Birchcliff Energy Ltd.

Growth by the drill bit

QUARTERLY REPORT

2014Q1

THREE MONTHS ENDED MARCH 31, 2014

May 14, 2014

Fellow Shareholders,

Birchcliff Energy Ltd. ("**Birchcliff**") is pleased to report its first quarter financial and operational results for the three month period ended March 31, 2014. Birchcliff had an excellent quarter. Record natural gas production together with strong natural gas prices resulted in record first quarter revenue, funds flow and earnings. In addition, total cash costs (operating, transportation and marketing, general and administrative and interest costs) were reduced on a per boe basis from the first quarter of 2013 and the fourth quarter of 2013, notwithstanding the difficult operating conditions resulting from the bitterly cold winter.

Outlook for 2014 Production and Cash Flow

Birchcliff is on track to achieve record annual average production of approximately 34,000 boe per day for 2014, representing 32% growth over the annual average of 25,829 boe per day in 2013.

Estimated fourth quarter average production is approximately 38,000 boe per day. We maintain our previously announced exit production rate guidance of 37,500 to 39,500 boe per day.

Estimated 2014 cash flow is approximately $331 million or $2.30 per share, based on forecasted annual production of 34,000 boe per day, an AECO natural gas price of $4.50 per GJ and WTI oil price of US $95.00 per bbl from April 1 through December 31, 2014, and based on basic weighted average common shares outstanding in the first quarter of 144,026,125.

Production

Current production is approximately 32,000 boe per day.

Birchcliff had record average production of 31,749 boe per day in the first quarter of 2014, an increase of 22% from 26,108 boe per day in the first quarter of 2013 and an increase of 12% from 28,391 boe per day in the fourth quarter of 2013. Production per share increased 20% from the first quarter of 2013.

Funds Flow and Earnings

Funds flow was $88.4 million or $0.61 per common share in the first quarter of 2014, an increase of 124% from $39.4 million and an increase of 118% from $0.28 per common share in the first quarter of 2013.

Birchcliff had record net income to common shareholders in the first quarter of 2014 of $38.5 million or $0.27 per common share, an increase of 499% and 440% respectively, from the first quarter of 2013. This is an increase of 259% from net income to common shareholders of $10.8 million in the fourth quarter of 2013, excluding a non-recurring gain on the sale of assets.

Continued Cost Reductions

We are very pleased that our operating costs per boe continue to decline quarter over quarter. The credit for maintaining our low operating costs in the bitterly cold winter and difficult operating conditions goes to our field employees. We never forget that our best assets are our people.

In the first quarter of 2014, we reduced our operating costs to an average of $5.21 per boe, a decrease of 10% from the first quarter of 2013 and a decrease 4% from the fourth quarter of 2013. Notably, at Birchcliff's 100% owned Pouce Coupe South Natural Gas Plant ("**PCS Gas Plant**"), where we processed 76% of our natural gas production and achieved an 81% operating margin, operating costs were approximately $0.43 per Mcfe or $2.61 per boe. We anticipate increasing the percentage of natural gas processed at the PCS Gas Plant as new Montney/Doig horizontal natural gas wells are drilled in 2014, which will further reduce our corporate operating costs on a per boe basis.

Total cash costs per boe, including operating costs, transportation and marketing costs, general and administrative expenses and interest were $11.28 per boe in the first quarter of 2014, a decrease of 11% from the first quarter of 2013 and a decrease of 8% from the fourth quarter of 2013. Strong oil and natural gas prices together with Birchcliff's low operating cost structure resulted in material funds flow netback of $30.93 per boe in the first quarter of 2014, an increase of 84% from $16.79 per boe in the first quarter of 2013.

Phase IV Expansion of the PCS Gas Plant

The Phase IV expansion of the PCS Gas Plant will bring processing capacity to 180 MMcf per day, from 150 MMcf per day, by adding additional compression and sales pipeline capacity. The estimated cost of the Phase IV expansion is approximately $11.6 million. The anticipated start-up date of the Phase IV expansion is September 2014. This project is on schedule and on budget.

Increase to Credit Facilities

On May 9, 2014, Birchcliff's bank syndicate approved an increase of the aggregate credit facilities limit to $750 million from $600 million and the revolving credit facilities were converted to a three-year term with a maturity date of May 9, 2017. The aggregate credit facilities include $620 million of revolving term credit facilities (previously $470 million); a $70 million non-revolving five-year term credit facility; and a $60 million non-revolving five-year term credit facility. The increased aggregate credit facilities will provide Birchcliff with increased financial flexibility.

Strategic Acquisitions

We are very pleased with the $56 million strategic acquisition of a partner's 30% working interest in land and production on the Montney/Doig Natural Gas Resource Play in January 2014, giving Birchcliff a 100% working interest in 38 sections of land that has Montney and Doig rights. Approximately 9.6 MMcfe per day (1,600 boe per day) of production was acquired, the majority of which goes to Birchcliff's PCS Gas Plant. This transaction has allowed Birchcliff to consolidate lands it formerly held at 70% working interest with lands it held at 100% working interest, allowing for a contiguous development plan, eliminating holding buffers and increasing the flexibility of capital allocation.

Land additions in the first quarter of 2014 have increased Birchcliff's number of Montney/Doig Resource Play net future horizontal drilling locations to 2,335.8 from 2,254.4 at December 31, 2013.

Hedging Activities

Birchcliff's natural gas production during the winter of 2013/2014 was unhedged and as a result we received the full benefit of the high natural gas prices in the first quarter of 2014.

Birchcliff has contracted forward physical sales of 75,000 GJ per day for approximately $4.35 per Mcf, representing 40% of our estimated natural gas volumes during the summer months, April 1 to October 31, 2014. We have no current intention of contracting forward physical sales of natural gas for the winter months of 2014/2015, however later in 2014 we will consider hedging natural gas for the 2015 summer months.

2014 FIRST QUARTER FINANCIAL AND OPERATIONAL RESULTS

Production

First quarter 2014 production averaged 31,749 boe per day, an increase of 22% from 26,108 boe per day in the first quarter of 2013.

Production consisted of approximately 83% natural gas and 17% crude oil and natural gas liquids in the first quarter of 2014. Approximately 76% of Birchcliff's natural gas production and 66% of corporate production was processed at the PCS Gas Plant during the first quarter of 2014.

Funds Flow and Earnings

First quarter 2014 funds flow was $88.4 million or $0.61 per common share, a 124% increase from $39.4 million or $0.28 per common share in the first quarter of 2013. The increase from the first quarter of 2013 was a result of the 24% increase in natural gas production and 78% increase in the AECO natural gas spot price, which averaged $5.71 per Mcf for the first quarter of 2014 compared to $3.20 per Mcf for the first quarter of 2013.

Birchcliff exceeded its previously announced 2014 first quarter cash flow guidance of $83 million by $5.4 million, due mainly to higher than forecasted oil and liquids pricing for February and March production.

Birchcliff had record net income to common shareholders in the first quarter of 2014 of $38.5 million or $0.27 per common share, an increase of 499% from $6.4 million and 440% from $0.05 per common share respectively from the first quarter of 2013. This is an increase of 259% from net income to common shareholders of $10.8 in the fourth quarter of 2013, excluding a non-recurring gain on the sale of assets.

Debt and Capitalization

At March 31, 2014, Birchcliff's long-term bank debt was $453.8 million from available credit facilities of approximately $600 million. Total debt, including the working capital deficit of $70.9 million, was $524.7 million as compared to $454.0 million at December 31, 2013.

On May 9, 2014, Birchcliff's bank syndicate approved an increase of the aggregate credit facilities limit to $750 million from $600 million as a result of the significant reserve additions in 2013.

At March 31, 2014, Birchcliff had outstanding 144,503,777 basic common shares.

Preferred Share Warrants

At March 31, 2014, Birchcliff had 6,000,000 warrants outstanding, each warrant providing the right to purchase one common share at an exercise price of $8.30 until August 8, 2014. Birchcliff expects that the holders of the warrants will exercise their warrants prior to August 8, which will result in Birchcliff receiving approximately $50 million in warrant proceeds and will require the issuance of six million common shares.

Operating Costs

Operating costs in the first quarter of 2014 were $5.21 per boe, a decrease of 10% from $5.77 per boe in the first quarter of 2013. This reduction of operating costs on a per boe basis was largely due to increased volumes of natural gas being processed through the PCS Gas Plant and the implementation of various optimization initiatives.

General and administrative expenses in the first quarter of 2014 was $1.89 per boe, a decrease of 9% from $2.08 per boe in the first quarter of 2013.

Capital Expenditures

The following table sets forth a summary of Birchcliff's capital expenditures at the end of the first quarter of 2014.

($000's)	**Three months ended March 31, 2014**
Land	9,064
Seismic	5,384
Workovers	2,952
Drilling and completions	66,942
Well equipment and facilities	20,230
Finding and development costs (F&D)	104,572
Acquisitions	56,553
Dispositions	-
Finding, development and acquisition costs (FD&A)	161,125
Administrative assets	278
Capital expenditures, net	**161,403**

PCS Gas Plant Netbacks

Processing natural gas at the PCS Gas Plant has materially improved Birchcliff's funds flow and net earnings. In the first quarter of 2014, operating costs for natural gas processed at the PCS Gas Plant averaged $0.43 per Mcfe ($2.61 per boe) and the estimated operating netback for Birchcliff's natural gas production flowing to the PCS Gas Plant was $5.25 per Mcfe. Approximately 76% of Birchcliff's natural gas production and 66% of corporate production was processed at the PCS Gas Plant in the first quarter of 2014.

The following table details Birchcliff's net production, estimated operating netback and operating margin for wells producing to the PCS Gas Plant, on a production month basis.

Production Processed at the PCS Gas Plant		Three months ended March 31, 2014[1]		Three months ended March 31, 2013
Average daily production, net to Birchcliff:				
Natural gas *(Mcf)*		120,316		87,104
Oil & NGLs *(bbls)*		923		246
Total boe *(6:1)*		**20,975**		14,763
Percentage of corporate natural gas production		*76%*		*68%*
Percentage of corporate production		*66%*		*57%*
Netback and cost:	*$/Mcfe*	*$/boe*	*$/Mcfe*	*$/boe*
Petroleum and natural gas revenue[2]	6.51	39.08	3.57	21.40
Royalty expense	(0.53)	(3.19)	(0.22)	(1.33)
Operating expense[3]	(0.43)	(2.61)	(0.28)	(1.68)
Transportation and marketing expense	(0.30)	(1.78)	(0.24)	(1.40)
Estimated operating netback	**5.25**	**31.50**	2.83	16.99
Operating margin[4]	**81%**	**81%**	79%	79%

(1) The PCS Gas Plant processed an average of 127 MMcf per day of gross raw gas at the inlet during the first quarter of 2014, against a current licensed processing capacity of 150 MMcf per day.

(2) AECO natural gas spot price averaged $5.71 per Mcf and $3.20 per Mcf in the first quarter of 2014 and first quarter of 2013, respectively.

(3) The increased operating expense per boe results from reduced third party recoveries as a result of the January 2014 acquisition of a partner's working interest in joint lands, offset by increased volumes of natural gas processed through the PCS Gas Plant.

(4) Operating margin at the PCS Gas Plant is determined by dividing the estimated operating netback by petroleum and natural gas revenue in the period.

OPERATIONS UPDATE

Drilling

Birchcliff's 2014 drilling program is focused on our two proven resource plays, the Montney/Doig Natural Gas Resource Play and the Worsley Charlie Lake Light Oil Resource Play. During the first quarter of 2014, Birchcliff drilled 15 (15.0 net) wells, all 100% working interest, including 7 (7.0 net) natural gas wells, and 8 (8.0 net) oil wells.

Wells drilled in the first quarter of 2014 include 7 (7.0 net) Montney/Doig horizontal natural gas wells, 2 (2.0 net) Montney/Doig horizontal oil wells; 1 (1.0 net) Upper Doig horizontal oil well; and 5 (5.0 net) Charlie Lake horizontal oil wells, all of which were completed utilizing multi-stage fracture stimulation technology, and all of which were successful.

Birchcliff currently has two drilling rigs at work in the Pouce Coupe area, drilling Montney/Doig horizontal natural gas wells through break-up on multi-well pads. These rigs are designed for multi-well pad drilling and as a result, have drilled over the break-up period. After break-up, two other rigs will resume their drilling programs, one rig will be drilling Montney/Doig horizontal wells in the Pouce Coupe area and the other rig will be drilling Charlie Lake horizontal wells in the Worsley area.

Land

The Corporation has been strategically acquiring more land. We have continued to expand our undeveloped land base and held 577,572 (549,083 net) acres at March 31, 2014, with a 95% average working interest. During the first quarter of 2014, Birchcliff acquired 17,953 net acres of land, all in its core area of the Peace River Arch of Alberta through Crown land sales and the purchase of third party lands. Most of the land acquired in the first quarter of 2014 was on the Montney/Doig Resource Play in the Pouce Coupe area. Key lands were acquired through the strategic acquisition of a partner's 30%

working interest in land and production on the Montney/Doig Resource Play, giving Birchcliff 100% interest in 38 sections of land. The other newly acquired lands on the Montney/Doig Resource Play are contiguous with our existing land base and we expect a significant amount of proved plus probable reserves and discovered resources to be attributed to these newly acquired lands at year end.

Birchcliff's land base primarily consists of large contiguous blocks of high working interest acreage located near facilities owned and/or operated by Birchcliff or near third party infrastructure. This gives Birchcliff the flexibility to optimize well layouts in order to maximize reservoir contact.

Seismic

Birchcliff believes seismic data, more specifically three dimensional ("**3-D**") seismic data, is a key technical tool in the development of resource plays. A high percentage of Birchcliff's drilling activities are supported by 3-D seismic. In the first quarter of 2014 Birchcliff spent $5.4 million on 3-D seismic, which included 74 square kilometers of new proprietary 3-D seismic; 27 square kilometers of new industry speculative 3-D seismic; and 308 square kilometers of trade 3-D seismic. This geophysical data gives a much more refined image of what the subsurface looks like, assisting in geological interpretations to delineate reservoir distribution of our resource plays, and assisting in the drilling of the horizontal wells.

Montney/Doig Natural Gas Resource Play

In the first quarter of 2014, Birchcliff drilled 7 (7.0 net) Montney/Doig horizontal natural gas wells and 2 (2.0 net) Montney/Doig horizontal light oil wells. Year-to-date Birchcliff has drilled 12 (12.0 net) Montney/Doig horizontal natural gas wells and 2 (2.0 net) Montney/Doig horizontal light oil wells. Birchcliff continues to expand the Montney/Doig Natural Gas Resource Play both geographically and stratigraphically.

All seven Montney/Doig horizontal natural gas wells and the two Montney/Doig horizontal light oil wells drilled in the first quarter of 2014 have been brought on production. With respect to the Montney/Doig light oil wells, Birchcliff has a modest development plan for the Montney/Doig light oil play, but at this time we have only a limited number of follow-up locations with oil potential in this area.

On our Montney/Doig Natural Gas Resource Play we are currently utilizing multi-well pad drilling, allowing us to drill continuously right through spring break-up. We are currently drilling on two multi-well pads where we are drilling five horizontal natural gas wells on each.

To quantify our aggressive growth strategy for the Montney/Doig Resource Play, in the first quarter of 2014, through landsales and acquisitions and removing any expires, we added 12.8 net sections of land for the Basal Doig/Upper Montney Play and 13.0 sections of land for the Middle/Lower Montney Play, for a total of 25.8 net sections to develop on the Montney/Doig Resource Play. These lands, developed at four wells per section, per play, yields a total of 103.2 net future locations.

At March 31, 2014, Birchcliff's total land holdings on the Middle/Lower Montney Play and the Basal Doig/Upper Montney Play was 644.5 (615.7 net) sections. On full development of four horizontal wells per section per play, at the end of the first quarter of 2014 Birchcliff had 2,462.7 net horizontal existing wells and future horizontal drilling locations. By subtracting the 126.9 net locations drilled at the end of the first quarter of 2014, there remain 2,335.8 net future horizontal drilling locations.

By definition, all of the new land on the play will contribute to our Total Petroleum Initially In Place ("**TPIIP**") so we anticipate a significant increase in TPIIP at year end. These newly acquired lands are proximal to our Pouce Coupe development area so we expect a large percentage of the TPIIP to be categorized as Discovered Petroleum Initially In Place.

Recently there have been some significant positive developments by industry on the Montney/Doig Natural Gas Resource Play. One general area of development is the increased exploration and commercialization of new stratigraphic intervals within this play. We continue to evaluate additional new target intervals within the Montney and Doig formations, to more fully define the potential of our Montney/Doig Natural Gas Resource Play. We anticipate drilling our first horizontal well in one of the new intervals by year end.

Worsley Charlie Lake Light Oil Resource Play

On the Worsley Charlie Lake Light Oil Resource Play, in the first quarter of 2014, Birchcliff drilled 5 (5.0 net) Charlie Lake horizontal oil wells, utilizing multi-stage fracture stimulation technology.

With the continued success of the water flood on the Worsley Light Oil pool, we are expanding the water flood area and are conducting the field operations necessary to convert two more wells to injectors and will install associated facility infrastructure.

SHAREHOLDER SUPPORT

We thank Mr. Seymour Schulich, our largest shareholder, for his ongoing financial and moral support. Mr. Schulich did not blink when natural gas prices hit $1.61 per GJ in September 2013, and in fact was even more supportive when extremely low gas prices made life difficult at Birchcliff. Having a significant shareholder with a long-term investment horizon is a significant reason why Birchcliff is where it is today. Mr. Schulich holds 40 million common shares representing 28.2% of the current issued and outstanding common shares.

OUTLOOK

Birchcliff has never had a brighter outlook than it has today. Our low cost structure, our solid low decline production base together with higher commodity prices has positioned us to accelerate our growth while improving our balance sheet.

I would like to summarize our current and future outlook as set out below:

1. Birchcliff is on track to achieve record annual average production of approximately 34,000 boe per day for 2014, representing 32% growth over the annual average of 25,829 boe per day in 2013.

2. We currently forecast fourth quarter average production to be approximately 38,000 boe per day. We maintain our previously announced exit production rate guidance of 37,500 to 39,500 boe per day.

3. Estimated 2014 cash flow is approximately $331 million or $2.30 per common share, based on estimated annual production of 34,000 boe per day, an AECO natural gas price of $4.50 per GJ and WTI oil price of US $95.00 per bbl from April 1 through December 31, 2014, and based on basic weighted average common shares outstanding in the first quarter of 144,026,125.

4. We have just had record first quarter cash flow and earnings while continuing to reduce our cash costs per boe. We expect to fund our 2014 budgeted capital expenditure program of $291 million (excluding acquisitions), wholly out of internally generated cash flow.

5. Funding our significant production growth out of our material cash flow has significantly improved our debt ratios, bringing them in line with or ahead of some of our peers.

6. We successfully purchased our partner out of the Pouce Coupe area, giving us 100% working interests in the heart of Pouce Coupe.
7. We are on schedule and on budget with the PCS Gas Plant Phase IV expansion to 180 MMcf per day of processing capacity, setting up for material production growth in the fourth quarter of 2014.
8. At March 31, 2014, Birchcliff's total land holdings on the Middle/Lower Montney Play and the Basal Doig/Upper Montney Play was 644.5 (615.7 net) sections. On full development of four horizontal wells per section per play, less the horizontal wells drilled to March 31, 2014, there remain 2,335.8 net future horizontal drilling locations.
9. To date we have drilled 132 (131.9 net) Montney/Doig horizontal natural gas wells, all the while focusing on reducing costs and increasing our knowledge and expertise on the play.
10. We believe that we have further exploration drilling opportunities on both our Montney/Doig Natural Gas Resource Play and our Worsley Charlie Lake Light Oil Resource Play, which may provide significant and material increases to our future drilling opportunities.
11. Natural gas prices look to be strong for the foreseeable future. With approximately 60% of our natural gas unhedged this summer, and totally unhedged beyond this summer, Birchcliff looks to benefit significantly from these high prices.

Birchcliff expects to receive approximately $50 million in proceeds from the exercise of $8.30 Warrants before their expiry on August 8, 2014. It is our expectation that in August 2014, Birchcliff will increase its capital budget by at least $50 million. We expect to announce the details of this budget increase with our second quarter results on August 13, 2014 at the close of markets. With strong natural gas prices and growing cash flow, we expect to continue to reinvest our cash flow and the proceeds from the exercise of the warrants, which will result in very strong year-end production growth and position Birchcliff for strong growth in 2015.

Our business worked very well and was profitable at low commodity prices. In 2013, we did not issue equity and dilute our shareholders when commodity prices were weak, we chose to carry more debt, yet we still had top decile production, cash flow and earnings growth. With strong natural gas prices and material cash flow growth, we intend to grow as quickly as we prudently can. We will take advantage of our approximately 2,335 net future Montney/Doig drilling locations and our 100% owned infrastructure, which gives us the ability to speed up and slow down capital expenditures. In 2014, we expect to fund our $291 million capital program (excluding acquisitions) wholly out of internally generated cash flow.

It's show time and we are ready to go.

On behalf of our Management Team and Directors, thank you to the Birchcliff staff for their continued loyalty, dedication and continued hard work to help us achieve our corporate goals.

(signed) "*A. Jeffery Tonken*"

A. Jeffery Tonken, President and Chief Executive Officer

Financial and Operational Highlights

	Three months ended March 31, 2014	Three months ended March 31, 2013
OPERATING		
Average daily production		
Light oil – *(barrels)*	3,977	4,047
Natural gas – *(thousands of cubic feet)*	158,456	128,101
NGLs – *(barrels)*	1,362	710
Total – barrels of oil equivalent *(6:1)*	**31,749**	26,108
Average sales price *($ CDN)*[1]		
Light oil – *(per barrel)*	97.30	84.82
Natural gas – *(per thousand cubic feet)*	6.10	3.40
NGLs – *(per barrel)*	95.35	86.80
Total – barrels of oil equivalent *(6:1)*	**46.73**	32.21
NETBACK AND COST *($ per barrel of oil equivalent at 6:1)*		
Petroleum and natural gas revenue	46.74	32.22
Royalty expense	(4.43)	(2.74)
Operating expense	(5.21)	(5.77)
Transportation and marketing expense	(2.48)	(2.25)
Netback	**34.62**	21.46
General & administrative expense, net	(1.89)	(2.08)
Interest expense	(1.70)	(2.59)
Realized loss on financial instruments	(0.10)	-
Funds flow netback	**30.93**	16.79
Stock-based compensation expense, net	(0.34)	(0.55)
Depletion and depreciation expense	(11.19)	(11.51)
Accretion expense	(0.21)	(0.20)
Amortization of deferred financing fees	(0.09)	(0.08)
Unrealized loss on financial instruments	(0.05)	-
Dividends on Series C Preferred Shares	(0.31)	-
Income tax expense	(4.92)	(1.29)
Net income	13.82	3.16
Dividends on Series A Preferred Shares	(0.35)	(0.43)
Net income to common shareholders	**13.47**	2.73
FINANCIAL		
Petroleum and natural gas revenue *($000's)*	133,558	75,718
Funds flow from operations *($000's)*[2]	88,369	39,444
Per common share – basic *($)*[2]	0.61	0.28
Per common share – diluted *($)*[2]	0.60	0.27
Net income *($000's)*	39,499	7,424
Net income to common shareholders *($000's)*[3]	38,499	6,424
Per common share – basic *($)*[3]	0.27	0.05
Per common share – diluted *($)*[3]	0.26	0.04
Common shares outstanding		
End of period – basic	144,503,777	142,096,130
End of period – diluted	166,085,345	164,106,949
Weighted average common shares for period – basic	144,026,125	141,821,280
Weighted average common shares for period – diluted	147,090,254	144,366,102
Dividends on Series A Preferred Shares *($000's)*	1,000	1,000
Dividends on Series C Preferred Shares (*$000's*)	875	-
Capital expenditures, net *($000's)*	161,403	81,010
Long-term bank debt *($000's)*	453,772	451,371
Working capital deficit *($000's)*[4]	70,948	50,920
Total debt *($000's)*	524,720	502,291

(1) Average sales price excludes the effect of hedges on financial instruments.

(2) Funds flow from operations and per common share amounts are non-GAAP measures that represent cash flow from operating activities as per the statements of cash flows before the effects of changes in non-cash working capital and decommissioning expenditures. Per common share amounts are calculated by dividing funds flow from operations by the weighted average number of basic or diluted common shares outstanding for the period.

(3) Net income to common shareholders is calculated using net income as determined in accordance with GAAP, adjusted for dividends paid on Series A Preferred Shares. Per common share amounts are calculated by dividing net income to common shareholders by the weighted average number of basic or diluted common shares outstanding for the period.

(4) Excludes the fair value of financial instruments and related deferred premium.

Management’s Discussion and Analysis

GENERAL

Birchcliff Energy Ltd. (“**Birchcliff**” or the “**Corporation**”) is a Calgary, Alberta based intermediate oil and natural gas company with operations concentrated in its one core area, the Peace River Arch of Alberta. Additional information relating to the Corporation, including its Annual Information Form, is available on the SEDAR website at www.sedar.com and on the Corporation’s website at www.birchcliffenergy.com. Birchcliff’s common shares are listed for trading on the Toronto Stock Exchange (“**TSX**”) under the symbol “BIR” and are included in the S&P/TSX Composite Index.

The following Management’s Discussion and Analysis (“**MD&A**”) is dated May 14, 2014. The unaudited interim condensed financial statements with respect to the three months ended March 31, 2014 (the “**Reporting Period**”) as compared to the three months ended March 31, 2013 (the “**Comparable Prior Period**”) and this MD&A have been prepared by management and approved by the Corporation’s Audit Committee and Board of Directors. This MD&A should be read in conjunction with the interim condensed financial statements of the Corporation and related notes for the Reporting Period and the 2013 Annual Report. All dollar amounts are expressed in Canadian currency, unless otherwise stated.

2014 OUTLOOK

Birchcliff’s 2014 budgeted capital expenditure program of $291 million (excluding acquisitions) is expected to be funded wholly out of internally generated funds flow.

Birchcliff is on track to achieve record annual average production of approximately 34,000 boe per day for 2014, representing 32% growth over the annual average of 25,829 boe per day in 2013.

We currently estimate fourth quarter average production to be approximately 38,000 boe per day. We maintain our previously announced exit production rate guidance of 37,500 to 39,500 boe per day.

Estimated 2014 cash flow is approximately $331 million or $2.30 per common share, based on estimated annual production of 34,000 boe per day, an AECO natural gas price of $4.50 per GJ and WTI oil price of US $95.00 per bbl from April 1 through December 31, 2014, and based on basic weighted average common shares outstanding in the first quarter of 144,026,125.

The Phase IV expansion of the PCS Gas Plant will bring processing capacity to 180 MMcf per day, from 150 MMcf per day, by adding additional compression and sales pipeline capacity. The estimated cost of the Phase IV expansion is approximately $11.6 million. The anticipated start-up date of the Phase IV expansion is September 2014. This project is on schedule and on budget.

Birchcliff has contracted forward physical sales of 75,000 GJ per day for approximately $4.35 per Mcf, representing 40% of our estimated natural gas volumes during the summer months, April 1 to October 31, 2014. We have no current intention of contracting forward physical sales of natural gas for the winter months of 2014/2015, however later in 2014 we will consider hedging natural gas for the 2015 summer months.

At March 31, 2014, Birchcliff had 6,000,000 warrants outstanding, each warrant providing the right to purchase one common share at an exercise price of $8.30 until August 8, 2014. Birchcliff expects that the holders of the warrants will exercise their warrants prior to August 8, which will result in Birchcliff receiving approximately $50 million in warrant proceeds and will require the issuance of six million common shares.

The Corporation does not foresee any liquidity issues with respect to the operation of its oil and natural gas business in 2014 and expects to meet its future obligations as they become due. The Corporation's two established resource plays provide it with a long-term and operationally reliable production base. Funds flow from this production is primarily dependent on commodity prices, which affect the pace at which the Corporation invests in its resource plays and the rate at which its production will grow.

Record production and a low cost structure, together with high natural gas prices has given Birchcliff tremendous momentum for strong financial results and production growth in 2014.

FUNDS FLOW AND NET INCOME

Funds Flow from Operations

Funds flow from operations and funds flow per common share are non-GAAP measures defined as cash flow from operating activities before the effects of changes in non-cash working capital and decommissioning expenditures. Birchcliff's calculation of funds flow from operations is considered to be a key measure of the ability to generate the cash necessary to fund future growth through capital investments, pay dividends on preferred shares and repay debt. The following schedule sets out the reconciliation of cash flow from operating activities, as determined in accordance with International Financial Reporting Standards ("**IFRS**"), to funds flow from operations:

($000's)	Three months ended March 31, 2014	Three months ended March 31, 2013
Cash flow from operating activities	73,310	35,310
Adjustments:		
Decommissioning expenditures	808	41
Changes in non-cash working capital	14,251	4,093
Funds flow from operations(1)	**88,369**	39,444
Per common share – basic *($)*(1)	**0.61**	0.28
Per common share – diluted *($)*(1)	**0.60**	0.27

(1) Funds flow from operations and funds flow per common share amounts as presented do not have any standardized meaning prescribed by IFRS and therefore it may not be comparable with the calculations of similar measures for other issuers. Funds flow from operations is not intended to represent cash flow from operating activities, net income or other measures of financial performance calculated in accordance with IFRS. Per common share amounts are calculated by dividing funds flow from operations by the weighted average number of basic and diluted common shares outstanding for the period.

Birchcliff achieved record quarterly funds flow of $88.4 million in the first quarter of 2014, an increase of 124% from $39.4 million in the first quarter of 2013. Funds flow, when compared to the first quarter of 2013, was positively impacted by a 79% increase in realized natural gas wellhead prices, a 15% increase in realized oil wellhead prices, a 24% increase in natural gas production and lower interest costs and negatively offset by higher general and administrative expenses and an increase in royalty, production and transportation costs resulting from higher production in the first quarter of 2014.

Strong oil and natural gas prices together with Birchcliff's low operating costs resulted in material funds flow netback of $30.93 per boe in the first quarter of 2014, an increase of 84% from $16.79 per boe in the first quarter of 2013.

Net Income to Common Shareholders

($000's)	Three months ended March 31, 2014	Three months ended March 31, 2013
Net income	39,499	7,424
Net income to common shareholders[1]	**38,499**	6,424
Per common share – basic *($)*[1]	**0.27**	0.05
Per common share – diluted *($)*[1]	**0.26**	0.04

(1) Net income to common shareholders is calculated using net income as determined in accordance with IFRS, adjusted for dividends paid on Series A Preferred Shares of $1.0 million during the Reporting Period (Comparable Prior Period - $1.0 million). Per common share amounts are calculated by dividing net income to common shareholders by the weighted average number of basic or diluted common shares outstanding for the period.

Birchcliff had record net income to common shareholders of $38.5 million in the first quarter of 2014, an increase of 499% from $6.4 million in the first quarter of 2013. This increase was mainly attributable to an improved natural gas price environment and increased natural gas production which translated to higher funds flow in the first quarter of 2014, offset by higher income taxes and depletion expense.

PCS GAS PLANT NETBACKS

The low operating cost structure together with the high operating netback margin at the 100% owned and operated PCS Gas Plant has allowed Birchcliff to achieve material funds flow and net earnings in the current quarter.

During the first quarter of 2014, the Corporation processed approximately 76% of its total natural gas production through the PCS Gas Plant at an average operating cost of $0.43 per Mcfe ($2.61 per boe). The estimated operating netback at the PCS Gas Plant was $5.25 per Mcfe ($31.50 per boe) resulting in an operating margin of 81% in the first quarter of 2014.

The following table details Birchcliff's net production, estimated operating netback and operating margin for wells producing to the PCS Gas Plant, on a production month basis:

Production Processed at the PCS Gas Plant	Three months ended March 31, 2014[1]		Three months ended March 31, 2013	
Average daily production, net to Birchcliff:				
Natural gas *(Mcf)*		120,316		87,104
Oil & NGLs *(bbls)*		923		246
Total boe *(6:1)*		**20,975**		14,763
Percentage of corporate natural gas production		*76%*		*68%*
Percentage of corporate production		*66%*		*57%*
Netback and cost:	*$/Mcfe*	*$/boe*	*$/Mcfe*	*$/boe*
Petroleum and natural gas revenue[2]	6.51	39.08	3.57	21.40
Royalty expense	(0.53)	(3.19)	(0.22)	(1.33)
Operating expense[3]	(0.43)	(2.61)	(0.28)	(1.68)
Transportation and marketing expense	(0.30)	(1.78)	(0.24)	(1.40)
Estimated operating netback	**5.25**	**31.50**	2.83	16.99
Operating margin[4]	**81%**	**81%**	79%	79%

(1) The PCS Gas Plant processed an average of 127 MMcf per day of gross raw gas at the inlet during the Reporting Period, against a current licensed capacity of 150 MMcf per day.

(2) AECO natural gas spot price averaged $5.71 per Mcf and $3.20 per Mcf in the Reporting Period and Comparable Prior Period, respectively.

(3) The increased operating expense per boe results from reduced third party recoveries as a result of the January 2014 acquisition of a partner's working interest in joint lands, offset by increased volumes of natural gas processed through the PCS Gas Plant.

(4) Operating margin at the PCS Gas Plant is determined by dividing the estimated operating netback by petroleum and natural gas revenue in the period.

MAJOR TRANSACTIONS AFFECTING FINANCIAL RESULTS

Asset Acquisition

Effective January 1, 2014, Birchcliff acquired a partner's 30% working interest in Montney/Doig Resource Play lands and production on the Montney/Doig Natural Gas Resource Play for approximately $56.0 million, giving Birchcliff a 100% working interest in 38 sections of land. Approximately 9.6 MMcfe (1,600 boe per day) of production was acquired, the majority of which goes to Birchcliff's PCS Gas Plant. The acquisition was funded through the Corporation's revolving credit facilities.

Credit Facilities

On May 9, 2014, the aggregate limit of Birchcliff's syndicated credit facilities limit was increased to $750 million from $600 million.

Birchcliff's bank syndicate approved an increase of the revolving credit facilities to an aggregate limit of $620 million from $470 million. The revolving credit facilities were converted to a three year term with a maturity date of May 9, 2017 (the "**Revolving Term Credit Facilities**"). The Revolving Term Credit Facilities include an increased credit limit for the extendible revolving syndicated term credit facility (the "**Syndicated Credit Facility**") of $580 million from $440 million and an increased credit limit for the extendible revolving working capital facility (the "**Working Capital Facility**") of $40 million from $30 million. Birchcliff may each year, at its option, request an extension to the maturity date in of the Syndicated Credit Facility and the Working Capital Facility for an additional period of up to three years from May 9 of the year in which the extension request is made.

The terms of the other credit facilities, a $70 million non-revolving five-year term credit facility maturing on May 25, 2016 and a $60 million non-revolving five-year term credit facility maturing on May 25, 2018, remain essentially unchanged. Birchcliff will no longer be required to make quarterly repayments of $350,000 under the $70 million credit facility.

DISCUSSION OF OPERATIONS

Petroleum and Natural Gas Revenues

Petroleum and natural gas ("**P&NG**") revenues totaled $133.6 million ($46.74 per boe) for the Reporting Period as compared to $75.7 million ($32.22 per boe) for the Comparable Prior Period. The increase in P&NG revenues from the Comparable Prior Period was largely due to improved natural gas prices and increased natural gas production in the Reporting Period. The following table details Birchcliff's P&NG revenues, production and percentage of production and sales price by category:

	Three months ended March 31, 2014				**Three months ended March 31, 2013**			
	Total Revenue *($000)*	**Average Daily Production**	*(%)*	**Average(1)** *($/unit)*	Total Revenue *($000)*	Average Daily Production	*(%)*	Average(1) *($/unit)*
Light oil *(bbls)*	34,826	3,977	13	97.30	30,897	4,047	16	84.82
Natural gas *(Mcf)*	87,004	158,456	83	6.10	39,228	128,101	82	3.40
Natural gas liquids *(bbls)*	11,692	1,362	4	95.35	5,549	710	2	86.80
Total P&NG sales *(boe)*	133,522	**31,749**	100	46.73	75,674	26,108	100	32.21
Royalty revenue	36			0.01	44			0.01
P&NG revenues	**133,558**			**46.74**	75,718			32.22

(1) Average sales price excludes the effect of hedges on financial instruments.

Production

Birchcliff achieved record quarterly production of 31,749 boe per day in the first quarter of 2014, an increase of 22% from 26,108 boe per day in the first quarter of 2013. This increase was largely due to incremental production added from new Montney/Doig horizontal natural gas multi-well pads that were drilled, completed and tied into the PCS Gas Plant throughout 2013 and into the Reporting Period and the addition of approximately 1,600 boe a day of production from the acquisition in January 2014 of a partner's working interest in joint lands, offset by natural production declines.

Production consisted of approximately 83% natural gas and 17% crude oil and natural gas liquids in the first quarter of 2014 as compared to 82% natural gas and 18% crude oil and natural gas liquids in the first quarter of 2013.

Commodity prices

Birchcliff sells all of its light crude oil on a spot basis and the majority of its natural gas production for prices based on the AECO natural gas spot price. The average realized price the Corporation receives for its light crude oil and natural gas production depends on a number of factors including the average benchmark prices for crude oil and natural gas, the US to Canadian dollar exchange rate, transportation and product quality differentials. The following table sets out the average benchmark prices and Birchcliff's average sales price:

	Three months ended March 31, 2014	**Three months ended March 31, 2013**
Average benchmark prices:		
Light oil – WTI Cushing *($USD/bbl)*	98.68	94.37
Light oil – Edmonton Par *($/bbl)*	99.73	88.16
Natural gas – AECO – C daily *($/MMbtu)*(1)	5.71	3.20
Exchange rate – *(USD$/CAD$)*	1.10	0.99
Birchcliff's average sales price(2):		
Light oil *($/bbl)*	97.30	84.82
Natural gas *($/Mcf)*	6.10	3.40
NGLs *($/bbl)*	95.35	86.80
Barrels of oil equivalent *($/boe)*	46.73	32.21

(1) $1.00/MMbtu = $1.00/Mcf based on a standard heat value Mcf.

(2) Average sales price excludes the effect of hedges on financial instruments.

The average benchmark prices for crude oil are impacted by global and regional events that dictate the level of supply and demand for these commodities. The principle benchmark trading exchanges that Birchcliff compares its oil price to are the US benchmark West Texas Intermediate at Cushing, Oklahoma ("**WTI**") spot price and the Canadian Edmonton Par spot price. The differential between WTI USD and Canadian Edmonton Par oil price can widen due to a number of factors including, but not limited to, downtime in North American refineries, rising domestic production, regional bottlenecks and curtailment of key processing infrastructure, high inventory levels in North America and lack of pipeline infrastructure connecting key consuming oil markets.

Natural gas prices are mainly driven by North American supply and demand fundamentals, which can be impacted by a number of factors including weather-related conditions, changing demographics, economic growth, natural gas storage levels, pipeline capacity, drilling rates and technological improvements in extracting natural gas from North American natural gas basins.

The AECO natural gas spot price averaged $5.71 per Mcf for the Reporting Period, a 78% increase from the Comparable Prior Period. This increase was largely attributable to colder-than-normal winter weather in North America which kept demand for natural gas high during the Reporting Period. Birchcliff's realized natural gas sales price at the wellhead averaged $6.10 per Mcf in the Reporting Period which is higher than the posted benchmark prices for that period. Birchcliff receives premium pricing for its natural gas production due to its high heat content. The following table details the average realized sales price and differential received by Birchcliff for its natural gas production:

	Three months ended March 31, 2014	Three months ended March 31, 2013
Average realized natural gas sales price *($/Mcf)*	6.10	3.40
Average natural gas – AECO – C daily *($/MMbtu)*[1]	5.71	3.20
Positive differential	**0.39**	0.20

(1) $1.00/MMbtu = $1.00/Mcf based on a standard heat value Mcf.

Risk Management Contracts

The Corporation has entered into certain commodity price risk management contracts for 2014 in order to reduce volatility in its financial results and protect its cash flow and capital expenditure program. Birchcliff's current strategy is to hedge a portion of its oil and natural gas using a combination of financial derivatives and physical delivery sales contracts to manage commodity risk.

Financial derivatives

As at March 31, 2014, the Corporation had the following financial derivatives in place:

Product	Option traded	Notional quantity	Term	Strike price	Fair value *($000's)*
Crude oil	Put option	500 bbls/day	April 1, 2014 – December 31, 2014	WTI USD $90/bbl	264
Crude oil	Put option	500 bbls/day	April 1, 2014 – December 31, 2014	WTI USD $85/bbl	151
Fair value assets[1]					**415**

(1) The Corporation also recorded approximately $0.9 million as a deferred premium on financial instruments, which represents the amount payable to the counterparty to these contracts at March 31, 2014.

As of March 31, 2014, if the future strip prices for WTI crude oil had been $1.00 USD per bbl higher, with all other variables held constant, after tax net income would have been $0.1 million (March 31, 2013 - NIL) lower.

The following table provides a summary of the realized and unrealized losses on financial derivative contracts:

	Three months ended March 31, 2014		Three months ended March 31, 2013	
	($000's)	*($/boe)*	*($000's)*	*($/boe)*
Realized loss on financial instruments	309	0.10	-	-
Unrealized loss on financial instruments	151	0.05	-	-

There were no financial derivative contracts entered into subsequent to March 31, 2014.

Physical sales contracts

Birchcliff has also entered into physical delivery sales contracts to manage commodity risk. These contracts are considered normal executory sales contracts and are not recorded at fair value in the financial statements. As at March 31, 2014, the Corporation had the following physical sales contracts in place:

Product	Type of contract	Volume	Term(1)	Contract price
Natural gas	AECO fixed price	75,000 GJ/day	April 1, 2014 to October 31, 2014	$3.82 CDN/GJ

(1) Transactions with common terms have been aggregated and presented as the weighted average price.

Birchcliff's total natural gas hedge position for summer 2014 is summarized below:

Product	Term(1)	Average production hedged(2)	Estimated average wellhead price(2)
Natural gas	April 1, 2014 to October 31, 2014	65,908 Mcf/day	$4.35 CDN/Mcf

(1) Transactions with common terms have been aggregated and presented as the weighted average price.

(2) The conversion from GJ to Mcf is based on estimated average natural gas heat content for Birchcliff's Pouce Coupe area of 40.4 MJ/m3.

There were no physical sales contracts entered into subsequent to March 31, 2014.

Royalties

Birchcliff recorded a royalty expense of $12.7 million ($4.43 per boe) for the Reporting Period as compared to $6.4 million ($2.74 per boe) for the Comparable Prior Period. Royalties are paid primarily to the Alberta Government. The following table details the Corporation's royalty expense:

	Three months ended March 31, 2014	Three months ended March 31, 2013
Oil & natural gas royalties *($000)*	12,651	6,427
Oil & natural gas royalties *($/boe)*	4.43	2.74
Effective royalty rate *(%)*(1)	9%	8%

(1) The effective royalty rate is calculated by dividing the aggregate royalties into petroleum and natural gas sales for the period.

The increase in the effective royalty rate from the Comparable Prior Period was mainly due to higher average oil and natural gas wellhead prices received for Birchcliff's production in the current quarter and the effect these higher prices have on the sliding scale royalty calculation, offset by production royalty incentives for a number of wells that are receiving a 5% royalty rate.

Operating Costs

Operating costs were $14.9 million ($5.21 per boe) for the Reporting Period as compared to $13.6 million ($5.77 per boe) for the Comparable Prior Period. Birchcliff continues to focus on controlling the infrastructure it uses to produce its oil and natural gas and on reducing operating costs on a per boe basis. The following table provides a breakdown of operating costs:

	Three months ended March 31, 2014		Three months ended March 31, 2013	
	($000's)	*($/boe)*	*($000's)*	*($/boe)*
Field operating costs	15,185	5.31	14,855	6.32
Recoveries	(277)	(0.09)	(1,679)	(0.71)
Field operating costs, net	14,908	5.22	13,176	5.61
Expensed workovers and other	(9)	(0.01)	376	0.16
Operating costs	**14,899**	**5.21**	13,552	5.77

Corporate operating costs per boe decreased by 10% from the Comparable Prior Period largely due to the continued cost benefits achieved from processing increased incremental volumes of natural gas through the PCS Gas Plant and the implementation of various optimization initiatives, offset by reduced third-party recoveries as a result of the recent acquisition of a partner's 30% working interest in land and production in the Pouce Coupe area.

On a production month basis, operating costs averaged $2.61 per boe at the PCS Gas Plant during the first quarter of 2014, where Birchcliff processed 76% of its total natural gas production.

Transportation and Marketing Expenses

Transportation and marketing expenses were $7.1 million ($2.48 per boe) for the Reporting Period as compared to $5.3 million ($2.25 per boe) for the Comparable Prior Period. The increased aggregate costs are primarily due to higher transportation expenses resulting from increased condensate trucking from the PCS Gas Plant and higher production in the Reporting Period as compared to the Comparable Prior Period.

Operating Netbacks

The following table details Birchcliff's net production and operating netback for the Montney/Doig Natural Gas Resource Play, the Worsley Charlie Lake Light Oil Resource Play and on a corporate basis:

	Three months ended March 31, 2014	Three months ended March 31, 2013
Montney/Doig Natural Gas Resource Play[(1)]		
Average daily production, net:		
Natural gas *(Mcf)*	144,364	113,240
Oil & NGLs *(bbls)*	1,261	512
Total boe *(6:1)*	**25,322**	19,386
% of corporate production[(2)]	***80%***	*74%*
Netback and cost *($ per Mcfe):*		
Petroleum and natural gas revenue	6.59	3.70
Royalty expense	(0.51)	(0.14)
Operating expense, net of recoveries	(0.63)	(0.66)
Transportation and marketing expense	(0.31)	(0.24)
Operating netback	**5.14**	2.66
Worsley Charlie Lake Light Oil Resource Play[(1)]		
Average daily production, net:		
Natural gas *(Mcf)*	9,003	8,165
Oil & NGLs *(bbls)*	3,545	3,257
Total boe *(6:1)*	**5,046**	4,617
% of corporate production[(2)]	***16%***	*18%*
Netback and cost *($ per boe):*		
Petroleum and natural gas revenue	79.50	65.70
Royalty expense	(10.05)	(8.77)
Operating expense, net of recoveries	(10.13)	(9.06)
Transportation and marketing expense	(5.84)	(6.04)
Operating netback	**53.48**	41.83
Total Corporate		
Average daily production, net:		
Natural gas *(Mcf)*	158,456	128,101
Oil & NGLs *(bbls)*	5,339	4,757
Total boe *(6:1)*	**31,749**	26,108
Netback and cost *($ per boe)*		
Petroleum and natural gas revenue	46.74	32.22
Royalty expense	(4.43)	(2.74)
Operating expense, net of recoveries	(5.21)	(5.77)
Transportation and marketing expense	(2.48)	(2.25)
Operating netback	**34.62**	21.46

(1) Most resource plays produce both oil and natural gas, however a resource play is categorized as either a natural gas resource play or an oil resource play based upon the predominate production or play type in that area.

(2) Production from Birchcliff's other conventional oil and natural gas properties were not individually significant during the Reporting Period and Comparable Prior Period.

Montney/Doig Natural Gas Resource Play

Birchcliff's production from the Montney/Doig Natural Gas Resource Play was 25,322 boe per day in the Reporting Period, a 31% increase from the same period in 2013. This increase was largely due to an increased production of natural gas and liquids from new Montney/Doig horizontal natural gas wells that were tied into the PCS Gas Plant throughout 2013 and into the Reporting Period; and the addition of approximately 1,600 boe per day of natural gas production from the acquisition in January 2014 of a partner's working interest in joint lands.

During the first quarter of 2014, Birchcliff's recoveries of liquids from its Montney/Doig natural gas production increased to 8.7 bbls per MMscf, which is an increase of 93% from 4.5 bbls per MMscf in the first quarter of 2013. Of the 8.7 bbls of liquids approximately 8.4 bbls (96%) is high value oil and condensate (C5+), which averaged $97.92 per bbl at the wellhead in the Reporting Period. Any natural gas liquids not recovered from the raw natural gas stream increases the heating value of our sales gas and the resulting sales price.

Birchcliff's operating netback from the Montney/Doig Natural Gas Resource Play was $5.14 per Mcfe ($30.86 per boe) in the Reporting Period, a 93% increase from the same period in 2013. This increase was largely due to higher realized natural gas prices, offset by an increase in royalty and transportation and marketing costs in the Reporting Period.

Worsley Charlie Lake Light Oil Resource Play

Birchcliff's production from the Worsley Charlie Lake Light Oil Resource Play was 5,046 boe per day in the Reporting Period, a 9% increase from the Comparable Prior Period. The increase in production from the Comparable Prior Period is due to prior year infrastructure limitations in a portion of the Worsley field that were resolved in the second half of 2013. Birchcliff's production from the Worsley Charlie Lake Light Oil Resource Play accounted for 16% of corporate production in the Reporting Period.

Operating netback from the Worsley Charlie Lake Light Oil Resource Play was $53.48 per boe in the Reporting Period, a 28% increase from the Comparable Prior Period. On a per boe basis, the increase in operating netback was largely due to higher realized petroleum and natural gas prices, offset by an increase in royalty and operating costs in the Reporting Period.

Administrative Expenses

Net administrative expenses were $6.4 million ($2.23 per boe) for the Reporting Period as compared to $6.2 million ($2.63 per boe) for the Comparable Prior Period. The components of net administrative expenses are detailed in the table below:

	Three months ended March 31, 2014		Three months ended March 31, 2013	
	($000's)	*(%)*	*($000's)*	*(%)*
Cash:				
Salaries and benefits[1]	4,642	59	3,989	56
Other[2]	3,270	41	3,080	44
	7,912	100	7,069	100
Operating overhead recoveries	(62)	(1)	(220)	(3)
Capitalized overhead[3]	(2,445)	(31)	(1,969)	(28)
General & administrative, net	5,405	68	4,880	69
General & administrative, net per boe	$1.89		$2.08	
Non-cash:				
Stock-based compensation	2,164	100	2,368	100
Capitalized stock-based compensation[3]	(1,205)	(56)	(1,065)	(45)
Stock-based compensation, net	959	44	1,303	55
Stock-based compensation, net per boe	$0.34		$0.55	
Administrative expenses, net	**6,364**		6,183	
Administrative expenses, net per boe	**$2.23**		$2.63	

(1) Includes salaries and benefits paid to all Officers and employees of the Corporation.

(2) Includes costs such as rent, legal, tax, insurance, minor computer hardware and software and other business expenses incurred by the Corporation.

(3) Includes a portion of salaries, benefits and stock-based compensation directly attributable to the exploration and development activities of the Corporation which have been capitalized.

A summary of the Corporation's outstanding stock options is presented below:

	Number	Exercise price[1]
Outstanding, December 31, 2013	10,931,520	$8.31
Granted	2,595,500	$8.65
Exercised	(827,116)	($7.21)
Forfeited	(58,068)	($8.34)
Outstanding, March 31, 2014	**12,641,836**	**$8.45**

(1) Determined on a weighted average basis.

At March 31, 2014, there were 2,939,732 performance warrants outstanding with an exercise price of $3.00 (January 31, 2015 expiry) and 6,000,000 warrants outstanding (issued in conjunction with the August 2012 preferred unit equity offering) with an exercise price of $8.30 (August 8, 2014 expiry). Each stock option, performance warrant and warrant entitles the holder to purchase one common share at the exercise price.

Depletion and Depreciation Expenses

Depletion and depreciation ("**D&D**") expenses were $32.0 million ($11.19 per boe) for the Reporting Period as compared to $27.0 million ($11.51 per boe) for the Comparable Prior Period. D&D expenses were higher on an aggregate basis mainly due to a 22% increase in production from the Comparable Prior Period.

D&D is a function of the estimated proved plus probable reserve additions, the finding and development costs attributable to those reserves, the associated future development capital required to recover those reserves and production in the period. The Corporation determines its D&D expenses on an area basis.

Asset impairment assessment

The Corporation's cash-generating units ("**CGU**") are reviewed at each reporting date for both internal and external indicators of potential impairment. Potential CGU impairment indicators include, but are not limited to, changes to Birchcliff's business plan; deterioration in commodity prices; negative changes in technological, economic, legal, capital or operating environment; adverse changes to the physical condition of a CGU; current expectation that a material CGU (or a significant component thereof) is more likely than not to be sold or otherwise disposed of before the end of its previously estimated useful life; non-compliance of financial debt covenants; deterioration in the financial and operational performance of a CGU; net assets exceeding market capitalization; and significant downward revisions of estimated recoverable proved plus probable reserves of a CGU. If impairment indicators exist, an impairment test is performed by comparing a CGU's carrying value to its recoverable amount.

Birchcliff performed an impairment assessment of its petroleum and natural gas assets on a CGU basis and determined there were no impairment triggers identified at the end of the Reporting Period. As a result, no impairment test was required at March 31, 2014.

Finance Expenses

Finance expenses were $5.7 million ($2.00 per boe) for the Reporting Period as compared to $6.8 million ($2.87 per boe) for the Comparable Prior Period. The components of the Corporation's finance expenses are shown in the table below:

	Three months ended March 31, 2014		Three months ended March 31, 2013	
	($000's)	*($/boe)*	*($000's)*	*($/boe)*
Cash:				
Interest on credit facilities	4,852	1.70	6,104	2.59
Non-cash:				
Accretion on decommissioning obligations	603	0.21	462	0.20
Amortization of deferred financing fees	259	0.09	188	0.08
Finance expenses	**5,714**	**2.00**	6,754	2.87

The aggregate interest expense is impacted by pricing margins established under Birchcliff's bank credit agreements, which are used to determine Birchcliff's average effective interest rate, and the average balance outstanding under its bank credit facilities during the period.

The effective interest rate applicable to the revolving working capital facility was 4.8% at the end of the Reporting Period as compared to 6.0% at the end of the Comparable Prior Period. The effective interest rate applicable to the bankers' acceptances issued under the revolving syndicated credit facility was 4.1% in the Reporting Period as compared to 5.5% in the Comparable Prior Period. The effective interest rate applicable to the bankers' acceptances issued under the non-revolving term credit facilities was 4.7% in the Reporting Period as compared to 5.6% in the Comparable Prior Period.

Birchcliff's average outstanding total credit facilities balance was approximately $447 million in the Reporting Period as compared to $439 million in the Comparable Prior Period, calculated as the simple average of the month end amounts.

Income Taxes

Birchcliff recorded an income tax expense of $14.0 million ($4.92 per boe) for the Reporting Period as compared to $3.0 million ($1.29 per boe) for the Comparable Prior Period. The components of income tax expense are shown in the table below:

($000's)	**Three months ended March 31, 2014**	**Three months ended March 31, 2013**
Deferred income tax expense	13,294	2,633
Dividend tax expense on preferred shares	750	400
Income tax expense	**14,044**	3,033

The increase in income tax expense from the Comparable Prior Period was largely due to higher recorded net income before taxes, which resulted in increased deferred income tax expense in the Reporting Period.

The Corporation's estimated income tax pools were $1.3 billion at March 31, 2014. Management expects that future taxable income will be available to utilize the accumulated tax pools. The components of the Corporation's estimated income tax pools are shown in the table below:

($000's)	**Tax pools as at March 31, 2014**
Canadian oil and gas property expense	279,531
Canadian development expense	301,626
Canadian exploration expense	185,895
Undepreciated capital costs	220,446
Non-capital losses	318,356
Financing costs	4,804
Estimated income tax pools	**1,310,658**

The Corporation's 2006 and 2007 income tax filings were reassessed by the Canada Revenue Agency ("**CRA**") in 2011. The reassessments are based on the CRA's determination that the tax pools available to Veracel Inc. ("**Veracel**"), prior to the amalgamation, ceased to be available to Birchcliff after the amalgamation.

The Veracel tax pools in dispute totaled $39.3 million and include approximately $16.2 million in non-capital losses, $15.6 million in scientific research and experimental development expenditures and $7.5 million in investment tax credits. The disputed assessments are outstanding at March 31, 2014. A trial of the matter was held in the Federal Court of Canada in November 2013 and Birchcliff is now awaiting the Court's decision.

The resolution of the disputed assessments may impact future income tax expense but will not impact cash taxes payable by the Corporation. Management believes that it will be successful in defending its tax position respecting the Veracel transaction, and as such, the Corporation has not recognized a related provision for the deferred income tax liability at March 31, 2014.

CAPITAL EXPENDITURES

The following table sets forth a summary of the Corporation's capital expenditures:

($000's)	Three months ended March 31, 2014	Three months ended March 31, 2013
Land	9,064	24,264
Seismic	5,384	121
Workovers	2,952	1,944
Drilling and completions	66,942	42,145
Well equipment and facilities	20,230	12,039
Finding and development costs (F&D)	104,572	80,513
Acquisitions	56,553	-
Dispositions	-	(4)
Finding, development and acquisition costs (FD&A)	161,125	80,509
Administrative assets	278	501
Capital expenditures, net	**161,403**	81,010

Net capital expenditures of $161.4 million in the Reporting Period include approximately $56.0 million (35%) on acquiring a partner's working interest in land and production on the Montney/Doig Natural Gas Resource Play, $53.2 million (33%) on drilling and completing new Montney/Doig horizontal natural gas wells to be tied into the PCS Gas Plant and the remaining $52.2 million (32%) on other Crown land purchases, expansion of the Montney/Doig Natural Gas Resource Play and the Worsley Charlie Lake Light Oil Resource Play, and on other oil and gas exploration, development and infrastructure projects in the Peace River Arch.

In the first quarter of 2014, Birchcliff drilled a total of 15 (15.0 net) wells, consisting of 7 (7.0 net) Montney/Doig horizontal natural gas wells, 2 (2.0 net) Montney/Doig horizontal oil wells; 1 (1.0 net) Upper Doig horizontal oil well; and 5 (5.0 net) Charlie Lake horizontal oil wells.

CAPITAL RESOURCES AND LIQUIDITY

Capital Resources

The following table sets forth a summary of the Corporation's capital resources:

($000's)	Three months ended March 31, 2014	Three months ended March 31, 2013
Funds flow from operations	88,369	39,444
Changes in non-cash working capital from operations	(14,251)	(4,093)
Decommissioning expenditures	(808)	(41)
Exercise of stock options	5,966	3,035
Dividends paid on preferred shares	(1,875)	(1,000)
Net change in non-revolving term credit facilities	(317)	44
Net change in revolving credit facilities	59,941	18,926
Changes in non-cash working capital from investing	24,378	24,695
Capital resources	**161,403**	81,010

Working Capital

The Corporation's working capital deficit (current assets minus current liabilities, excluding the fair value of financial instruments and related deferred premium) increased to $70.9 million at March 31, 2014 from $60.1 million at December 31, 2013. The deficit at the end of the Reporting Period is largely comprised of costs incurred from the drilling and completion of new wells.

At March 31, 2014, the major components of Birchcliff's current assets were joint interest billings to be received from its partners (10%) and revenue to be received from its marketers in respect of March 2014 production (87%), which was subsequently received in April 2014. In contrast, current liabilities largely consisted of trade and joint venture payables (55%) and accrued capital and operating costs (37%). Birchcliff routinely assesses the financial strength of its marketers and joint venture partners in accordance with the Corporation's credit risk guidelines. At this time, Birchcliff expects that such counterparties will be able to meet their financial obligations.

Birchcliff manages its working capital deficit using funds flow from operations and advances under bank credit facilities. The Corporation's working capital deficit does not reduce the amount available under its bank credit facilities. The Corporation did not identify any liquidity issues with respect to the operation of its petroleum and natural gas business during the Reporting Period.

Long-Term Bank Debt

At March 31, 2014, the amount outstanding under the Corporation's long-term bank credit facilities was $453.8 million (December 31, 2013 - $394.0 million), which is net of $2.9 million (December 31, 2013 - $2.3 million) in unamortized interest and fees. Birchcliff's available credit facilities aggregate to approximately $600 million at March 31, 2014.

Total debt, including the working capital deficit, was $524.7 million at March 31, 2014 as compared to $454.0 million at December 31, 2013. Total debt from the end of 2013 increased by $70.7 million, largely due to the $56.0 million acquisition and capital spent in excess of funds flow in the Reporting Period.

A significant portion of the funds drawn under Birchcliff's bank credit facilities during the Reporting Period was to pay costs relating to the drilling and completion of new Montney/Doig horizontal natural gas wells and the $56.0 million acquisition of a partner's 30% working interest in land and production on the Montney/Doig Natural Gas Resource Play.

The following table shows the Corporation's unused bank credit facilities:

As at, *($000's)*	**March 31, 2014**	**December 31, 2013**
Maximum borrowing base limit[(1)(2)]:		
Non-revolving term credit facilities[(3)]	128,950	129,300
Revolving credit facilities	470,000	470,000
	598,950	599,300
Principal amount utilized:		
Drawn non-revolving term credit facilities[(4)]	(128,950)	(129,300)
Drawn revolving credit facilities[(4)]	(329,166)	(268,411)
Outstanding letters of credit[(5)]	(184)	(184)
	(458,300)	(397,895)
Unused credit	**140,650**	201,405

(1) The Corporation's credit facilities are subject to a semi-annual review of the borrowing base limit, which is directly impacted by the value of Birchcliff's petroleum and natural gas reserves.

(2) The quarterly financial covenants applicable to the Corporation's credit facilities include (i) an interest coverage ratio, which is calculated on a historical rolling four quarter basis, as earnings before interest and non-cash items including income taxes, stock-based compensation, gains and losses on sale of assets, unrealized gains and losses on financial instruments and depletion, depreciation and amortization ("**EBITDA**") divided by interest expense; and (ii) a debt to EBITDA ratio. Interest expense for this purpose means total interest charges on borrowings with respect to all outstanding indebtedness and all preferred share dividends declared and paid in the period. Debt for this purpose means indebtedness for borrowed money, as determined at the end of the reporting period, and includes outstanding debt under the Corporation's credit facilities as shown on the statements of financial position before unamortized deferred financing fees and including outstanding letters of credit, but does not include working capital deficiency and capital securities.

The Corporation is required to ensure that on the last day of each quarter, the ratio of EBITDA to interest expense, determined on a historical rolling four quarter basis equals or exceeds 3.5:1.0 and the ratio of debt to EBITDA, determined on a historical rolling four quarter basis does not exceed 4.0:1.0. At March 31, 2014, Birchcliff's EBITDA to interest expense was 9.0:1.0 and debt to EBITDA was 1.8:1.0. The Corporation was compliant with all financial covenants under its credit facilities as at March 31, 2014 and December 31, 2013.

(3) The $70 million non-revolving five-year term credit facility requires quarterly principle repayments of $350,000 which commenced on July 1, 2013.

(4) The drawn amounts are not reduced for unamortized costs and fees associated with each credit facility.

(5) Letters of credit are issued to various service providers. There were no amounts drawn on the letters of credit during the periods ended March 31, 2014 and December 31, 2013.

Contractual Obligations

The Corporation enters into contractual obligations in the ordinary course of conducting its day-to-day business. The following table lists Birchcliff's estimated material contractual obligations at March 31, 2014:

($000's)	**2014**	**2015**	**2016 - 2018**
Accounts payable and accrued liabilities	118,388	-	-
Drawn non-revolving term credit facilities	1,050	1,400	126,500
Drawn revolving credit facilities	-	-	329,166
Office lease[(1)]	2,618	3,490	6,690
Transportation and processing	13,547	10,567	8,573
Deferred premium on risk management contracts	944	-	-
Estimated contractual obligations[(2)]	**136,547**	**15,457**	**470,929**

(1) The Corporation is committed under an operating lease relating to its office premises, beginning December 1, 2007 and expiring on November 30, 2017. Effective December 1, 2012, Birchcliff is committed to the entire leased premise and has not sublet any excess space to an arm's length party.

(2) Contractual commitments that are routine in nature and form part of the normal course of operations for Birchcliff are not included. The Corporation's decommissioning obligations are excluded from the table as these obligations arose from a regulatory requirement rather than from a contractual arrangement. Birchcliff estimates the total undiscounted cash flow to settle its decommissioning obligations on its wells and facilities at March 31, 2014 to be approximately $152.6 million and will be incurred as follows: 2015 - $6.9 million and $145.7 million thereafter. The estimate for determining the undiscounted decommissioning obligations requires significant assumptions on both the abandonment cost and timing of the decommissioning and therefore the actual obligation may differ materially.

Birchcliff's Series C Preferred Shares, which are redeemable by their holders after June 30, 2020, have not been included in this table as they are not contractual obligations of the Corporation at the end of the Reporting Period. Upon receipt of a notice of redemption, the Corporation has an obligation to redeem the Series C Preferred Shares, at its option, in cash or common shares.

Off-Balance Sheet Transactions

Birchcliff was not involved in any off-balance sheet transactions that would result in a material change to its financial position, performance or cash flows during the Reporting Period and Comparable Prior Period.

OUTSTANDING SHARE INFORMATION

At March 31, 2014, Birchcliff had outstanding common shares, Series A Preferred Shares, Series C Preferred Shares and warrants issued in conjunction with the Series A Preferred Shares. Birchcliff's common shares began trading on the TSX on July 21, 2005 under the symbol "**BIR**" and were at the same time de-listed from the TSX Venture Exchange where they were trading under the same symbol prior to such time. Birchcliff's common shares are included in the S&P/TSX Composite Index. Birchcliff's Series A Preferred Shares, Series C Preferred Shares and warrants are individually listed on the TSX under the symbols "**BIR.PR.A**", "**BIR.PR.C**" and "**BIR.WT**", respectively.

The following table summarizes the common shares issued:

	Common shares
Balance at December 31, 2013	143,676,661
Issue of common shares upon exercise of options	827,116
Balance at March 31, 2014	**144,503,777**

As of May 13, 2014, there were outstanding 145,008,843 common shares; 2,000,000 Series A Preferred Shares; 2,000,000 Series C Preferred Shares; 12,193,370 stock options to purchase an equivalent number of common shares; 2,939,732 performance warrants to purchase an equivalent number of common shares; and 5,990,000 warrants to purchase an equivalent number of common shares.

On March 12, 2014, the Board of Directors declared a quarterly cash dividend of $1.0 million or $0.50 per Series A Preferred Share and $0.875 million or $0.4375 per Series C Preferred Share for the calendar quarter ending March 31, 2014. Both dividends are designated as an eligible dividend for purposes of the *Income Tax Act* (Canada).

SUMMARY OF QUARTERLY RESULTS

The following are the quarterly results of the Corporation for the eight most recently completed quarters:

Quarter ending,	Mar.31 2014	Dec. 31, 2013	Sep. 30, 2013	Jun. 30, 2013	Mar. 31, 2013	Dec. 31, 2012	Sep. 30, 2012	Jun. 30, 2012
Average daily production *(boe 6:1)*	**31,749**	28,391	24,662	24,141	26,108	26,655	21,426	22,039
Realized natural gas price *($/Mcf)*	**6.10**	3.81	2.60	3.78	3.40	3.43	2.47	2.05
Realized oil price *($/bbl)*	**97.30**	81.52	102.82	91.19	84.82	83.38	82.45	81.45
Total revenues *($000's)*	**133,558**	89,092	72,762	79,065	75,718	78,001	58,643	57,729
Operating costs *($/boe)*	**5.21**	5.44	5.66	5.89	5.77	5.88	6.01	6.22
Capital expenditures, net *($000's)*	**161,403**	18,188	76,186	40,386	81,010	32,137	88,099	58,815
Funds flow from operations *($000's)*	**88,369**	50,060	43,053	41,804	39,444	39,848	28,230	25,985
Per common share - basic *($)*	**0.61**	0.35	0.30	0.29	0.28	0.28	0.20	0.19
Per common share - diluted *($)*	**0.60**	0.34	0.30	0.29	0.27	0.28	0.20	0.19
Net income *($000's)*	**39,499**	37,062	10,156	10,775	7,424	6,305	2,744	416
Net income to common shareholders *($000's)*[(1)]	**38,499**	36,062	9,156	9,775	6,424	5,305	2,165	416
Per common share - basic *($)*	**0.27**	0.25	0.06	0.07	0.05	0.04	0.02	-
Per common share - diluted *($)*	**0.26**	0.25	0.06	0.07	0.04	0.04	0.02	-
Total assets *($000's)*	**1,729,994**	1,586,531	1,558,456	1,513,772	1,498,753	1,430,324	1,420,582	1,350,759
Long-term bank debt *($000's)*	**453,772**	393,967	444,719	409,091	451,371	432,563	390,541	400,876
Total debt *($000's)*[(2)]	**524,720**	454,038	487,707	453,123	502,291	462,130	468,184	455,708
Dividends on preferred shares (Series A) *($000's)*	**1,000**	1,000	1,000	1,000	1,000	1,000	579	-
Dividends on preferred shares (Series C) *($000's)*	**875**	875	1,038	-	-	-	-	-
Preferred shares outstanding (Series A) *(000's)*	**2,000**	2,000	2,000	2,000	2,000	2,000	2,000	-
Preferred shares outstanding (Series C) *(000's)*	**2,000**	2,000	2,000	2,000	-	-	-	-
Common shares outstanding *(000's)*								
Basic	**144,504**	143,677	142,752	142,390	142,096	141,596	141,535	141,434
Diluted	**166,085**	163,548	163,396	164,110	164,107	162,997	162,946	157,232
Wtd. average common shares outstanding *(000's)*								
Basic	**144,026**	143,063	142,549	142,240	141,821	141,585	141,474	138,426
Diluted	**147,090**	145,319	145,087	145,165	144,366	144,239	143,572	138,837

(1) Reduced for Series A Preferred Share dividends paid in the period.

(2) Includes the aggregate amounts outstanding under Birchcliff's long term bank debt and working capital deficit at the end of the period and excludes the fair value of financial instruments and related deferred premium.

Production was higher compared to the fourth quarter of 2013 and the first quarter of 2013 largely due to incremental production gains from new Montney/Doig horizontal natural gas multi-well pads that were drilled, completed and tied into the PCS Gas Plant throughout 2013 and into the Reporting Period and the addition of approximately 1,600 boe a day of production from the acquisition in January 2014 of a partner's working interest in joint lands, offset by natural production declines.

The Corporation achieved record quarterly funds flow of $88.4 million in the first quarter of 2014, an increase of 77% from $50.1 million in the fourth quarter of 2013 and an increase of 124% from $39.4 million in the first quarter of 2013. The increase in funds flow from the comparative quarters was mainly due to higher realized oil and natural gas prices and increased natural gas production in the Reporting Period.

Birchcliff continued to report significant positive earnings in the first quarter of 2014, an increase of 499% to $38.5 million from $6.4 million in the first quarter of 2013. This increase was mainly attributable to higher funds flow in the first quarter of 2014, offset by higher income taxes and depletion expense in the Reporting Period.

Excluding a gain on sale of assets of $33.8 million ($25.3 million, net of tax) in the fourth quarter of 2013, net income to common shareholders was up 259% from the previous quarter mainly due to higher funds flow, offset by higher income taxes and depletion expense in the Reporting Period.

POTENTIAL TRANSACTIONS

Within its focus area, the Corporation is always reviewing potential property acquisitions and corporate mergers and acquisitions for the purpose of determining whether any such potential transaction is of interest to the Corporation, as well as the terms on which such a potential transaction would be available. As a result, the Corporation may from time to time be involved in discussions or negotiations with other parties or their agents in respect of potential property acquisitions and corporate merger and acquisition opportunities. The Corporation is not committed to any such potential transaction and cannot be reasonably confident that it can complete any such potential transaction until appropriate legal documentation has been signed by the relevant parties.

CONTROLS AND PROCEDURES

Disclosure Controls and Procedures

The Corporation has established and maintained disclosure control and procedures ("**DC&P**") that have been designed by, or under the supervision of, the Corporation's Chief Executive Officer and the Chief Financial Officer ("**Certifying Officers**") to provide reasonable assurance that information required to be disclosed by the Corporation in its annual filings, interim filings or other reports filed or submitted under securities legislation is accumulated and communicated to management, as appropriate, to allow timely decisions regarding required disclosure. The Certifying Officers have evaluated, or caused to be evaluated under their supervision, the effectiveness of the Corporation's DC&P at March 31, 2014 and have concluded that the Corporation's DC&P are appropriately designed and operating effectively to provide reasonable assurance that information required by securities legislation to be disclosed is made known to them by others, to allow timely decisions regarding the required disclosure.

While the Certifying Officers believe that the Corporation's DC&P provide a reasonable level of assurance and are effective, they do not expect that the DC&P will prevent all errors and fraud. A control system, no matter how well conceived, maintained and operated, can provide only reasonable, but not absolute, assurance that the objectives of the control system will be met.

Internal Controls over Financial Reporting

The Corporation has established and maintains internal controls over financial reporting ("**ICFR**") that have been designed using the Committee of Sponsoring Organizations "Internal Control Over Financial Reporting - Guidance for Smaller Public Companies". The control framework was designed by, or under the supervision of, the Corporation's Certifying Officers to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with the generally accepted accounting principles applicable to the Corporation and to provide reasonable assurance that all assets are safeguarded and transactions are appropriately authorized and recorded to facilitate the preparation of relevant, reliable and timely information. The Certifying Officers have evaluated, or caused to be evaluated under their supervision, the effectiveness of the Corporation's ICFR at March 31, 2014 and have concluded that the Corporation's ICFR was effective at March 31, 2014 for the purposes described above. No changes were made to the Corporation's ICFR during the Reporting Period that have materially affected, or are reasonably likely to materially affect the Corporation's ICFR.

While the Certifying Officers believe that the Corporation's ICFR provide a reasonable level of assurance and are effective, they do not expect that the ICFR will prevent all errors and fraud. A control system, no matter how well conceived, maintained and operated, can provide only reasonable, but not absolute, assurance that the objectives of the control system will be met.

CRITICAL ACCOUNTING ESTIMATES

The preparation of the financial statements requires management to make judgments, estimates and assumptions that affect the application of IFRS accounting policies; reported amounts of assets and liabilities; and income and expenses. Accordingly, actual results may differ from these estimates. Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimates are revised and in any future periods affected.

Critical Judgements in Applying Accounting Policies

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

Identification of cash-generating units

Birchcliff's assets are aggregated into CGU's for the purpose of calculating impairment based on their ability to generate largely independent cash inflows. CGU's have been determined based on similar geological structure, shared infrastructure, geographical proximity, operating structure, commodity type and similar exposures to market risks. By their nature, these assumptions are subject to management's judgement and may impact the carrying value of the Corporation's assets in future periods.

Identification of impairment indicators

IFRS requires Birchcliff to assess, at each reporting date, whether there are any indicators that its assets may be impaired. Birchcliff is required to consider information from both external sources (such as negative downturn in commodity prices, significant adverse changes in the technological, market, economic or legal environment in which the entity operates) and internal sources (such as downward revisions in reserves, significant adverse effect on the financial and operational performance of a CGU, evidence of obsolescence or physical damage to the asset). By their nature, these assumptions are subject to management's judgement and may impact the carrying value of the Corporation's assets in future periods.

Tax uncertainties

IFRS requires Birchcliff, at each reporting date, to make certain judgements on uncertain tax positions by relevant tax authorities. Judgements include determining whether the Corporation will "more likely than not" be successful in defending its tax positions by considering information from relevant tax interpretations and tax laws in Canada. As such, this recognition threshold is subject to management's judgement and may impact the carrying value of the Corporation's deferred tax assets and liabilities at the end of the reporting period.

Key Sources of Estimation Uncertainty

The following are the key assumptions concerning the sources of estimation uncertainty at the end of the reporting period, that have a significant risk of causing adjustments to the carrying amounts of assets and liabilities within the next financial year.

Reserves

Reported recoverable quantities of proved and probable reserves requires estimation regarding production profile, commodity prices, exchange rates, remediation costs, timing and amount of future development costs, and production, transportation and marketing costs for future cash flows. It also requires interpretation of geological and geophysical models in order to make an assessment of the size, shape, depth and quality of reservoirs, and their anticipated recoveries. The economical, geological and technical factors used to estimate reserves may change from period to period. Changes in reported reserves can impact the carrying values of the Corporation's petroleum and natural gas properties and equipment, the calculation of depletion and depreciation, the provision for decommissioning obligations, and the recognition of deferred tax assets due to changes in expected future cash flows. The recoverable quantities of reserves and estimated cash flows from Birchcliff's petroleum and natural gas interests are independently evaluated by reserve engineers at least annually.

The Corporation's petroleum and natural gas reserves represent the estimated quantities of petroleum, natural gas and natural gas liquids which geological, geophysical and engineering data demonstrate with a specified degree of certainty to be economically recoverable in future years from known reservoirs and which are considered commercially producible. Such reserves may be considered commercially producible if management has the intention of developing and producing them and such intention is based upon (i) a reasonable assessment of the future economics of such production; (ii) a reasonable expectation that there is a market for all or substantially all the expected petroleum and natural gas production; and (iii) evidence that the necessary production, transmission and transportation facilities are available or can be made available. Reserves may only be considered proven and probable if producibility is supported by either production or conclusive formation tests. Birchcliff's oil and gas reserves are determined in accordance with the standards contained in National Instrument 51-101 *Standard of Disclosures for Oil and Gas Activities and the Canadian Oil and Gas Evaluation Handbook*.

Share-based payments

All equity-settled, share-based awards issued by the Corporation are fair valued using the Black-Scholes option-pricing model. In assessing the fair value of equity-based compensation, estimates have to be made regarding the expected volatility in share price, option life, dividend yield, risk-free rate and estimated forfeitures at the initial grant date.

Decommissioning obligations

The Corporation estimates future remediation costs of production facilities, wells and pipelines at different stages of development and construction of assets or facilities. In most instances, removal of assets occurs many years into the future. This requires an estimate regarding abandonment date, future environmental and regulatory legislation, the extent of reclamation activities, the engineering methodology for estimating cost, future removal technologies in determining the removal cost and liability-specific discount rates to determine the present value of these cash flows.

Impairment of non-financial assets

For the purposes of determining the extent of any impairment or its reversal, estimates must be made regarding future cash flows taking into account key assumptions including future petroleum and natural gas prices, expected forecasted production volumes and anticipated recoverable quantities of proved and probable reserves. These assumptions are subject to change as new information becomes available. Changes in economic conditions can also affect the rate used to discount future cash flow estimates. Changes in the aforementioned assumptions could affect the carrying amount of the Corporation's assets, and impairment charges and reversal will affect profit or loss.

Income taxes

Birchcliff files corporate income tax, goods and service tax and other tax returns with various provincial and federal taxation authorities in Canada. There can be differing interpretations of applicable tax laws and regulations. The resolution of these tax positions through negotiations or litigation with tax authorities can take several years to complete. The Corporation does not anticipate that there will be any material impact upon the results of its operations, financial position or liquidity.

Tax provisions are based on enacted or substantively enacted laws. Changes in those laws could affect amounts recognized in profit or loss both in the period of change, which would include any impact on cumulative provisions, and in future periods.

Deferred tax assets (if any) are recognized only to the extent it is considered probable that those assets will be recoverable. This involves an assessment of when those deferred tax assets are likely to reverse and a judgment as to whether or not there will be sufficient taxable profits available to offset the tax assets when they do reverse. This requires assumptions regarding future profitability and is therefore inherently uncertain. Estimates of future taxable income are based on forecasted cash flows from operations. To the extent that any interpretation of tax law is challenged by the tax authorities or future cash flows and taxable income differ significantly from estimates, the ability of Birchcliff to realize the deferred tax assets recorded at the balance sheet date could be impacted.

ADOPTION OF NEW ACCOUNTING STANDARD

Effective January 1, 2014, the Corporation adopted IFRIC 21 *Levies*, which addresses payments made to government bodies. There was no impact to the Corporation's interim condensed financial statements as a result of adopting this new standard.

ADVISORIES

Unaudited numbers: *All financial amounts referred to in this MD&A and the Corporation's first quarter report for the Reporting Period and the Comparable Prior Period ("**Q1 Report**") are management's best estimates and are unaudited.*

Non-GAAP measures: *This MD&A and the Q1 Report uses uses "funds flow", "funds flow from operations", "funds flow netback", "funds flow per common share", "netback", "operating netback", "estimated operating netback" and "operating margin", which do not have standardized meanings prescribed by generally accepted accounting principles ("**GAAP**") and therefore may not be comparable measures to other companies where similar terminology is used. Netback or operating netback denotes petroleum and natural gas revenue less royalties, less operating expenses and less transportation and marketing expenses. Operating costs at the PCS Gas Plant are calculated on a production month basis. Estimated operating netback of the PCS Gas Plant (and the components thereof) is based upon certain cost allocations and accruals directly related to the PCS Gas Plant and the related wells and infrastructure, calculated on a production month basis. Funds flow, funds flow netback or funds flow from operations denotes cash flow from operating activities as it appears on the Corporation's statements of cash flows before decommissioning expenditures and changes in non-cash working capital. Funds flow, funds flow netback or funds flow from operations is derived from net income plus income tax expense, depletion and depreciation expense, accretion expense, stock-based compensation expense, amortization of deferred financing fees and gains on divestitures. Funds flow per common share denotes funds flow divided by the weighted average number of common shares. Operating margin is calculated by dividing the estimated operating netback for the period by the petroleum and natural gas revenue for the period.*

Boe Conversions: *Barrel of oil equivalent ("**boe**") amounts have been calculated by using the conversion ratio of six thousand cubic feet (6 Mcf) of natural gas to one barrel of oil (1 bbl). Boe amounts may be misleading, particularly if used in isolation. A boe conversion ratio of 6 Mcf to 1 bbl is based on an energy equivalency conversion method primarily applicable at the burner tip and does not represent a value equivalency at the wellhead.*

Mcfe Conversions: *Thousands of cubic feet of gas equivalent ("**Mcfe**") amounts have been calculated by using the conversion ratio of one barrel of oil (1 bbl) to six thousand cubic feet (6 Mcf) of natural gas. Mcfe amounts may be misleading, particularly if used in isolation. A conversion ratio of 1 bbl to 6 Mcf is based on an energy equivalency conversion method primarily applicable at the burner tip and does not represent a value equivalency at the wellhead.*

MMbtu pricing conversions: *\$1.00 per MMbtu equals \$1.00 per Mcf based on a standard heat value Mcf.*

Forward-Looking Information: *This MD&A and the Q1 Report contains forward-looking information within the meaning of applicable Canadian securities laws. Forward-looking information relates to future events or future performance and is based upon the Corporation's current internal expectations, estimates, projections, assumptions and beliefs. All information other than historical fact is forward-looking information. Information relating to reserves and resources is forward-looking as it involves the implied assessment, based on certain estimates and assumptions, that the reserves and resources exist in the quantities estimated and that they will be commercially viable to produce in the future. Words such as "plan", "expect", "project", "intend", "believe", "anticipate", "estimate", "forecast', "may", "will", "potential", "proposed" and other similar words that convey certain events or conditions "may" or "will" occur are intended to identify forward-looking information. In particular, this MD&A and the Q1 Report contains forward-looking information relating to estimated annual and average production for 2014;*

planned exit production increases; planned 2014 capital spending and sources of fudning; anticipated reduction of operating costs on a per boe basis; the intention to drill and complete future wells; an expansion of the PCS Gas Plant; and expected future reserves and resource additions.

The forward-looking information is based upon assumptions as to future commodity prices, currency exchange rates, inflation rates, well production rates, well drainage areas, success rates for future drilling and availability of labour and services. With respect to estimates of reserves and resource volumes, a key assumption is the validity of the data used by Deloitte in their independent reserves evaluation and resource assessments. With respect to numbers of future wells to be drilled, a key assumption is that geological and other technical interpretations performed by the Corporation's technical staff, which indicate that commercially economic volumes can be recovered from the Corporation's lands as a result of drilling future wells, are valid. Estimates as to 2014 exit production rates assume that no unexpected outages occur in the infrastructure that the Corporation relies on to produce its wells, that existing wells continue to meet production expectations and future wells scheduled to come on production in 2014 meet timing and production expectations.

Undue reliance should not be placed on forward-looking information, as there can be no assurance that the plans, intentions or expectations upon which they are based will occur. Although the Corporation believes that the expectations reflected in the forward-looking statements are reasonable, there can be no assurance that such expectations will prove to be correct. As a consequence, actual results may differ materially from those anticipated.

Forward-looking information necessarily involves both known and unknown risks associated with oil and gas exploration, production, transportation and marketing such as uncertainty of geological and technical data, imprecision of reserves and resource estimates, operational risks, environmental risks, loss of market demand, general economic conditions affecting ability to access sufficient capital, changes in governmental regulation of the oil and gas industry and competition from others for scarce resources.

The foregoing list of risk factors is not exhaustive. Additional information on these and other risk factors that could affect operations or financial results are included in the Corporation's most recent Annual Information Form and in other reports filed with Canadian securities regulatory authorities. Forward-looking information is based on estimates and opinions of management at the time the information is presented. The Corporation is not under any duty to update the forward-looking information after the date of this MD&A and the Q3 Report to conform such information to actual results or to changes in the Corporation's plans or expectations, except as otherwise required by applicable securities laws.

Birchcliff Energy Ltd.
Condensed Statements of Financial Position

Unaudited (Expressed in thousands of Canadian dollars)

As at,	March 31, 2014	December 31, 2013
ASSETS		
Current assets:		
Cash	**96**	96
Accounts receivable	**47,750**	37,022
Prepaid expenses and deposits	**994**	1,138
Fair value of financial instruments *(Note 11)*	**415**	826
	49,255	39,082
Non-current assets:		
Exploration and evaluation *(Note 3)*	**2,328**	2,264
Petroleum and natural gas properties and equipment *(Note 4)*	**1,678,411**	1,545,185
	1,680,739	1,547,449
Total assets	**1,729,994**	1,586,531
LIABILITIES		
Current liabilities:		
Accounts payable and accrued liabilities	**118,388**	96,927
Non-revolving term credit facilities *(Note 5)*	**1,400**	1,400
Deferred premium on financial instruments *(Note 11)*	**944**	1,205
	120,732	99,532
Non-current liabilities:		
Non-revolving term credit facilities *(Note 5)*	**126,884**	127,144
Revolving credit facilities *(Note 6)*	**326,888**	266,823
Decommissioning obligations *(Note 7)*	**75,890**	73,433
Deferred income taxes	**70,421**	57,127
Capital securities *(Note 8)*	**48,064**	47,986
	648,147	572,513
Total liabilities	**768,879**	672,045
SHAREHOLDERS' EQUITY		
Share capital *(Note 8)*		
Common shares	**702,932**	694,183
Preferred shares *(perpetual)*	**41,434**	41,434
Contributed surplus	**59,500**	60,119
Retained earnings	**157,249**	118,750
	961,115	914,486
Total shareholders' equity and liabilities	**1,729,994**	1,586,531

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

Approved by the Board

(signed) "Larry A. Shaw"

Larry A. Shaw
Director

(signed) "A. Jeffery Tonken"

A. Jeffery Tonken
Director

Birchcliff Energy Ltd.

Condensed Statements of Net Income and Comprehensive Income

Unaudited (Expressed in thousands of Canadian dollars, except per share information)

Three months ended,	March 31, 2014	March 31, 2013
REVENUE		
Petroleum and natural gas sales	133,558	75,718
Royalties	(12,651)	(6,427)
Net revenue from oil and natural gas sales	120,907	69,291
Realized loss on financial instruments *(Note 11)*	(309)	-
Unrealized loss on financial instruments *(Note 11)*	(151)	-
	120,447	69,291
EXPENSES		
Operating	14,899	13,552
Transportation and marketing	7,073	5,311
Administrative, net	6,364	6,183
Depletion and depreciation *(Note 4)*	31,979	27,034
Finance	5,714	6,754
Dividends on capital securities *(Note 8)*	875	-
	66,904	58,834
INCOME BEFORE TAXES	53,543	10,457
Income tax expense	14,044	3,033
NET INCOME AND COMPREHENSIVE INCOME	39,499	7,424
Net income per common share *(Note 8)*		
Basic	$0.27	$0.05
Diluted	$0.26	$0.04

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

Birchcliff Energy Ltd.
Condensed Statements of Changes in Shareholders' Equity

Unaudited (Expressed in thousands of Canadian dollars)

	Share Capital				
	Common Shares	**Preferred Shares**	**Contributed Surplus**	**Retained Earnings**	**Total**
As at December 31, 2012	677,802	41,434	57,678	57,333	834,247
Dividends on perpetual preferred shares	-	-	-	(1,000)	(1,000)
Exercise of stock options	4,459	-	(1,424)	-	3,035
Stock-based compensation	-	-	2,368	-	2,368
Net income and comprehensive income	-	-	-	7,424	7,424
As at March 31, 2013	682,261	41,434	58,622	63,757	846,074
As at December 31, 2013	694,183	41,434	60,119	118,750	914,486
Dividends on perpetual preferred shares *(Note 8)*	-	-	-	(1,000)	(1,000)
Exercise of stock options *(Notes 8 and 9)*	8,749	-	(2,783)	-	5,966
Stock-based compensation *(Notes 9)*	-	-	2,164	-	2,164
Net income and comprehensive income	-	-	-	39,499	39,499
As at March 31, 2014	**702,932**	**41,434**	**59,500**	**157,249**	**961,115**

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

Birchcliff Energy Ltd.
Condensed Statements of Cash Flows

Unaudited (Expressed in thousands of Canadian dollars)

Three months ended,	March 31, 2014	March 31, 2013
Cash provided by (used in):		
OPERATING		
Net income and comprehensive income	39,499	7,424
Adjustments for items not affecting operating cash:		
Unrealized loss on financial instruments	151	-
Depletion and depreciation	31,979	27,034
Stock-based compensation	959	1,303
Finance	5,714	6,754
Income taxes	14,044	3,033
Interest paid	(4,852)	(6,104)
Dividends on capital securities	875	-
Decommissioning expenditures *(Note 7)*	(808)	(41)
Changes in non-cash working capital	(14,251)	(4,093)
	73,310	35,310
FINANCING		
Exercise of stock options	5,966	3,035
Dividends on perpetual preferred shares *(Note 8)*	(1,000)	(1,000)
Dividends on capital securities *(Note 8)*	(875)	-
Net change in non-revolving term credit facilities	(317)	44
Net change in revolving credit facilities	59,941	18,926
	63,715	21,005
INVESTING		
Development of petroleum and natural gas properties and equipment	(104,786)	(80,937)
Additions of exploration and evaluation assets	(64)	(73)
Acquisition of petroleum and natural gas properties and equipment *(Note 4)*	(56,553)	-
Changes in non-cash working capital	24,378	24,695
	(137,025)	(56,315)
NET CHANGE IN CASH	-	-
CASH, BEGINNING OF PERIOD	96	46
CASH, END OF PERIOD	96	46

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

Birchcliff Energy Ltd.
Notes to the Interim Condensed Financial Statements
for the Three Months Ended March 31, 2014

(Expressed In Thousands Of Canadian Dollars, Unless Otherwise Stated) (Unaudited)

1. NATURE OF OPERATIONS

Birchcliff Energy Ltd. (“**Birchcliff**” or the “**Corporation**”) is domiciled and incorporated in Canada. Birchcliff is engaged in the exploration for and the development, production and acquisition of petroleum and natural gas reserves in Western Canada. The Corporation’s financial year end is December 31. The address of the Corporation’s registered office is 500, 630 – 4th Avenue SW, Calgary, Alberta, Canada T2P 0J9. Birchcliff’s common shares, Series A Preferred Shares, Series C Preferred Shares, and warrants are listed for trading on the Toronto Stock Exchange under the symbols “**BIR**”, “**BIR.PR.A**”, “**BIR.PR.C**” and “**BIR.WT**”, respectively.

These financial statements were approved and authorized for issuance by the Board of Directors on May 14, 2014.

2. BASIS OF PREPARATION

These unaudited interim condensed financial statements present Birchcliff’s financial results of operations and financial position under International Financial Reporting Standards (“**IFRS**”) as at and for the three months ended March 31, 2014, including the 2013 comparative period. The financial statements have been prepared in accordance with International Accounting Standard (“**IAS**”) 34 *Interim Financial Reporting*, as issued by the International Accounting Standards Board (“**IASB**”).

These financial statements have been prepared following the same IFRS accounting policies and methods of computation as disclosed in the annual audited financial statements for the year ended December 31, 2013, except as detailed below. Certain information and disclosures normally required to be included in the notes to the annual audited financial statements have been condensed, omitted or have been disclosed on an annual basis only. Accordingly, these financial statements should be read in conjunction with the annual audited financial statements and the notes thereto for the year ended December 31, 2013.

Effective January 1, 2014, the Corporation adopted IFRIC 21 *Levies*, which addresses payments made to government bodies. There was no impact to the Corporation’s interim condensed financial statements as a result of adopting this new standard.

Birchcliff’s financial statements are prepared on a historical cost basis, except for certain financial and non-financial assets and liabilities which have been measured at fair value. The Corporation’s financial statements include the accounts of Birchcliff only and are expressed in Canadian dollars, unless otherwise stated. There are no subsidiary companies.

3. EXPLORATION AND EVALUATION ASSETS

The continuity for Exploration and Evaluation ("**E&E**") assets are as follows:

($000's)	**E&E**[(1)]
As at December 31, 2012	2,106
Additions	158
As at December 31, 2013	2,264
Additions	64
As at March 31, 2014[(2)]	**2,328**

(1) E&E assets consist of the Corporation's exploration activities which are pending the determination of economic quantities of commercially producible proven reserves. Additions represent the Corporation's net share of costs incurred on E&E activities during the period. A review of each exploration project by area is carried out at each reporting date to ascertain whether economical quantities of proven reserves have been discovered and whether such costs should be transferred to depletable petroleum and natural gas components. There were no exploration costs reclassified from the E&E category to petroleum and natural gas properties and equipment category during the three months ended March 31, 2014.

(2) The Corporation performed an impairment assessment of its E&E assets and determined there were no impairment triggers identified at the end of the reporting period. As a result, no impairment test was required at March 31, 2014.

4. PETROLEUM AND NATURAL GAS PROPERTIES AND EQUIPMENT

The continuity for Petroleum and Natural Gas ("**P&NG**") Properties and Equipment are as follows:

($000's)	**P&NG Assets**	**Corporate Assets**	**Total**
Cost:			
As at December 31, 2012	1,609,760	6,848	1,616,608
Additions	280,899	1,954	282,853
Dispositions[(1)]	(34,667)	-	(34,667)
As at December 31, 2013	1,855,992	8,802	1,864,794
Acquisitions[(2)]	58,110	-	58,110
Additions	106,817	278	107,095
As at March 31, 2014[(3)]	2,020,919	9,080	2,029,999
Accumulated depletion and depreciation:			
As at December 31, 2012	(214,030)	(4,339)	(218,369)
Depletion and depreciation expense	(107,856)	(945)	(108,801)
Dispositions[(1)]	7,561	-	7,561
As at December 31, 2013	(314,325)	(5,284)	(319,609)
Depletion and depreciation expense	(31,703)	(276)	(31,979)
As at March 31, 2014	(346,028)	(5,560)	(351,588)
Net book value:			
As at December 31, 2013	1,541,667	3,518	1,545,185
As at March 31, 2014[(4)]	1,674,891	3,520	**1,678,411**

(1) Mainly consists of an asset disposition in the Progress area with a net book value of $27.0 million for net proceeds of $54.7 million.

(2) Mainly consists of Birchcliff acquiring a partner's 30% working interest in land and production for cash proceeds of approximately $56.0 million.

(3) The Corporation's P&NG properties and equipment were pledged as security for its credit facilities. Although the Corporation believes that it has title to its petroleum and natural gas properties, it cannot control or completely protect itself against the risk of title disputes and challenges. There were no borrowing costs capitalized to P&NG properties and equipment.

(4) Birchcliff performed an impairment assessment of its petroleum and natural gas assets on a CGU basis and determined there were no impairment triggers identified at the end of the reporting period. As a result, no impairment test was required at March 31, 2014.

5. NON-REVOLVING TERM CREDIT FACILITIES

The components of the Corporation's non-revolving term credit facilities include:

As at, *($000's)*	March 31, 2014	December 31, 2013
Current portion of non-revolving credit facilities	1,400	1,400
Non-current portion of non-revolving credit facilities	127,550	127,900
Drawn non-revolving credit facilities	128,950	129,300
Unamortized prepaid interest on bankers' acceptances	-	(33)
Unamortized deferred financing fees	(666)	(723)
Non-revolving credit facilities(1)	**128,284**	128,544

(1) The debt covenants applicable to the Corporation's credit facilities are disclosed in Note 10 to these financial statements.

The Corporation has a $60 million non-revolving five-year term credit facility with a maturity date of May 25, 2018. This facility is provided by a syndicate of banks and is fully drawn at March 31, 2014.

The Corporation also has a $70 million non-revolving five-year term credit facility with a maturity date of May 25, 2016. This facility requires principle repayments of $350,000 per quarter which commenced on July 1, 2013. The current portion due under this facility is $1.4 million at March 31, 2014.

6. REVOLVING CREDIT FACILITIES

The components of the Corporation's revolving credit facilities include:

As at, *($000's)*	March 31, 2014	December 31, 2013
Syndicated credit facility	307,000	251,000
Working capital facility	22,166	17,411
Drawn revolving credit facilities	329,166	268,411
Unamortized prepaid interest on bankers' acceptances	(2,237)	(1,424)
Unamortized deferred financing fees	(41)	(164)
Revolving credit facilities(1)	**326,888**	266,823

(1) The debt covenants applicable to the Corporation's credit facilities are disclosed in Note 10 to these financial statements.

At March 31, 2014, the revolving credit facilities consisted of a revolving syndicated credit facility with an authorized limit of $440 million and revolving working capital facility with an authorized limit of $30 million.

7. DECOMMISSIONING OBLIGATIONS

A reconciliation of the decommissioning obligations is provided below:

As at, *($000's)*	March 31, 2014	December 31, 2013
Balance, beginning	73,433	68,967
Obligations incurred	1,105	3,260
Obligations acquired	1,557	90
Obligations divested	-	(6,104)
Changes in estimated future cash flows	-	5,602
Accretion expense	603	2,175
Actual expenditures	(808)	(557)
Balance, ending(1)	**75,890**	73,433

(1) A risk-free rate of 3.2% and an inflation rate of 2.0% were used to calculate the discounted fair value of decommissioning liabilities at March 31, 2014 (December 31, 2013 – 3.2% and 2.0%, respectively).

8. CAPITAL STOCK

Share Capital

(a) Authorized:

Unlimited number of voting common shares, with no par value

Unlimited number of preferred shares, with no par value

The preferred shares may be issued in one or more series and the directors are authorized to fix the number of shares in each series and to determine the designation, rights, privileges, restrictions and conditions attached to the shares of each series.

(b) Number of common shares and perpetual preferred shares issued:

Common shares and perpetual preferred shares are classified as equity and recorded to share capital. Incremental costs directly attributable to the issuance of common and perpetual preferred shares are recognized as a reduction to share capital, net of any tax effects. Dividend distributions on perpetual preferred shares are recorded directly to equity.

	March 31, 2014	December 31, 2013
Common Shares:		
Outstanding at beginning of period - Jan 1	143,676,661	141,596,279
Exercise of stock options	827,116	2,080,382
Outstanding at end of period	**144,503,777**	143,676,661
Series A Preferred Shares (perpetual):		
Outstanding at beginning of period - Jan 1	2,000,000	2,000,000
Outstanding at end of period	**2,000,000**	2,000,000

Capital Securities

The issuance of Series C Preferred Shares, which are presented as "capital securities" on the statements of financial position, are classified as "other financial liabilities" under IFRS. The incremental costs directly attributable to the issuance of Series C Preferred Shares are initially recognized as a reduction to capital securities and subsequently amortized to profit and loss, using the effective interest rate method, as a finance expense. Dividend distributions on capital securities are recorded as an expense directly to profit and loss and presented as a financing activity on the statements of cash flows.

The Corporation has outstanding 2,000,000 Series C Preferred Shares at March 31, 2014 and December 31, 2013.

Dividends

On March 12, 2014, the Board of Directors declared a quarterly cash dividend of $1.0 million or $0.50 per Series A Preferred Share and $0.875 million or $0.4375 per Series C Preferred Share for the calendar quarter ending March 31, 2014. Both dividends are designated as an eligible dividend for purposes of the *Income Tax Act* (Canada).

Warrants

Birchcliff issued 6,000,000 warrants in conjunction with the offering of Series A Preferred Share in August 2012. Each warrant is exercisable until August 8, 2014 at a price of $8.30 to purchase one common share of Birchcliff. There were 6,000,000 warrants outstanding and exercisable at March 31, 2014.

Per Common Share

The Corporation calculates basic and diluted per common share amounts by dividing net income, which has been reduced for any dividends paid on perpetual preferred shares, by the weighted average number of basic or diluted common shares outstanding. The following table presents the computation of net income per common share:

Three months ended,	March 31, 2014	March 31, 2013
Net income and comprehensive income *($000's)*	39,499	7,424
Dividends on Series A Preferred Shares *($000's)*	(1,000)	(1,000)
Net income to common shareholders *($000's)*	38,499	6,424
Weighted average common shares *(000's)*:		
Weighted average common shares outstanding (basic)	144,026	141,821
Effect of dilutive stock options, performance warrants & warrants	3,064	2,545
Weighted average common shares outstanding (diluted)(1)	147,090	144,366
Net income per common share *($/share)*		
Basic	**$0.27**	$0.05
Diluted	**$0.26**	$0.04

(1) The weighted average diluted common shares outstanding at March 31, 2014 excludes 7,472,968 (March 31, 2013 – 8,246,601) stock options and NIL (March 31, 2013 – 6,000,000) warrants that are anti-dilutive.

9. SHARE-BASED PAYMENTS

Stock Options

At March 31, 2014, the Corporation's Amended and Restated Stock Option Plan permitted the grant of options in respect of a maximum of 14,450,378 (March 31, 2013 – 14,209,613) common shares. At March 31, 2014, there remained available for issuance options in respect of 1,808,542 (March 31, 2013 – 1,138,526) common shares. For stock options exercised during the three months ended March 31, 2014, the weighted average share trading price was $9.29 (March 31, 2013 – $7.71) per common share.

A summary of the outstanding stock options is presented below:

	Number	Exercise price(1)
Outstanding, December 31, 2013	10,931,520	$8.31
Granted	2,595,500	$8.65
Exercised	(827,116)	($7.21)
Forfeited	(58,068)	($8.34)
Outstanding, March 31, 2014	**12,641,836**	**$8.45**

(1) Determined on a weighted average basis.

The weighted average fair value per option granted during the three months ended March 31, 2014 was $2.80 (March 31, 2013 – $2.73). In determining the stock-based compensation expense for options issued during the three months ended March 31, 2014, the Corporation applied a weighted average estimated forfeiture rate of 14% (March 31, 2013 – 14%). The weighted average assumptions used in calculating the Black-Scholes fair values are set forth below:

Three months ended,	March 31, 2014	March 31, 2013
Risk-free interest rate	1.4%	1.3%
Option life *(years)*	3.9	3.9
Expected volatility	39.6%	47.0%

A summary of the stock options outstanding and exercisable under the plan at March 31, 2014 is presented below:

Exercise Price		Awards Outstanding			Awards Exercisable		
Low	High	Quantity	Weighted Average Remaining Contractual Life	Weighted Average Exercise Price	Quantity	Weighted Average Remaining Contractual Life	Weighted Average Exercise Price
$4.53	$6.00	2,514,668	3.07	$5.96	788,657	3.07	$5.96
$6.01	$9.00	5,870,200	4.27	$8.00	837,494	3.42	$7.49
$9.01	$12.00	4,129,968	1.40	$10.48	4,058,468	1.34	$10.49
$12.01	$13.26	127,000	2.16	$12.77	84,665	2.16	$12.77
		12,641,836	**3.07**	**$8.45**	**5,769,284**	**1.89**	**$9.47**

Performance Warrants

Performance warrants were issued on January 14, 2005 as part of the Corporation's initial restructuring to become a public entity. Birchcliff issued 4,049,665 performance warrants with an exercise price of $3.00 with an amended expiration date of January 31, 2015. There are 2,939,732 performance warrants outstanding and exercisable at March 31, 2014 (March 31, 2013 – 2,939,732).

Each stock option and performance warrant entitles the holder to purchase one common share at the exercise price.

10. CAPITAL MANAGEMENT

The Corporation's general policy is to maintain a sufficient capital base in order to manage its business in the most effective manner with the goal of increasing the value of its assets and thus its underlying share value. The Corporation's objectives when managing capital are to maintain financial flexibility in order to preserve its ability to meet financial obligations, including potential obligations arising from additional acquisitions; to maintain a capital structure that allows Birchcliff to finance its growth strategy using primarily internally-generated cash flow and its available debt capacity; and to optimize the use of its capital to provide an appropriate investment return to its shareholders. There were no changes in the Corporation's approach to capital management during the three months ended March 31, 2014.

The following table shows the Corporation's total available credit:

As at, *($000's)*	March 31, 2014	December 31, 2013
Maximum borrowing base limit[(1)(2)]:		
Non-revolving term credit facilities[(3)]	128,950	129,300
Revolving credit facilities	470,000	470,000
	598,950	599,300
Principal amount utilized:		
Drawn non-revolving term credit facilities	(128,950)	(129,300)
Drawn revolving credit facilities	(329,166)	(268,411)
Outstanding letters of credit[(4)]	(184)	(184)
	(458,300)	(397,895)
Unused credit[(2)]	**140,650**	201,405

(1) The Corporation's credit facilities are subject to a semi-annual review of the borrowing base limit, which is directly impacted by the value of Birchcliff's petroleum and natural gas reserves.

(2) The quarterly financial covenants applicable to the Corporation's credit facilities include (i) an interest coverage ratio, which is calculated on a historical rolling four quarter basis, as earnings before interest and non-cash items including income taxes, stock-based compensation, gains and losses on sale of assets, unrealized gains and losses on financial instruments and depletion, depreciation and amortization ("**EBITDA**") divided by interest expense; and (ii) a debt to EBITDA ratio. Interest expense for this purpose means total interest charges on borrowings with respect to all outstanding indebtedness and all preferred share dividends declared and paid in the period. Debt for this purpose means indebtedness for borrowed money, as determined at the end of the reporting period, and includes outstanding debt under the Corporation's credit facilities as shown on the statements of financial position before unamortized deferred financing fees and including outstanding letters of credit, but does not include working capital deficiency and capital securities.

The Corporation is required to ensure that on the last day of each quarter, the ratio of EBITDA to interest expense, determined on a historical rolling four quarter basis equals or exceeds 3.5:1.0 and the ratio of debt to EBITDA, determined on a historical rolling four quarter basis does not exceed 4.0:1.0. At March 31, 2014, Birchcliff's EBITDA to interest expense was 9.0:1.0 and debt to EBITDA was 1.8:1.0. The Corporation was compliant with all financial covenants under its credit facilities as at March 31, 2014.

(3) The $70 million non-revolving five-year term credit facility requires quarterly principle repayments of $350,000 which commenced on July 1, 2013.

(4) Letters of credit are issued to various service providers. There were no amounts drawn on the letters of credit during the three months ended March 31, 2014.

The capital structure of the Corporation is as follows:

As at, *($000's)*	March 31, 2014	December 31, 2013	Change
Shareholders' equity[(1)]	961,115	914,486	
Capital securities	48,064	47,986	
Shareholders' equity & capital securities	1,009,179	962,472	5%
Shareholders' equity & capital securities as a % of total capital[(2)]	66%	68%	
Working capital deficit[(3)]	70,948	60,071	
Non-current portion drawn non-revolving term credit facilities	127,550	127,900	
Non-current portion drawn revolving credit facilities	329,166	268,411	
Drawn debt	527,664	456,382	16%
Drawn debt as a % of total capital	34%	32%	
Capital	**1,536,843**	1,418,854	8%

(1) Shareholders' equity is defined as share capital plus contributed surplus plus retained earnings, less any deficit.

(2) Of the 66%, approximately 60% relates to common capital stock and 6% relates to preferred capital stock.

(3) Working capital deficit is defined as current assets less current liabilities (excluding fair value of financial instruments and deferred premium).

11. FINANCIAL RISK MANAGEMENT

Birchcliff is exposed to credit risk, liquidity risk and market risk as part of its normal course of business. The Board of Directors has overall responsibility for the establishment and oversight of the Corporation's financial risk management framework and periodically reviews the results of all risk management activities and all outstanding positions. Management has implemented and monitors compliance with risk management guidelines as outlined by the Board of Directors. The Corporation's risk management guidelines are established to identify and analyze the risks faced by the Corporation, to set appropriate risk limits and controls and to monitor risks and adherence to market conditions and the Corporation's activities.

As at March 31, 2014, Birchcliff has entered into certain financial derivative and physical delivery sales contracts in order to manage commodity price risk. These instruments are not used for trading or speculative purposes. Birchcliff has not designated its financial derivative contracts as effective accounting hedges, even though the Corporation considers all commodity contracts to be effective economic hedges. As a result, all such financial derivative contracts are recorded on the statement of financial position at fair value, with the changes in fair value being recognized as an unrealized gain or loss in profit or loss.

Financial Derivatives

As at March 31, 2014, the Corporation had the following financial derivatives in place:

Product	Option traded	Notional quantity	Term	Strike price	Fair value[(1)] *($000's)*
Crude oil	Put option	500 bbls/day	April 1, 2014 – December 31, 2014	WTI USD $90/bbl	264
Crude oil	Put option	500 bbls/day	April 1, 2014 – December 31, 2014	WTI USD $85/bbl	151
Fair value assets[(2)]					**415**

(1) The Corporation recorded approximately $0.9 million as a deferred premium on financial instruments which represents the amount payable to the counterparty to these contracts at March 31, 2014.

(2) The fair value of financial derivative contracts are based on option models that use published information with respect to quoted forward prices, volatility and interest rates. These instruments are considered level two under the fair value hierarchy.

As of March 31, 2014, if the future strip prices for WTI crude oil had been $1.00 USD per bbl higher, with all other variables held constant, after tax net income would have been $0.1 million (March 31, 2013 – NIL) lower.

The following table provides a summary of the realized and unrealized losses on financial instruments:

Three months ended, *($000's)*	**March 31, 2014**
Realized loss on financial instruments	309
Unrealized loss on financial instruments	151

There were no financial derivative contracts entered into subsequent to March 31, 2014.

Physical Sales Contracts

The Corporation has also entered into physical delivery sales contracts to manage commodity risk. These contracts are considered normal executory sales contracts and are not recorded at fair value in the financial statements. As at March 31, 2014, the Corporation had the following physical delivery sales contracts in place:

Product	Type of contract	Volume	Term[(1)]	Contract price
Natural gas	AECO fixed price	75,000 GJ/day	April 1, 2014 to October 31, 2014	$3.82 CDN/GJ

(1) Transactions with common terms have been aggregated and presented as the weighted average price.

There were no physical sales contracts entered into subsequent to March 31, 2014.

12. CONTINGENT LIABILITY

The Corporation's 2006 and 2007 income tax filings were reassessed by the Canada Revenue Agency ("**CRA**") in 2011. The reassessments are based on the CRA's determination that the tax pools available to Veracel Inc. ("**Veracel**"), prior to the amalgamation, ceased to be available to Birchcliff after the amalgamation. The Veracel tax pools in dispute totaled $39.3 million and include approximately $16.2 million in non-capital losses, $15.6 million in scientific research and experimental development expenditures and $7.5 million in investment tax credits. The disputed assessments are outstanding at March 31, 2014. The resolution of the disputed assessments may impact future income tax expense but will not impact cash taxes payable by the Corporation. Management believes that it will be successful in defending its tax position respecting the Veracel transaction, and as such, the Corporation has not recognized a related provision for deferred income tax liability at March 31, 2014.

Corporate Information

OFFICERS

A. Jeffery Tonken
President & Chief Executive Officer

Myles R. Bosman
Vice President, Exploration & Chief Operating Officer

Chris A. Carlsen
Vice President, Engineering

Bruno P. Geremia
Vice President & Chief Financial Officer

David M. Humphreys
Vice President, Operations

James W. Surbey
Vice President, Corporate Development

DIRECTORS

Larry A. Shaw (Chairman)
Calgary, Alberta

Kenneth N. Cullen
Calgary, Alberta

Werner A. Siemens
Calgary, Alberta

A. Jeffery Tonken
President & Chief Executive Officer
Calgary, Alberta

SOLICITORS

Borden Ladner Gervais LLP
Calgary, Alberta

AUDITORS

KPMG LLP, Chartered Accountants
Calgary, Alberta

RESERVES EVALUATOR

Deloitte LLP
Calgary, Alberta

BANKERS

The Bank of Nova Scotia

HSBC Bank Canada

Union Bank

Alberta Treasury Branch

National Bank of Canada

Canadian Imperial Bank of Commerce

The Toronto Dominion Bank

Business Development Bank of Canada

United Overseas Bank

ICICI Bank Canada

TRANSFER AGENT

Olympia Trust Company
Calgary, Alberta and
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