**2**	2	**—**	—	**100%**	100%
Cardium	**8**	26	**—**	1	**—**	—	**100%**	100%
Alberta/BC	**—**	7	**—**	—	**—**	—	**—**	100%
Total	**15**	47(1)	**2**	3	**—**	—	**100%**	100%

(1) Excludes four wells drilled in the disposed Conventional Business Unit during the six months ended June 30, 2014.

Our strategy for 2015 is to adopt a conservative capital plan given the current low oil price environment with the objective of preserving our long-term value without incurring additional debt, prior to any foreign exchange translation adjustments. Capital spending during the first six months of 2015 reflects this strategy as capital expenditures of $80 million, before asset acquisitions and dispositions, were 69% lower than the $261 million spent in the first half of 2014. The majority of second quarter 2015 capital spending was focused on drilling one non-operated well in the Bakken, completing and equipping six of the seven wells that were in inventory at the end of Q1 2015 and facilities spending within our Bakken and Cardium core areas. We completed our planned 2015 operated drilling program during the first quarter of 2015 on time and within our budget. Given the encouraging results to date from the Cardium Falher gas play, we are planning to drill another operated Falher well during the second half of 2015 in order to efficiently utilize our existing gas infrastructure.

Divestiture activity during the first six months of 2015 consisted primarily of the sale of royalty and fee title assets in our Alberta/BC business unit for gross proceeds of $12.4 million in Q1 2015. Proceeds from this disposition were used to reduce our outstanding debt. We continue to look for further opportunities to divest non-core assets and remain committed to monetizing all or a portion of our Bakken business unit at an appropriate valuation.

Decommissioning Liabilities

Decommissioning liabilities decreased by $9.1 million in Q2 2015, primarily as a result of a change in the risk free discount rate to 2.25% from 2.0% in Q1 2015. Decommissioning liabilities increased by $14.3 million for the first six months of 2015, primarily as a result of a change in the risk free discount rate to 2.25% from 2.5% in Q4 2014 and, to a lesser extent from new obligations from wells drilled during the year and accretion expense. The discount rate as at June 30, 2015 was 2.25% (December 31, 2014 - 2.5%). At June 30, 2015, the decommissioning liabilities were $212.7 million (December 31, 2014 - $198.4 million).

SUMMARY OF QUARTERLY RESULTS

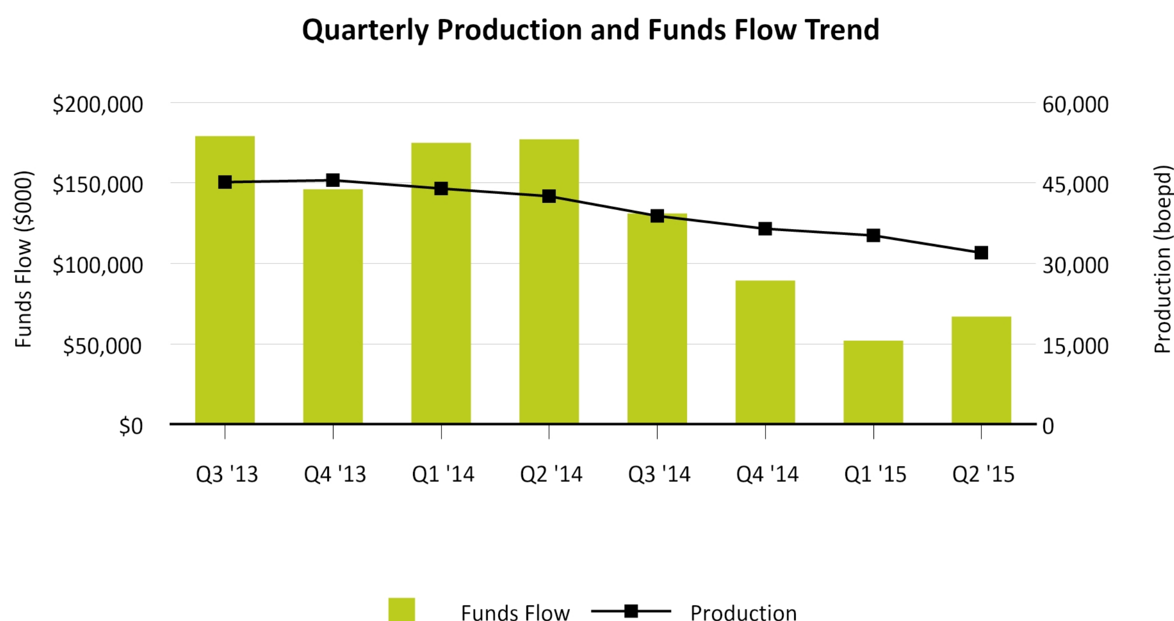
	2015		2014				2013	
	Q2	**Q1**	Q4	Q3	Q2	Q1	Q4	Q3
Financial ($000s except where noted)								
Total debt [1]	**1,668,123**	**1,731,248**	1,646,862	1,557,817	1,985,342	2,248,702	2,274,122	2,195,808
Capital expenditures[2]	**20,175**	**60,254**	121,124	90,164	61,249	199,283	155,933	141,124
Net capital expenditures [1]	**18,324**	**48,931**	123,194	(372,259)	(77,174)	85,603	154,487	139,212
Dividends [1]	**—**	**—**	19,247	24,370	24,351	24,298	40,320	47,876
Per share [1]	**—**	**—**	0.10	0.12	0.12	0.12	0.20	0.24
Cash dividends [1]	**—**	**—**	19,247	24,370	24,351	24,298	33,983	32,189
Per share [1]	**—**	**—**	0.10	0.12	0.12	0.12	0.17	0.16
Payout ratio (%)[1]	**—**	**—**	22	19	14	14	28	27
Cash payout ratio (%) [1]	**—**	**—**	22	19	14	14	23	18
Oil and natural gas sales	**136,265**	**121,131**	186,861	269,177	326,552	325,234	287,727	331,814
Adjusted net income (loss)	**(51,533)**	**(127,162)**	160,386	6,935	68,202	14,399	(45,598)	52,031
Per share – basic[1]	**(0.26)**	**(0.64)**	0.81	0.03	0.34	0.07	(0.23)	0.26
Per share – diluted[1][3]	**(0.26)**	**(0.64)**	0.80	0.03	0.34	0.07	(0.23)	0.26
Funds flow from operations	**66,966**	**51,928**	89,278	130,950	177,034	174,970	146,017	179,713
Per share – basic[1]	**0.34**	**0.26**	0.45	0.65	0.88	0.88	0.73	0.91
Per share – diluted[1][3]	**0.34**	**0.26**	0.44	0.64	0.87	0.86	0.72	0.90
Operations								
Oil equivalent sales price ($/boe)[4]	**46.54**	**37.96**	55.38	74.84	83.92	81.77	68.29	79.36
Royalties	**4.47**	**4.61**	8.76	11.32	12.12	11.76	10.11	11.36
Production expenses	**12.89**	**12.48**	13.47	14.85	14.31	13.90	12.75	13.25
Operating netback[1][4]	**29.18**	**20.87**	33.15	48.67	57.49	56.11	45.43	54.75
Average daily production								
Crude oil and NGL's (bbls)	**23,066**	**26,607**	27,299	30,203	34,128	35,209	36,421	35,445
Natural gas (Mcf)	**53,399**	**51,429**	55,037	51,802	50,309	52,503	54,600	58,290
Total (boe)[5]	**31,966**	**35,179**	36,472	38,837	42,513	43,960	45,521	45,160

(1) Non-GAAP measure. See "Non-GAAP Measures" section within the MD&A.
(2) Prior to asset acquisitions and dispositions.
(3) Includes common shares, stock options, deferred common shares and incentive shares on the same basis as net income. Convertible debentures have been included as at the period end date based on the stated conversion price as of that date.
(4) Net of transportation expenses.
(5) Six Mcf of natural gas is equivalent to one barrel of oil equivalent.

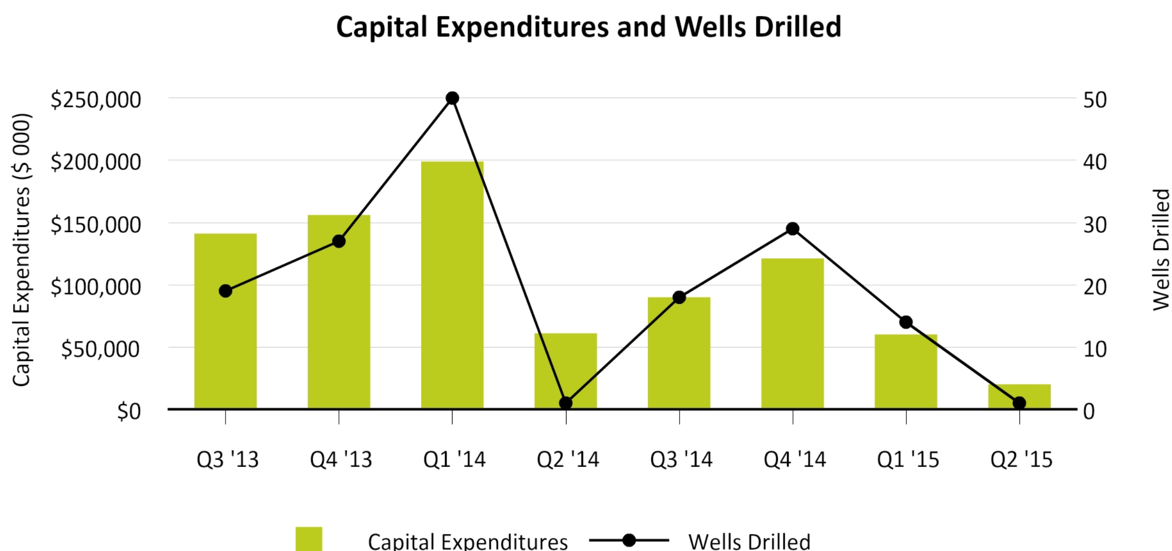
MANAGEMENT'S DISCUSSION AND ANALYSIS

Significant factors influencing quarterly results were:

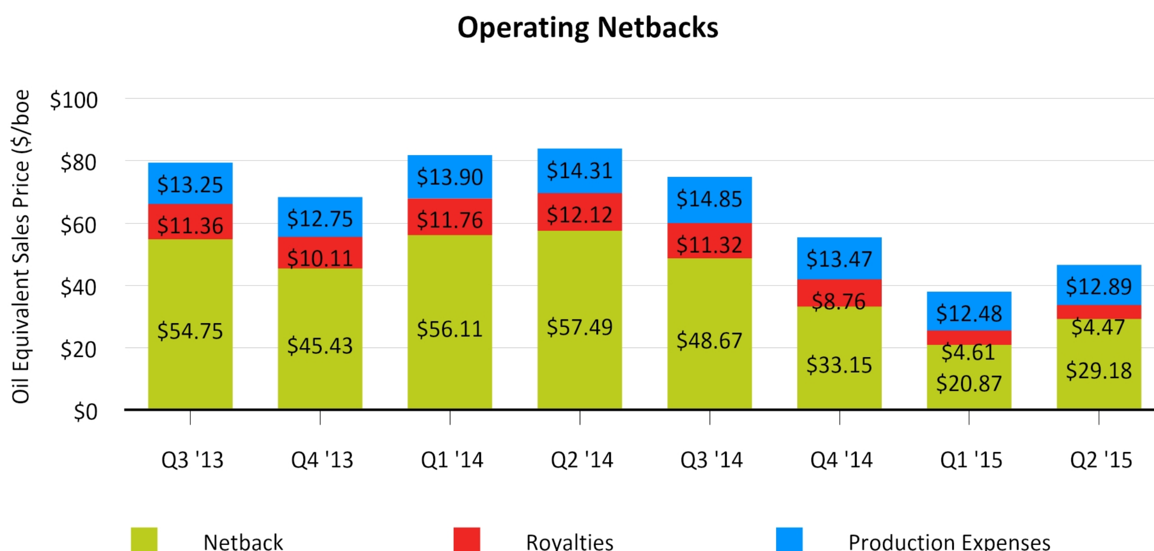
- Production has decreased since Q1 2014 as we executed our divestiture plan and reduced the amount of capital spending on new wells. The attenuation in the level of capital spending over that time has resulted in natural declines exceeding new production.
- Funds flow from operations is primarily impacted by variability in production levels and operating netback. Funds flow from operations decreased from Q2 2014 to Q1 2015, both on a total dollar and per share basis, due to the decrease in production combined with significantly lower realized prices. The decrease in realized pricing is primarily driven by lower WTI prices, which decreased from an average of US$102.99 in the second quarter of 2014 to an average of US$48.56 in the first quarter of 2015. That trend was interrupted in Q2 2015, as funds flow from operations increased due to higher WTI prices that averaged US$57.94 in the second quarter of 2015.



- Both capital expenditures and the number of wells drilled in the second quarter of 2015 were the lowest since Q2 2014, which is indicative of our conservative capital spending program in 2015 as a result of the current low oil price environment. During the second quarter of 2015, capital expenditures were $20 million, representing our lowest spending quarter in the past eight quarters. We drilled one non-operated well during Q2 2015, as our operated well drilling program was largely completed in Q1 2015.



- Second quarter 2015 operating netback of $29.18/boe increased 40% over $20.87/boe in Q1 2015 but remained lower than previous quarters due to the significant drop in commodity prices. Royalties per boe are at historically low levels consistent with lower realized pricing and reduced revenues. Production expenses per boe increased slightly in Q2 2015 over Q1 2015 but remain low due to reduced variable production costs resulting from lower production and the sale of higher cost production in 2014.



COMMITMENTS

The following is a summary of the estimated costs required to fulfill the Company's remaining contractual commitments at June 30, 2015:

Type of commitment	1 Year	2-3 Years	4-5 Years	Thereafter	Total
Office leases [1]	$ 6,093	$ 19,034	$ 9,734	$ 2,163	**$ 37,024**
Other	157	—	—	—	**157**
Total	**$ 6,250**	**$ 19,034**	**$ 9,734**	**$ 2,163**	**$ 37,181**

(1) Includes sublease recoveries of $1.3 million (1 Year), $1.0 million (2-3 Years).

LIQUIDITY AND CAPITAL RESOURCES

Since inception, Lightstream's long-term business strategy has been to provide a reasonable dividend yield to shareholders combined with an accretive long-term growth-oriented business plan. We remain focused on securing appropriate levels of capitalization to support this business strategy. As commodity prices fluctuate, we have the ability to alter our capital program and/or dividend payments in order to adjust debt levels. As a result of the recent decline in oil prices, we have taken steps to preserve our financial flexibility and future asset value by reducing our capital program and suspending our dividend with the objective of ensuring our expenditures will be funded through cash flow, without an increase to overall debt levels prior to any foreign exchange translation adjustments to our U.S. dollar denominated debt. We will continue to monitor our plans and forecasts and make further adjustments as required in order to reduce levels of capitalization while adhering to our long-term business strategy.

During the second quarter of 2015, we renegotiated the terms on our Credit Facility resulting in the implementation of a borrowing base structure and amendments to our covenants. At June 30, 2015, the Company had a secured termed credit facility with a syndicate of lenders in the amount of $750 million, subject to borrowing base re-determinations on a semi-annual basis, and a maturity date of June 2, 2017, subject to further extension. During the term of the facility, the Company will not pay cash dividends without unanimous consent of the lenders. The Credit Facility has a single covenant that limits the ratio of facility borrowing to trailing twelve month Adjusted EBITDA to:

January 1, 2015 - September 30, 2015 - 3.0x

October 1, 2015 - June 30, 2016 - 3.75x

July 1, 2016 - December 31, 2016 - 4.25x

January 1, 2017 - June 2, 2017 - 4.0x

The Company is in compliance with this covenant. As at June 30, 2015, Lightstream had $626 million drawn on this facility. The amended Credit Facility is expected to provide an appropriate level of liquidity and covenant relief during the current low-price commodity environment. Subsequent to June 30, 2015, we reduced the amount outstanding under our Credit Facility by approximately $250 million through the issuance of US$200 million of second lien notes ("Secured Notes") for cash proceeds. Upon closing of this transaction, the credit available under our facility was approximately $375 million.

At June 30, 2015, the Company had US$800 million of senior unsecured notes ("Unsecured Notes") outstanding. The Unsecured Notes bear interest at a rate of 8.625% per annum and mature February 1, 2020. The Unsecured Notes contain covenants that could limit the Company's ability to issue additional debt, pay dividends, and repurchase stock, among other restrictions. The Company is in compliance with all of these covenants.

Subsequent to June 30, 2015, the Company entered into privately negotiated transactions involving the exchange of existing Unsecured Notes for Secured Notes. On July 2, 2015, we issued US$395 million of Secured Notes in exchange for US$465 million of Unsecured Notes, which were cancelled. On August 4, 2015, a further US$54.8 million of Secured Notes were issued in exchange for US$81 million of Unsecured Notes, which were cancelled. The Secured Notes bear interest at 9.875% per annum and mature June 15, 2019. The Secured Notes are secured by second-priority liens on all of Lightstream's assets which rank behind the security under our Credit Facility.

As at June 30, 2015, Lightstream had convertible debentures outstanding of US$4.5 million with an annual coupon of 3.125%. The convertible debentures have a financial covenant that limits the amount of security and encumbrances to 35% of our total assets. The Company is in compliance with this covenant. During the first quarter of 2015, we repurchased US$2 million principal amount of outstanding convertible debentures for an aggregate purchase price of US$1.6 million, including accrued interest. The repurchased debentures were retired.

In addition to the liquidity noted above, other possible sources of funds available to Lightstream include the following:

- Funds flow from operations;
- Sale of producing or non-producing assets (including joint venture structures). Cash generated from a sale may be reduced by any required debt repayments;
- Further adjustments to capital program;
- Monetization of any risk management assets;
- Issuance of additional subordinated or convertible debt;
- Issuance of equity.

We expect to satisfy ongoing working capital requirements with funds flow from operations and available credit.

Capital Plan

The $100 - $120 million capital plan for 2015 is expected to be funded through internally generated cash flow and is focused on the continued development of our Cardium oil properties in central Alberta and our Bakken light oil properties in southeast Saskatchewan, through new well drilling and the optimization of existing wells. Our 2015 operated drilling program was largely completed in Q1 2015 and we expect minimal operated new well activity throughout the remainder of the year. Based on our guidance, we expect to continue generating cash in excess of capital expenditures and look to further reduce debt levels over the second half of 2015.

Dividends

The Company paid a monthly dividend of $0.04 per share or $0.48 per share per annum from January 2014 to November 2014, which was then reduced to $0.015 per share or $0.18 per share per annum for the month of December 2014. Subsequent to December 31, 2014, the dividend was suspended to help preserve the financial flexibility of the Company.

Transactions with Related Parties

Petrobank Energy Resources Ltd. ("Petrobank") was considered a related party until April 30, 2014, as both companies had the same Chief Executive Officer.

In the three and six months ended June 30, 2015, Lightstream had no related party transactions with Petrobank. In the three and six months ended June 30, 2014, Petrobank purchased natural gas from Lightstream at market prices for $0.2 million and $0.4 million respectively. In the three and six months ended June 30, 2014, Lightstream received $nil and $0.1 million in management fees respectively, provided for certain executive functions and legal services.

Summary of Quarterly Results

Below is the summary of quarterly results of the Company:

	2015		2014				2013	
	Q2	**Q1**	Q4	Q3	Q2	Q1	Q4	Q3
Financial ($000s except where noted)								
Oil and natural gas sales	**136,265**	**121,131**	186,861	269,177	326,552	325,234	287,727	331,814
Net Income (loss) [1]	**(51,533)**	**(126,741)**	(532,560)	3,891	68,195	14,402	(1,387,533)	52,044
Per share – basic	**(0.26)**	**(0.64)**	(2.68)	0.02	0.34	0.07	(6.98)	0.26
Per share – diluted[2]	**(0.26)**	**(0.64)**	(2.68)	0.02	0.34	0.07	(6.98)	0.26

(1) Amounts are stated in Canadian dollars and have been prepared in accordance with IFRS.

(2) Includes common shares, stock options, deferred common shares, and incentive shares on the same basis as net income.

Over the past eight quarters, the Company's oil and gas sales have fluctuated primarily due to changes in production levels, the C$WTI benchmark price and corporate oil price differentials.

Net income (loss) has fluctuated primarily due to changes in funds flow from operations, unrealized derivative gains and losses, gains and losses on asset dispositions, unrealized foreign exchange gains and losses related to the Company's unsecured termed debt, gains and losses on long-term investments and impairments recorded in the fourth quarter of 2014 and 2013.

Outstanding Share Data

As at the date of this MD&A, there are 197.6 million Lightstream common shares outstanding, 0.8 million stock options, 4.0 million incentive shares and 0.6 million deferred common shares outstanding.

Risks and Uncertainties

There have been no significant changes in the six months ended June 30, 2015 to the risk and uncertainties identified in the MD&A for the year ended December 31, 2014.

Sensitivities

Lightstream's earnings and funds flow from operations are sensitive to changes in crude oil and natural gas prices, exchange rates and interest rates.

The following factors demonstrate the expected impact on annualized before tax funds flow from operations excluding the effect of risk management activities impacting 2015:

Change of:		(millions)
Crude oil	US$1.00/bbl WTI reference price (assuming 23,000 bopd)	**$8.7**
	1,000 bopd of production @ US$52.50/bbl WTI	**$17.6**
Natural gas	$0.10/Mcf AECO reference price (assuming 53 MMcf/d)	**$1.8**
	1.0 MMcf per day of production @ $3.00/Mcf AECO	**$0.8**
Currency	US$0.01 in exchange rate	**$2.6**
Interest rate	1% in interest rate (assuming $626 million of floating rate debt)	**$6.3**

Critical Accounting Estimates

There have been no changes to the Company's critical accounting policies and estimates in the three and six months ended June 30, 2015.

Changes in Accounting Policies

There have been no significant changes to the Company's accounting policies for the three and six months ended June 30, 2015.

Policies

Internal Control over Financial Reporting

Lightstream is required to comply with National Instrument 52-109 "Certification of Disclosure in Issuers' Annual and Interim Filings". The certification of interim filings for the interim period ended June 30, 2015 requires that Lightstream disclose in the interim MD&A any changes in Lightstream's internal control over financial reporting that occurred during the period that have materially affected, or are reasonably likely to materially affect, Lightstream's internal control over financial reporting. Lightstream confirms that no such changes were made to its internal controls over financial reporting during the three months ended June 30, 2015.

Non-GAAP Measures

Funds flow from operations, funds flow per share, adjusted net income, adjusted net income per share, dividends paid, dividends paid per share, cash dividends paid, cash dividends paid per share, payout ratio, cash payout ratio, total debt, operating netback, net capital expenditures, and sustainability ratio do not have standardized meanings and are therefore unlikely to be comparable to similar measures presented by other companies.

***Funds flow from operations** reflects cash generated from operating activities from continuing operations before changes in non-cash working capital. Funds flow per share is calculated as funds flow from operations divided by the weighted average number of shares outstanding for the period.*

The following table reconciles cash flow from operating activities to funds flow from operations:

	Three months ended June 30, 2015	Three months ended June 30, 2014	Six months ended June 30, 2015	Six months ended June 30, 2014
Cash flow from operating activities	**$ 72,246**	$ 213,922	**$ 111,446**	$ 347,464
Adjustments:				
Changes in non-cash working capital	**(5,280)**	(36,888)	**7,448**	4,540
Funds flow from operations:	**$ 66,966**	$ 177,034	**$ 118,894**	$ 352,004
Weighted Average shares outstanding - basic	**197,470**	200,060	**197,406**	199,958
Weighted Average shares outstanding - diluted[1]	**198,031**	203,661	**197,725**	203,445

(1) Includes dilution impact of convertible debentures

Adjusted net income *is determined by adding back to net income from continuing operations any losses or deducting any gains on the derivative financial liability, adding back any losses or deducting any gains on settlement of convertible debentures, and adding back impairments. Adjusted net income per share is calculated as adjusted net income divided by the weighted average number of shares outstanding for the period.*

Dividends *paid are total declared dividends paid by Lightstream. Dividends paid per share reflect total declared dividends paid divided by the total shares outstanding.*

Cash dividends *paid are total dividends paid in cash by Lightstream. Cash dividends paid per share reflects cash dividends paid divided by the total shares outstanding.*

Payout ratio *is determined as declared dividends paid as a percentage of funds flow from operations.*

Cash payout ratio *is determined as cash dividends paid as a percentage of funds flow from operations.*

Management considers funds flow from operations, funds flow per share, adjusted net income, adjusted net income per share, dividends paid, dividends paid per share and payout ratio important as they help to evaluate performance and demonstrate the ability to generate sufficient cash to fund future growth opportunities, pay dividends and repay debt.

EBITDA *is defined as earnings before interest, taxes, depletion and depreciation, and other non-cash items. This measure is used to evaluate compliance with certain financial covenants.*

Total debt *includes credit facility outstanding plus accounts payable less accounts receivable and prepaid expense plus the full value outstanding on the senior unsecured notes and convertible debentures converted to Canadian dollars at the exchange rate on the period end date less the value of long-term investments.*

Total debt is used to evaluate Lightstream's financial leverage.

As at,	June 30, 2015	December 31, 2014
Secured termed credit facility	$ 625,958	$ 572,495
Working capital deficiency:		
Accounts payable and accrued liabilities	130,738	253,320
Accounts receivable	(82,373)	(105,333)
Prepaid expenses	(9,150)	(7,861)
Senior unsecured notes[(1)]	997,864	928,028
Convertible debentures[(1)]	5,613	7,541
Long-term investments	(527)	(1,328)
Total Debt	$ 1,668,123	$ 1,646,862

(1) Converted using US$/CDN$ period end exchange rate of 0.79 at June 30, 2015 (December 31, 2014 - 0.86).

Operating netback *reflects revenues less royalties, transportation costs and production expenses divided by production for the period. Operating netback demonstrates profitability relative to commodity prices per unit of production.*

Net capital expenditures *represent capital expenditures from continuing operations, including exploration and evaluation expenditures and asset acquisitions, less proceeds from asset dispositions from continuing operations.*

Sustainability Ratio *is a comparison of a company's annual cash outflows (capital investment, prior to acquisitions and dispositions, and cash dividends) to its annual cash inflows (funds flow) and is used by the Company to assess the appropriateness of its dividend level and the long-term ability to fund its development plan.*

Forward-Looking Statements

Certain information provided in this MD&A constitute forward-looking statements. The use of any of the words "expect", "anticipate", "continue", "estimate", "objective", "ongoing", "may", "will", "project", "should", "believe", "plans", "intends", "strategy", and similar expressions and statements relating to matters that are not historical facts constitute forward-looking information within the meaning of applicable Canadian securities legislation.

In particular, forward-looking statements include, but are not limited to: Lightstream's guidance for 2015 as outlined under the 2015 Guidance section, including planned capital spending, production targets and anticipated product type weighting; expectations regarding realized oil and natural gas prices; proposed exploration and development activities (including the number of wells to be drilled, completed and put on production); sources of capital; expectation that funds flow will exceed capital expenditures in 2015 and plans to reduce debt with excess funds flow; anticipated impact of the use of financial commodity derivatives and foreign exchange contracts on the stability of cash flows; and a number of other matters including future results from operations; projected financial results and future capital and operating costs.

The forward-looking statements in this MD&A are based upon certain material factors and expectations and assumptions of Lightstream including, without limitation: that Lightstream will continue to conduct operations in a manner consistent with past operations; the general continuance of current industry conditions; the continuance of existing (and in certain circumstances, the implementation of proposed) tax, royalty and regulatory regimes, the accuracy of the estimates of Lightstream's reserves and resource volumes; certain

commodity price and other cost assumptions; and the continued availability of adequate financing and cash flow to fund our planned expenditures. Although Lightstream believes the material factors, expectations and assumptions on which the forward-looking statements are based are reasonable, no assurance can be given that these factors, expectations and assumptions will prove to be correct.

The forward-looking statements in this MD&A are not guarantees of future performance and should not be unduly relied upon. Such statements involve known and unknown risks, uncertainties and other factors that may cause actual results or events to differ materially from those anticipated in such forward-looking statements including, but not limited to: changes in commodity prices and exchange rates; general conditions in the oil and gas industry; operational risks in development, exploration and production; unanticipated operating results or production declines; changes in exploration or development plans; the uncertainty of oil and gas reserve estimates; increase in costs; reliance on industry partners; availability of equipment and personnel; changes in tax or environmental laws, royalty rates or other regulatory matters; increased debt levels or debt service requirements; limited, unfavorable or lack of access to capital markets; a lack of adequate insurance coverage; the impact of competition; and certain other risks detailed from time to time in Lightstream's public disclosure documents (including, without limitation, those risks set out in more detail in this MD&A and in our Annual Information Form).

The forward-looking statements contained in this MD&A speak only as of the date of this MD&A and, except as may be required by applicable securities laws, Lightstream assumes no obligation to publicly update or revise any forward-looking statements made herein or otherwise, whether as a result of new information, future events or otherwise.

Additional Information

Further information regarding Lightstream Resources Ltd., including our Annual Information Form, can be accessed under the Company's public filings found at http://www.sedar.com and on the Company's website at www.lightstreamresources.com.

INTERIM CONSOLIDATED BALANCE SHEETS

(Unaudited, thousands of Canadian dollars)

As at,	Note	June 30, 2015	December 31, 2014
Assets			
Current assets			
Accounts receivable		**$ 82,373**	$ 105,333
Prepaid expenses		**9,150**	7,861
Risk management assets	13	**22,841**	66,712
		114,364	179,906
Long-term investments		**527**	1,328
Exploration and evaluation	4	**288,915**	335,837
Property, plant and equipment	5	**3,221,004**	3,276,141
Total assets		**$ 3,624,810**	$ 3,793,212
Liabilities and Equity			
Current liabilities			
Accounts payable and accrued liabilities		**$ 130,738**	$ 253,320
Convertible debentures	7	**5,428**	—
Risk management liabilities	13	**1,348**	—
		137,514	253,320
Secured termed credit facility	6	**621,456**	568,668
Senior unsecured notes	8	**979,421**	909,402
Convertible debentures	7	**—**	7,172
Other long-term liabilities		**7,289**	8,344
Decommissioning liabilities	9	**212,665**	198,387
Deferred tax liabilities		**444,761**	451,448
		2,403,106	2,396,741
Shareholders' equity			
Shareholders' capital	10	**2,361,401**	2,358,361
Contributed surplus	10	**165,086**	164,619
Deficit		**(1,304,783)**	(1,126,509)
Total shareholders' equity		**1,221,704**	1,396,471
Total liabilities and equity		**$ 3,624,810**	$ 3,793,212

Commitments (Note 15) Subsequent events (Note 8, 12, 13, 17)
See accompanying notes to these interim consolidated financial statements.

Approved by the Board of Directors

Kenneth McKinnon
Chairman of the Board of Directors

Corey C. Ruttan
Director

FINANCIAL STATEMENTS

INTERIM CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE (LOSS) INCOME

(Unaudited, thousands of Canadian dollars, except per share amounts)

		Three months ended June 30,		Six months ended June 30,	
	Note	**2015**	2014	**2015**	2014
Revenues					
Oil and natural gas sales		**$ 136,265**	$ 326,552	**$ 257,396**	$ 651,786
Royalties		**(13,002)**	(46,873)	**(27,588)**	(93,390)
Oil and natural gas revenues		**123,263**	279,679	**229,808**	558,396
(Loss) gain on risk management contracts	13	**(17,283)**	(12,161)	**4,090**	(20,453)
		105,980	267,518	**233,898**	537,943
Expenses					
Production		**37,497**	55,352	**77,020**	110,335
Transportation		**872**	1,891	**1,806**	3,636
General and administrative		**9,491**	11,465	**22,438**	23,107
Share-based compensation	10	**2,083**	3,877	**3,494**	8,529
(Gain) loss on dispositions	5	**(556)**	(13,141)	**1,332**	(40,919)
Long-term investments loss (gain)		**250**	(1,162)	**416**	83
Interest and other	3	**30,409**	33,561	**59,363**	68,210
Foreign exchange (gain) loss		**(16,351)**	(33,188)	**72,656**	6,156
Depletion and depreciation expense	5	**87,008**	121,408	**180,334**	243,159
		150,703	180,063	**418,859**	422,296
(Loss) income before taxes		**(44,723)**	87,455	**(184,961)**	115,647
Income tax expense (recovery)		**6,810**	19,260	**(6,687)**	33,050
Net (loss) income and comprehensive (loss) income		**$ (51,533)**	$ 68,195	**$ (178,274)**	$ 82,597
Basic (loss) income per share	11	**$ (0.26)**	$ 0.34	**$ (0.90)**	$ 0.41
Diluted (loss) income per share	11	**$ (0.26)**	$ 0.34	**$ (0.90)**	$ 0.41

See accompanying notes to these interim consolidated financial statements.

FINANCIAL STATEMENTS

INTERIM CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY

(Unaudited, thousands of Canadian dollars)

	Common Shares	Contributed Surplus	Deficit	Total Shareholders' Equity
January 1, 2015	$ 2,358,361	$ 164,619	$ (1,126,509)	$ 1,396,471
Net loss	—	—	(178,274)	(178,274)
Issued under employee incentive plan	13	—	—	13
Share-based compensation	—	3,494	—	3,494
Share-based settlements	3,027	(3,027)	—	—
June 30, 2015	**$ 2,361,401**	**$ 165,086**	**$ (1,304,783)**	**$ 1,221,704**

	Common Shares	Contributed Surplus	Deficit	Total Shareholders' Equity
January 1, 2014	$ 2,386,052	$ 134,923	$ (588,171)	$ 1,932,804
Net income	—	—	82,597	82,597
Issued under employee incentive plan	91	—	—	91
Share-based compensation	—	8,529	—	8,529
Share-based settlements	5,129	(5,129)	—	—
Dividends	—	—	(48,649)	(48,649)
June 30, 2014	**$ 2,391,272**	**$ 138,323**	**$ (554,223)**	**$ 1,975,372**

See accompanying notes to these interim consolidated financial statements.

INTERIM CONSOLIDATED STATEMENTS OF CASH FLOW

(Unaudited, thousands of Canadian dollars)

	Note	Three months ended June 30, 2015	Three months ended June 30, 2014	Six months ended June 30, 2015	Six months ended June 30, 2014
Operating Activities					
Net (loss) income		**$ (51,533)**	$ 68,195	**$(178,274)**	$ 82,597
Adjusted for:					
Depletion and depreciation		**87,008**	121,408	**180,334**	243,159
Income tax expense (recovery)		**6,810**	19,260	**(6,687)**	33,050
Unrealized loss on risk management contracts	13	**36,750**	9,467	**45,219**	16,864
Unrealized foreign exchange (gain) loss		**(16,474)**	(33,415)	**69,005**	3,499
Share-based compensation	10	**2,083**	3,877	**3,494**	8,529
(Gain) loss on dispositions	5	**(556)**	(13,141)	**1,332**	(40,919)
Unrealized loss (gain) on long-term investments		**250**	(1,162)	**416**	83
Non-cash interest and other	3	**2,626**	2,687	**4,594**	5,572
Decommissioning liabilities settled	9	**2**	(142)	**(539)**	(430)
		66,966	177,034	**118,894**	352,004
Changes in non-cash working capital	14	**5,280**	36,888	**(7,448)**	(4,540)
		72,246	213,922	**111,446**	347,464
Investing Activities					
Expenditures on property, plant, and equipment	5	**(20,240)**	(60,882)	**(80,393)**	(259,673)
Exploration and evaluation expenditures	4	**(19)**	(357)	**(120)**	(914)
Proceeds from dispositions	4,5	**1,935**	138,413	**13,258**	252,158
Proceeds from disposition of long-term investments		**385**	—	**385**	—
Changes in non-cash working capital	14	**(40,461)**	(124,968)	**(90,851)**	(60,036)
		(58,400)	(47,794)	**(157,721)**	(68,465)
Financing Activities					
Issuance of shares		**9**	80	**13**	91
(Repayment) issuance of secured termed credit facility – net of costs		**(13,802)**	(141,646)	**51,936**	(230,029)
Repurchase of convertible debentures	7	**—**	—	**(2,007)**	—
Dividends paid		**—**	(24,351)	**—**	(48,649)
Changes in non-cash working capital	14	**(53)**	(211)	**(3,667)**	(412)
		(13,846)	(166,128)	**46,275**	(278,999)
Net change in cash and cash equivalents		**—**	—	**—**	—
Cash and cash equivalents, beginning of period		**—**	—	**—**	—
Cash and cash equivalents, end of period		**$ —**	$ —	**$ —**	$ —
Other cash flow information					
Cash interest paid	3	**$ 27,783**	$ 30,874	**$ 54,769**	$ 62,638

See accompanying notes to these interim consolidated financial statements.

Note 1 – Corporate Information and Basis of Presentation

Corporate Information

Lightstream Resources Ltd. ("Lightstream" or the "Company"), is a Canadian corporation with shares listed on the Toronto Stock Exchange ("TSX"). The records office and principal address is located at 2800, 525 -8th Avenue SW, Calgary, Alberta T2P 1G1.

The Company is principally engaged in the exploration and development of oil and natural gas in western Canada.

Basis of Presentation and Statement of Compliance

The interim consolidated financial statements for Lightstream as at June 30, 2015 and for the three and six months ended June 30, 2015 and 2014 should be read in conjunction with the audited consolidated financial statements as at and for the year ended December 31, 2014. The interim consolidated financial statements are prepared using the same accounting policies and methods of computation as disclosed in the annual consolidated financial statements.

The interim consolidated financial statements are stated in Canadian dollars and have been prepared in accordance with International Financial Reporting Standards ("IFRS") applicable to the presentation of interim financial statements and in accordance with International Accounting Standards ("IAS") 34 *Interim Financial Reporting*.

These interim consolidated financial statements were authorized for issue by the Board of Directors on August 5, 2015.

Note 2 – Changes in Accounting Policies

Future Accounting Pronouncements

IFRS 9 - Financial Instruments

> Since November 2009, the IASB has been in the process of completing a three-phase project to replace IAS 39, "Financial Instruments: Recognition and Measurement" with IFRS 9, which includes requirements for hedge accounting, accounting for financial assets and liabilities and impairment of financial instruments. As of July 2014, the IASB completed the final elements of IFRS 9, setting the mandatory effective date to January 1, 2018. The Company will assess the effect of this future pronouncement on its financial statements.

IFRS 15 - Revenue from Contracts with Customers

> In May 2014, the IASB and FASB jointly issued IFRS 15 "Revenue from Contracts with Customers", which replaces IAS 18 Revenue, IAS 11 Construction Contracts and other revenue related interpretations. In July 2015, the IASB deferred the mandatory effective date to January 1, 2018 with early adoption permitted. The Company will assess the effect of this future pronouncement on its financial statements.

Note 3 – Interest and Other

The interest and other costs for the Company are as follows:

	Three months ended June 30,		Six months ended June 30,	
	2015	2014	**2015**	2014
Interest on unsecured termed debt [1]	**$ 21,309**	$ 21,219	**$ 42,790**	$ 42,332
Interest on secured termed credit facility and other	**6,474**	9,655	**11,979**	20,306
Cash interest and other	**27,783**	30,874	**54,769**	62,638
Accretion on unsecured termed debt	**850**	789	**1,698**	1,561
Accretion on decommissioning liability	**1,317**	1,488	**2,465**	3,193
Amortization of deferred financing costs	**459**	403	**852**	814
Other [2]	**—**	7	**(421)**	4
Interest and Other	**$ 30,409**	$ 33,561	**$ 59,363**	$ 68,210

(1) Unsecured termed debt consists of senior unsecured notes and convertible debentures.

(2) Other comprised of gain on retirement of unsecured termed debt and loss (gain) on deferred financial liability.

Note 4 – Exploration and Evaluation Assets

As at,	**June 30, 2015**	December 31, 2014
Exploration and evaluation assets, beginning of period	**$ 335,837**	$ 550,337
Additions[1]	**120**	5,939
Dispositions[1]	**(11,795)**	(154,923)
Transfers to property, plant and equipment	**(35,247)**	(65,516)
Exploration and evaluation assets, end of period	**$ 288,915**	$ 335,837

(1) Includes $nil (December 31, 2014 - $1.5 million) of non-cash consideration.

At December 31, 2014, the Company performed a comprehensive review of the carrying value of its exploration and evaluation assets. At June 30, 2015, the Company assessed the exploration and evaluation assets for indicators of impairment. Based on this assessment, management has determined that no impairment needs to be recognized on these assets as at June 30, 2015.

Note 5 – Property, Plant and Equipment

	Oil and Natural Gas Assets	Other [1]	Total
Balance as at December 31, 2014	**$ 3,267,293**	**$ 8,848**	**$ 3,276,141**
Cost			
As at January 1, 2015	$ 6,250,054	$ 43,636	$ 6,293,690
Additions [2]	92,808	—	92,808
Dispositions	(4,320)	—	(4,320)
Transfers from exploration and evaluation assets	35,247	—	35,247
As at June 30, 2015	$ 6,373,789	$ 43,636	$ 6,417,425
Depletion and Depreciation			
As at January 1, 2015	$ 2,982,761	$ 34,788	$ 3,017,549
Charge for the period	179,143	1,191	180,334
Dispositions	(1,462)	—	(1,462)
As at June 30, 2015	$ 3,160,442	$ 35,979	$ 3,196,421
Balance as at June 30, 2015	**$ 3,213,347**	**$ 7,657**	**$ 3,221,004**

(1) Other fixed assets are mainly comprised of office furniture and fixtures, and computer equipment.

(2) Includes $12.4 million of asset retirement costs.

Asset dispositions

During the three months ended June 30, 2015, the Company recognized a gain on dispositions of $0.2 million resulting from sales of non-core assets for net proceeds of $1.5 million, as well as adjustments to dispositions that occurred in Q1 2015 and 2014 of $0.4 million for a total gain of $0.6 million (2014 - proceeds of $138.8 million, $0.4 million of which was comprised of non-cash asset swaps).

During the six months ended June 30, 2015, the Company recognized a loss on dispositions of $0.8 million resulting from sales of non-core assets for net proceeds of $13.7 million, as well as adjustments to dispositions that occurred in 2014 of $0.5 million for a total loss of $1.3 million (2014 - proceeds of $255.9 million, $3.8 million of which was comprised of non-cash asset swaps).

At December 31, 2014, the Company performed a comprehensive review of the carrying value of its property, plant and equipment. At June 30, 2015, the Company assessed the property, plant and equipment assets for indicators of impairment. Based on this assessment, management has determined that no further impairment needs to be recognized on these assets as at June 30, 2015.

Note 6 – Secured Termed Credit Facility

The Company's secured termed credit facility ("Credit Facility") was amended on May 29, 2015 with its syndicate of lenders. The amended Credit Facility provides for a borrowing base in the amount of $750 million (December 31, 2014 - $1.15 billion), maturing on June 2, 2017, subject to further extension. The lending amount available under the Credit Facility is subject to a semi-annual borrowing base re-determination. During the term of the Credit Facility, the Company will not pay cash dividends without the unanimous consent of the lenders.

The Credit Facility has a single financial covenant that limits the ratio of facility borrowing to trailing twelve months earnings before interest, taxes and other non-cash items ("Adjusted EBITDA") to:

January 1, 2015 - September 30, 2015 - 3.0x
October 1, 2015 - June 30, 2016 - 3.75x
July 1, 2016 - December 31, 2016 - 4.25x
January 1, 2017 - June 2, 2017 - 4.0x

The Company is in compliance with the financial covenant on the Credit Facility at June 30, 2015.

As at,		June 30, 2015		December 31, 2014
Secured termed credit facility outstanding	$	625,958	$	572,495
Deferred financing costs		(4,502)		(3,827)
Secured termed credit facility	$	621,456	$	568,668

The Company had letters of credit issued to third parties totaling $7.2 million (December 31, 2014 - $5.5 million), which reduce the borrowing capacity under the Credit Facility.

Note 7 - Convertible Debentures

At June 30, 2015, Lightstream had US$4.5 million of unsecured convertible debentures outstanding maturing in February 2016.

During the six months ended June 30, 2015, the Company repurchased $2.4 million (US$2.0 million) principal amount of the convertible debentures outstanding for an aggregate purchase price of $2.0 million (US$1.6 million).

Upon conversion, based on the adjusted conversion price of US$26.49 at June 30, 2015, a minimum of 169,907 common shares may be issued. The Company is in compliance with the financial covenants on its convertible debentures. Refer to Note 12 for details.

Note 8 – Senior Unsecured Notes

The Company had US$800 million of Senior Unsecured Notes (the “Unsecured Notes”) outstanding at June 30, 2015 (December 31, 2014 - US$800 million). The Unsecured Notes bear interest at a rate of 8.625% per annum and mature on February 1, 2020. The Unsecured Notes are subordinate to Lightstream's Credit Facility. The Company is in compliance with all financial covenants on its Unsecured Notes. Refer to Note 12 for details.

The following table summarizes the Unsecured Notes:

As at,	June 30, 2015	December 31, 2014
Unsecured Notes, beginning of period	$ 909,402	$ 935,191
Repurchase of Unsecured Notes	—	(103,847)
Gain on settlement	—	(4,002)
Accretion	1,569	2,855
Changes in exchange rate	68,450	79,205
Unsecured Notes, end of period	$ 979,421	$ 909,402

Subsequent to June 30, 2015, the Company cancelled US$546 million of Unsecured Notes in exchange for the issuance of US$449.8 million in second lien notes (the "Secured Notes"). Refer to Note 17 for details.

Note 9 – Decommissioning Liabilities

The total future decommissioning liabilities were estimated by management based on the Company's net ownership interest in all wells, gathering lines and facilities, estimated costs to reclaim and abandon the wells and facilities and the estimated timing of the costs to be incurred.

Changes to decommissioning liabilities were as follows:

	June 30, 2015	December 31, 2014
Balance, beginning of period	$ 198,387	$ 234,511
Change in estimate	11,129	16,508
Obligations incurred	1,286	9,666
Obligations acquired	—	895
Obligations disposed	(63)	(63,386)
Obligations settled	(539)	(4,675)
Accretion	2,465	4,868
Balance, end of period	$ 212,665	$ 198,387

The decommissioning liabilities have been calculated using an inflation rate of 2.0% and discounted using a risk free rate of 2.25% per annum (December 31, 2014 – inflation rate of 2.0% and risk free rate of 2.5%). Most of these obligations are not expected to be paid for several years extending up to 45 years in the future and are expected to be funded from the general resources of the Company at the settlement date. The change in estimate primarily relates to changes in the risk free rate.

Note 10 – Shareholders' Capital

Authorized

The authorized share capital of Lightstream consists of an unlimited number of common shares without nominal or par value.

Normal Course Issuer Bid

During the year ended December 31, 2014, the Company repurchased and canceled 3,499,121 shares at an average price of $2.86 per share. Of the $10 million paid, $41.8 million reduced the book value of the common shares and $31.8 million was recorded as an increase to contributed surplus. The Company did not repurchase any shares for cancellation during the three and six months ended June 30, 2015.

Shareholders' Capital

	June 30, 2015		December 31, 2014	
Share Continuity (thousands of shares)	**Number**	**Amount**	Number	Amount
Balance, beginning of period	**197,304**	**$ 2,358,361**	199,774	$ 2,386,052
Repurchase of common shares	**—**	**—**	(3,499)	(41,779)
Issued pursuant to dividend reinvestment plan/stock dividend plan	**—**	**—**	—	—
Exercise of stock options, incentive shares and deferred common shares	**261**	**13**	1,029	133
Share-based settlement on exercises	**—**	**3,027**	—	13,955
Balance, end of period	**197,565**	**$ 2,361,401**	197,304	$ 2,358,361

Contributed Surplus

Changes in Contributed Surplus		**Amount**
Balance at January 1, 2014	$	134,923
Share-based compensation		11,889
Share-based settlement		(13,955)
Normal course issuer bid		31,762
Balance at December 31, 2014	$	164,619
Share-based compensation		3,494
Share-based settlement		(3,027)
Balance at June 30, 2015	**$**	**165,086**

Dividends

On January 19, 2015, the Company suspended the monthly dividend. The Company paid no dividends for the three and six months ended June 30, 2015 (2014 - $24.4 million and $48.7 million).

Stock Options, Incentive Shares, Deferred Common Shares

Stock Options

Options granted under the stock option plan have an exercise price that is no less than the five day weighted average trading price of the Company's common shares on the TSX prior to the date of the grant. Stock option terms are determined by the Company's Board of Directors, but typically options vest over a period of one to four years from the date of grant and expire between five and 10 years from the date of the grant.

The following is a continuity of stock options outstanding:

	June 30, 2015		December 31, 2014	
(thousands of shares)	**Stock Options**	**Weighted-Average Exercise Price**	Stock Options	Weighted-Average Exercise Price
Balance, beginning of period	**1,161**	**$ 10.27**	9,489	$ 10.96
Granted	**—**	**—**	572	7.38
Exercised	**—**	**—**	(11)	7.57
Expired	**(49)**	**10.34**	(10)	14.33
Forfeited	**(245)**	**10.44**	(2,231)	10.81
Modified	**—**	**—**	(6,648)	10.82
Balance, end of period	**867**	**$ 10.22**	1,161	$ 10.27
Exercisable	**362**	**$ 10.52**	404	$ 10.78

The following table summarizes information about stock options outstanding at June 30, 2015:

Stock Options Outstanding

Range of exercise prices	Number (thousands of shares)	Weighted - Average Remaining Contractual Life (Years)	Weighted-Average Exercise Price
$3.94 - $8.15	284	2.4	$ 7.45
$8.16 - $11.52	353	2.2	10.50
$11.53 - $23.12	230	1.6	13.19
	867	**2.1**	**$ 10.22**

Incentive Shares

The following is a continuity of incentive shares outstanding:

(thousands of shares)	**June 30, 2015**	December 31, 2014
Balance, beginning of period	**4,225**	4,142
Granted	**646**	1,622
Exercised	**(244)**	(909)
Forfeited	**(438)**	(630)
Balance, end of period	**4,189**	4,225
Exercisable [1]	**1,153**	1,128

(1) Incentive shares vested and exercisable into common shares at $0.05 per share.

Deferred Common Shares

The following is a continuity of deferred common shares outstanding:

(thousands of shares)	June 30, 2015	December 31, 2014
Balance, beginning of period	**665**	461
Granted	**—**	314
Exercised	**(17)**	(110)
Balance, end of period	**648**	665
Exercisable [1]	**250**	62

(1) Deferred Common Shares vested and exercisable into common shares at $0.05 per share.

Note 11 – Earnings per Share

The following table summarizes the basic and diluted weighted average number of common shares used in calculating earnings per share:

	Three months ended June 30,		Six months ended June 30,	
	2015	2014	**2015**	2014
Weighted average common shares outstanding, basic [1]	**197,470**	200,060	**197,406**	199,958
Effect of:				
Stock options	**—**	—	**—**	8
Incentive shares	**—**	2,643	**—**	2,522
Deferred common shares	**—**	727	**—**	726
Weighted average common shares outstanding, diluted [1]	**197,470**	203,430	**197,406**	203,214
Net loss and comprehensive loss	**$ (51,533)**	$ 68,195	**$ (178,274)**	$ 82,597
Basic earnings (loss) per share	**(0.26)**	0.34	**(0.90)**	0.41
Diluted earnings (loss) per share	**$ (0.26)**	$ 0.34	**$ (0.90)**	$ 0.41

(1) Thousands of shares.

In determining the weighted average number of common shares outstanding on a diluted basis for the three months ended June 30, 2015, 4.2 million incentive shares and 0.6 million deferred common shares were excluded because the effect would be anti-dilutive (2014 - 8.8 million stock options, nil incentive shares and nil deferred common shares). For the six months ended June 30, 2015, 4.2 million incentive shares and 0.6 million deferred common shares were excluded (2014 - 8.0 million stock options, nil incentive shares, and nil deferred common shares).

The 169,907 common shares issuable on the conversion of the debentures (2014 - 231,232) were considered anti-dilutive and were excluded from the weighted average number of shares on a diluted basis.

Note 12 – Capital Management

The Company's capital structure includes common shares, credit facility outstanding, convertible debentures, senior unsecured notes and working capital. The Company's policy is to maintain a strong capital base in order to provide flexibility for the future development of the business. In order to maintain or adjust the capital structure, from time to time, the Company may issue/repurchase common shares, issue/repurchase debt or other securities, sell assets or adjust capital spending or dividend payments to manage current and projected debt levels. The Company manages its capital structure and makes adjustments to it in light of changes in economic conditions and the risk characteristics of the underlying assets.

As at,		**June 30, 2015**		December 31, 2014
Working capital deficit[1]	**$**	**39,215**	$	140,126
Secured termed credit facility – principal		**625,958**		572,495
Convertible debentures – principal amount (US$)		**4,500**		6,500
Senior unsecured notes – principal amount (US$)		**799,955**		799,955
Shareholders' capital		**2,361,401**		2,358,361
Secured termed credit facility – lending limit	**$**	**750,000**	$	1,150,000
Available credit capacity [2]	**$**	**116,863**	$	572,005

[1] Working capital deficit is calculated as accounts payable and accrued liabilities less accounts receivable and prepaid expenses.
[2] Available credit capacity reduced by $7.2 million (December 31, 2014 - $5.5 million) to reflect issued letters of credit.

The Company uses a ratio of debt to trailing twelve month Adjusted EBITDA and the amount of available credit facility capacity to monitor leverage and the strength of the balance sheet. In order to facilitate the management of these measures, the Company prepares annual budgets, which are updated as necessary depending on varying factors, including current and forecast commodity prices, changes in capital structure, execution of the Company's business plan and general industry conditions. The annual budget is approved by the Lightstream Board of Directors and updates are prepared and reviewed as required.

As at June 30, 2015, the Company had $116.9 million (December 31, 2014 - $572 million) of Credit Facility capacity available. Subsequent to June 30, 2015, the Company issued US$200 million of second lien notes and used the proceeds to reduce the amount outstanding on the Credit Facility while maintaining the borrowing base at $750 million. Refer to Note 17 for details.

The Company is in compliance with the financial covenant on the Credit Facility. At June 30, 2015, the Credit Facility had one financial covenant that limited the ratio of first lien debt (defined as total drawn on the Credit Facility) to Adjusted EBITDA on a trailing twelve month basis to 3:1 (June 30, 2015 - 1.4:1).

The Company is in compliance with its financial covenants on its Unsecured Notes. The Unsecured Notes contain covenants that could limit the Company's ability to issue additional debt, pay dividends, and repurchase stock, among other restrictions.

The Company is in compliance with the financial covenants on its convertible debentures. The convertible debenture indenture stipulates that the ratio of secured debt to total assets is not to exceed 35% (June 30, 2015 - 17.3%).

Note 13 – Financial Instruments and Financial Risk Management

The Company uses derivative instruments to reduce its exposure to fluctuations in commodity prices and foreign exchange rates.

Foreign Exchange Contracts

Lightstream, from time to time, enters into short-term foreign exchange contracts for its USD interest payments and other routine transactions. The following is a summary of foreign exchange contracts in place at June 30, 2015:

Foreign exchange risk management contracts

Settlement	Type		Amount (US$)	Rate (US$/CDN$)
Jul. 2015	Forward	$	22,548	0.80[1]

[1] Prices are the volume weighted average prices for the period.

There were additional contracts entered into subsequent to June 30, 2015 to convert US dollar proceeds from the second lien note issuance to Canadian dollars in order to repay amounts outstanding on the Credit Facility. Below is the summary of contracts that were entered into subsequent to this report

Foreign exchange risk management contracts

Settlement	Type		Amount (US$)	Rate (US$/CDN$)
Jul. 2015	Forward	$	200,000	0.79[1]

[1] Prices are the volume weighted average prices for the period.

Commodity Contracts

The Company uses derivative instruments to reduce its exposure to fluctuations in commodity prices. The following is a summary of crude oil derivative contracts in place as at June 30, 2015:

Crude Oil Price Risk Management Contracts – WTI

Remaining Term	Volume (bopd)	Average Price ($/bbl) [1]	Type
Jul. 2015 – Dec. 2015	4,796	US$80.52 floor/US$103.35 ceiling	Costless Collar
Jul. 2015 - Dec. 2015	1,500	US$56.45	Fixed Price Swap

[1] Prices are the volume weighted average prices for the period.

The following is a summary of natural gas derivative contracts in place as at June 30, 2015:

Remaining Term	Volume (GJ/d)	Average Price ($/GJ) [1]	Type
Jul. 2015 - Dec. 2015	1,000	$2.86	Fixed Price Swap
Jan. 2016 - Dec. 2016	2,000	$2.88	Fixed Price Swap

[1] Prices are the volume weighted average prices for the period.

There were additional contracts entered into subsequent to June 30, 2015. Below is the summary of contracts that were entered into as of the date of this report.

Remaining Term	Volume (GJ/d)	Average Price ($/GJ) [1]	Type
Jul. 2015 - Dec. 2015	1,000	$2.86	Fixed Price Swap
Jan. 2016 - Dec. 2016	4,000	$2.92	Fixed Price Swap

[1] Prices are the volume weighted average prices for the period.

The following is a summary of the fair value risk management contracts in place at June 30, 2015 and December 31, 2014:

As at,	**June 30, 2015**			December 31, 2014		
	Asset	**Liability**	**Net**	Asset	Liability	Net
Crude oil	**$ 22,541**	**$ (1,348)**	**$ 21,193**	$ 66,712	$ —	$ 66,712
Natural gas	**6**	**—**	**6**	—	—	—
Foreign exchange	**294**	**—**	**294**	—	—	—
Total	**$ 22,841**	**$ (1,348)**	**$ 21,493**	$ 66,712	$ —	$ 66,712

Fair Value of Financial Derivative Contracts

The unrealized gain/loss represents the fair value of the underlying risk management contracts to be settled in the future. The realized gain/loss represents the risk management contracts settled during the period.

The table below summarizes the components of risk management contracts:

	Three months ended June 30,		Six months ended June 30,	
	2015	2014	**2015**	2014
Realized gain (loss) on risk management contracts:				
Crude oil derivative contracts	**$ 19,457**	$ (2,159)	**$ 47,810**	$ (2,579)
Natural gas derivative contracts	**12**	(607)	**12**	(2,005)
Foreign exchange contracts	**(2)**	72	**1,487**	995
	19,467	(2,694)	**49,309**	(3,589)
Unrealized gain (loss) on risk management contracts:				
Crude oil derivative contracts	**(37,074)**	(9,874)	**(45,576)**	(14,830)
Natural gas derivative contracts	**62**	1,296	**62**	(977)
Foreign exchange contracts	**262**	(889)	**295**	(1,057)
	(36,750)	(9,467)	**(45,219)**	(16,864)
Gain (loss) on risk management contracts	**$ (17,283)**	$ (12,161)	**$ 4,090**	$ (20,453)

Fair value of Financial Instruments

The Company's financial instruments include cash and cash equivalents, accounts receivable, long-term investments, accounts payable and accrued liabilities, risk management assets and liabilities, secured termed credit facility, convertible debentures, and senior unsecured notes on the consolidated balance sheet.

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

> Level 1 - Quoted prices are available in active markets for identical assets or liabilities as of the reporting date. Active markets are those in which transactions occur in sufficient frequency and volume to provide pricing information on an ongoing basis.
>
> Level 2 - Pricing inputs are other than quoted prices in active markets included in Level 1. Prices in Level 2 are either directly or indirectly observable as of the reporting date. Level 2 valuations are based on inputs, including quoted forward prices for commodities, time value and volatility factors, which can be substantially observed or corroborated in the marketplace.
>
> Level 3 - Valuations in this level are those with inputs for the asset or liability that are not based on observable market data.

Assessment of the significance of a particular input to the fair value measurement requires judgment and may affect the placement within the fair value hierarchy level.

Due to the short-term nature of accounts receivable, accounts payable and accrued liabilities, their carrying value approximates their fair value. The credit facility bears interest at a floating rate and accordingly the fair value approximates the carrying value excluding deferred financing costs.

The carrying value and fair value of these financial instruments at June 30, 2015 is disclosed below by financial instrument classification:

	June 30, 2015		December 31, 2014	
	Carrying Value	**Fair Value**	Carrying Value	Fair Value
Financial Assets				
Accounts receivable	**82,373**	**82,373**	105,333	105,333
Long-term investments [1]	**527**	**527**	1,328	1,328
Risk management asset[2]	**22,841**	**22,841**	66,712	66,712
Financial Liabilities				
Accounts payable and accrued liabilities	**130,738**	**130,738**	253,320	253,320
Secured termed credit facility	**621,456**	**625,958**	568,668	572,495
Convertible debentures[1]	**5,428**	**4,491**	7,172	6,033
Senior unsecured notes[1]	**979,421**	**688,526**	909,402	651,976
Risk management liabilities[2]	**1,348**	**1,348**	—	—

(1) Level 1
(2) Level 2

Note 14 – Changes in Non-Cash Working Capital

	Three months ended June 30, 2015	Three months ended June 30, 2014	Six months ended June 30, 2015	Six months ended June 30, 2014
Change in:				
Accounts receivable	**$ 6,467**	$ 12,798	**$ 22,960**	$ (10,892)
Prepaid expenses	**(1,718)**	(1,252)	**(1,289)**	(2,823)
Accounts payable and accrued liabilities	**(39,421)**	(99,223)	**(122,582)**	(50,045)
Other	**(562)**	(614)	**(1,055)**	(1,228)
	$ (35,234)	$ (88,291)	**$ (101,966)**	$ (64,988)
Changes relating to:				
Attributable to operating activities	**$ 5,280**	$ 36,888	**$ (7,448)**	$ (4,540)
Attributable to investing activities	**$ (40,461)**	$ (124,968)	**$ (90,851)**	$ (60,036)
Attributable to financing activities	**$ (53)**	$ (211)	**$ (3,667)**	$ (412)

Note 15 – Commitments and Contingencies

The following is a summary of the estimated costs required to fulfill the Company's remaining contractual commitments at June 30, 2015:

Type of commitment	1 Year	2-3 Years	4-5 Years	Thereafter	Total
Office leases (1)	6,093	19,034	9,734	2,163	**37,024**
Other	157	—	—	—	**157**
Total	**$ 6,250**	**$ 19,034**	**$ 9,734**	**$ 2,163**	**$ 37,181**

(1) Includes sublease recoveries of $1.3 million (1 Year), $1.0 million (2-3 Years).

Note 16 – Related Party Transactions

Petrobank Energy Resources Ltd. ("Petrobank") was considered a related party until April 30, 2014, as both companies had the same Chief Executive Officer.

In the three and six months ended June 30, 2015, Lightstream had no related party transactions with Petrobank. In the three and six months ended June 30, 2014, Petrobank purchased natural gas from Lightstream at market prices for $0.2 million and $0.4 million respectively. In the three and six months ended June 30, 2014, Lightstream received $nil and $0.1 million in management fees respectively, provided for certain executive functions and legal services.

Note 17 – Subsequent Events

Subsequent to June 30, 2015, the Company issued US$649.8 million of Secured Notes. On July 2, 2015, in connection with the issuance of US$395 million of Secured Notes, the Company cancelled US$465 million of Unsecured Notes. On July 14, 2015, a further US$200 million of Secured Notes were issued for cash proceeds which were used to partially reduce the outstanding borrowing under the Credit Facility. On August 4, 2015, the Company issued an additional US$54.8 million of Secured Notes in exchange for US$81 million of Unsecured Notes which were cancelled.

The Secured Notes bear interest at 9.875% per annum and mature June 15, 2019. The Secured Notes are secured by second priority liens on all of the Company's assets and are subordinate to the Credit Facility. The Company is assessing the impact of the transaction on its financial statements.

CORPORATE INFORMATION

DIRECTORS

Ian Brown (1)(4)
Calgary, Alberta

Martin Hislop (1)(3)
Calgary, Alberta

E. Craig Lothian (2)(4)
Regina, Saskatchewan

Kenneth McKinnon (1)(3)(4)(5)
Calgary, Alberta

Corey C. Ruttan (1)(4)
Calgary, Alberta

W. Brett Wilson (2)(3)
Calgary, Alberta

John D. Wright (2)
Calgary, Alberta

(1) Member of the Audit Committee
(2) Member of the Reserves Committee
(3) Member of the Compensation Committee
(4) Member of the Governance and Nominating Committee
(5) Chairman of the Board of Directors

REGISTRAR AND TRANSFER AGENT

Computershare
600, 530 – 8th Avenue SW
Calgary, Alberta T2P 3S8
TEL: 1 (800) 564-6253
FAX: 1 (888) 453-0330

LEGAL COUNSEL

McCarthy Tétrault LLP
Calgary, Alberta, Canada

BANKERS

The Toronto-Dominion Bank
Calgary, Alberta, Canada

AUDITORS

Deloitte LLP
Calgary, Alberta, Canada

RESERVE ENGINEERS

Sproule Associates Limited
Calgary, Alberta, Canada

EXCHANGE LISTING

The Toronto Stock Exchange
SYMBOL: LTS

OFFICERS

Annie Belecki
General Counsel

Mary Bulmer
Vice President, Corporate Services

Lawrence Fisher
Vice President, Land

Peter Hawkes
Vice President, Geosciences

Rene LaPrade
Senior Vice President and
Chief Operating Officer

Brad Malley
Vice President, Development Services

Doreen Scheidt
Vice President and Controller

Peter D. Scott
Senior Vice President and Chief Financial Officer

John D. Wright
President and Chief Executive Officer

HEAD OFFICE
Lightstream Resources Ltd.
Eighth Avenue Place
2800, 525 – 8th Avenue SW
Calgary, Alberta T2P 1G1

TEL: (403) 268-7800
FAX: (403) 218-6075
WEBSITE: http://www.lightstreamresources.com
EMAIL: ir@lightstreamres.com

SECURITIES FILINGS

www.sedar.com

Information requests and other investor relations inquiries can be directed to ir@lightstreamres.com or by telephone at (403) 268-7800. Additional corporate information can be obtained through Lightstream's website at http://www.lightstreamresources.com