

**Enhanced Oil Resources Inc.**

**Management's Discussion & Analysis**

**Year Ended December 31, 2014**

**Enhanced Oil Resources Inc.  
Management's Discussion & Analysis for the Year ended December 31, 2014**

**DATE AND BASIS OF INFORMATION**

Enhanced Oil Resources Inc. ("we", "our" or "the Company") is a natural resource company incorporated in 1980 and is currently engaged in the acquisition, exploration, exploitation, and development of natural resource properties in the Southwestern United States. In June 2007, the Company changed its name to Enhanced Oil Resources Inc. to reflect a change in the Company's added focus on the development of enhanced recovery activities, principally, techniques of carbon dioxide ("CO<sub>2</sub>") injection used to increase an oil field's ultimate crude oil recovery and extend an oil field's productive life. The Company's office is headquartered in Houston, Texas. Common shares of the Company are listed for trading on the TSX Venture Exchange ("TSX-V") under the symbol "EOR" and quoted on the OTCQX ("Over the Counter" qualified stock exchange) under the symbol "EORIF". Additional information relating to the Company can be found on the SEDAR website at [www.sedar.com](http://www.sedar.com).

**Basis of Presentation**

The following Management's Discussion and Analysis ("MD&A") is dated April 30, 2014 and should be read in conjunction with the Company's consolidated financial statements and related notes for the year ended December 31, 2014, as well as the consolidated financial statements and MD&A for the year ended December 31, 2013. The referenced consolidated financial statements have been prepared by management and approved by the Company's Board of Directors as of the above date. Unless otherwise noted, all financial information presented herein has been prepared in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board (IASB).

All financial information is in US dollars, unless otherwise indicated.

**Non-IFRS Financial Measures**

Certain financial measures in this MD&A, namely netback, cash flow from operations, lifting costs and EBITDA are not prescribed, do not have a standardized meaning by IFRS and therefore may not be comparable with the calculation of similar measures by other companies.

Netbacks are used by the Company as a key measure of performance and are not intended to represent operating profit nor should they be viewed as an alternative to cash flow provided by operating activities, net earnings or other measures of financial performance calculated in accordance with IFRS. A netback is a per barrel (or mcf) computation determined by deducting royalties, production expenses, transportation and selling expenses from the oil or gas sales price to measure the average net cash received from the barrels or mcf sold.

Lifting costs include all production costs necessary to produce oil or gas, however exclude severance taxes.

EBITDA refers to income (loss) before income taxes, depletion, depreciation, amortization and accretion and is often referred to as 'cash flow from operations'.

There is an abbreviations section at the end of this document that lists abbreviations and definitions commonly referred to in the energy business and may be used in this MD&A.

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**BUSINESS OVERVIEW**

**Overview of Year Ended 2014**

**Change in Management and Directors.** Operating and financial performance in 2014 resulted in the sale of a significant portion of the Company's oil production in October. Following a complete change in the Board of Directors of the Company in December 2014, including the appointment of Andrew Hromyk as Chief Executive Officer and President, the new Board was elected by a majority of the shareholders at the annual general meeting held January 15, 2015. Currently, management is undertaking a substantial restructuring of objectives and operating actions to facilitate raising new capital and/or financing arrangements for the reactivation and development of the Company's oilfields. With the decline of crude oil prices during the first quarter of 2015, management took steps to reduce overhead and personnel, closed our Midland, Texas office and relocated our Houston office to smaller premises.

**Crude Oil and Natural Gas Business Segment.** The Company has one reportable business segment, crude oil and natural gas production and development, with all activities located in the United States of America. As such, we produce oil and gas from three Permian Basin crude oilfields located in eastern New Mexico. The New Mexico fields were purchased in 2007 ("Chaveroo Field" and "Milnesand Unit") and 2008 ("Crossroads Unit") because they represented candidates for enhanced oil recovery through CO<sub>2</sub> injection based on estimates of substantial remaining original-oil-in-place ("OOIP"). The OOIP utilized by the Company's independent reserves auditors for these fields represents approximately 318 million barrels, of which some estimates project as much as 20% of OOIP could still be recoverable through enhanced recovery methods by CO<sub>2</sub> injection. The Company's net proved reserves at December 31, 2014 and 2013, respectively, were 4.8 million and 3.6 million barrels of equivalents with a net present value of \$54.2 million and \$68.5 million using a 10% discount rate for 2014 and 2013.

**Subsidiaries and operations.** The Company commenced activities in 1980 and has two wholly-owned and directly held U.S. subsidiaries, Enhanced Oil Resources USA Inc. ("EORUS"), and Ridgeway Petroleum Florida, Inc. Oil and gas operations of the Company are conducted in two indirectly held, wholly-owned subsidiaries: Ridgeway Arizona Oil Corp. ("Ridgeway") and EOR Operating Company.

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**RESULTS OF OPERATIONS**

**Consolidated Statements of Operations and Comprehensive (Loss):**

<i>(In thousands of US dollars)</i>	<b>Three Months Ended</b>		<b>Year Ended</b>	
	<b>December 31,</b>		<b>December 31,</b>	
	<b>2014</b>	<b>2013</b>	<b>2014</b>	<b>2013</b>
<b>Revenues</b>				
Oil and gas gross sales	\$ 705	\$ 3,048	\$ 8,001	\$ 13,136
Less royalties	(146)	(739)	(1,665)	(2,804)
	<u>559</u>	<u>2,309</u>	<u>6,336</u>	<u>10,332</u>
<b>Expenses</b>				
Production costs and taxes	379	616	2,422	3,307
Workover expenses	41	608	3,464	1,182
Field expenses	373	425	1,366	1,389
General and administrative	1,392	560	3,752	3,314
(Gain) on disposition of assets	(1,188)	-	(106)	-
Depreciation, depletion and amortization	290	521	1,509	2,026
Financing costs and other, net	143	119	631	708
Stock-based compensation	-	-	-	125
(Gain) loss on financial instruments	(214)	(96)	(256)	367
Foreign currency translation (gain) loss	(13)	47	(7)	45
	<u>1,203</u>	<u>2,800</u>	<u>12,775</u>	<u>12,463</u>
(Loss) before income taxes	<u>(644)</u>	<u>(491)</u>	<u>(6,439)</u>	<u>(2,131)</u>
Income tax provision	-	-	-	-
Net comprehensive (loss) for the period	<u>\$ (644)</u>	<u>\$ (491)</u>	<u>\$ (6,439)</u>	<u>\$ (2,131)</u>
<i>(Loss) per share - basic and diluted</i>	<u>\$ (0.00)</u>	<u>\$ (0.00)</u>	<u>\$ (0.04)</u>	<u>\$ (0.01)</u>

The Company's crude oil sales revenues for the year ended December 31, 2014, decreased \$5.1 million (or 39.1%) to \$8.0 million, compared to \$13.1 million in 2013. In addition, net loss for the period increased by \$4.3 million (or 202.2%) to \$6.4 million, compared to a \$2.1 million net loss for the year ended December 31, 2013. Per share results (basic and fully diluted) were net losses of \$0.04 and \$0.01 for the years ended December 31, 2014 and 2013, respectively. Cash used in operating activities for the year ended December 31, 2014 was \$5.9 million compared to \$1.7 million in 2013, an increase of \$4.2 million. The increase in net loss and operating cash uses was principally related to the sidetrack-drilling and workover costs associated with the Crossroads #202 well, declining crude oil prices, decreases in crude oil production associated with the sale of oil and gas fields in 2014 (See Disposition of Oil and Gas Properties below) and increased general and administrative expense. Offsetting these increases in 2014 were decreases in costs related to DD&A, stock based compensation, accretion of asset retirement obligations, and unrealized losses on derivatives.

Results of operations for the three months ended December 31, 2014, included crude oil revenues of \$0.7 million, and a net loss of \$0.6 million, compared to \$3.0 million and \$0.5 million, respectively, for the three months ended December 31, 2013. In addition, loss per share results (basic and fully diluted) were nil for the three months ended

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December 31, 2014 and 2013. The significant decrease in revenue was related to the sale of the Crossroads field in October 2014, which represented 65% of the crude oil produced during the first nine months of 2014. General and administrative expenses increased \$0.5 million in the fourth quarter, principally related to severance costs associated with the prior chief executive officer and a vice president in December in connection with settlements associated with existing employment contracts.

**Revenue**

In 2014, crude oil sales revenue decreased by \$5.1 million (or 39.1 %) to \$8.0 million, compared to \$13.1 million in 2013. The decrease was due to both a 52,256 Boe (or 36.0 %) reduction in crude oil sales volumes (92,874 gross Boe's in 2014 compared to 145,130 gross Boe's in 2013) and lower average sales prices (\$86.15 in 2014 compared to \$90.51 in 2013).

Sales of crude oil decreased by \$2.3 million (or 76.9%) to \$0.7 million for the fourth quarter in 2014 compared to \$3.0 million in 2013. The decrease was due to both a 22,888 Boe (or 69.0 %) reduction in crude oil sales volumes (10,264 gross Boe's in the fourth quarter 2014 compared to 33,152 gross Boe's in the fourth quarter 2013) and lower average sales prices (\$68.70 in the fourth quarter 2014 compared to \$91.94 in the fourth quarter 2013).

**Production Costs, Workover Expenses and Field Expenses**

Our efforts have been focused on increasing oil recovery from legacy oil fields, which normally reflect higher operating costs than fields with newly established production. Since all of the Company's properties are older oil fields, we expect that operating costs will always be relatively higher due to the higher frequency of workovers, increasing compliance costs associated with increased regulatory activity, and higher maintenance costs pending current field development.

*Production Costs:* Production costs for the year ended December 31, 2014 decreased by \$0.9 million (or 26.8 %) to \$2.4 million, compared to \$3.3 million for 2013. Although lifting costs decreased as a result of decreased production, per Boe lifting costs increased \$2.73 (or 15.7 %) to \$20.08 in 2014, compared to \$17.35 in 2013. This increase in per Boe lifting costs is a result of the higher operating costs in the Milnesand and Chaveroo fields, the only two remaining producing fields following the disposition of the Crossroads field in October 2014.

*Workover Expenses:* Workover expense for the year ended December 31, 2014 increased significantly, by approximately \$2.3 million (or 193.1 %). This represents a \$29.33 increase workover expenses to \$37.46 per gross Boe. The increase is primarily related to the re-drilling of the Crossroads #202 well which ultimately cost \$3.4 million. In 2012, a similar submersible pump failure in the Crossroads #303 well required approximately \$1.9 million to re-drill and recover its reserves and production. In both wells, the depth, the age and the condition of very narrow wellbores presented significant and costly drilling and workover problems. In each case, the depth of the Crossroads field wells (approximately 12,000 feet) was a principal determinant of workover cost. In an effort to overcome the risk associated with small wellbore diameters, the Company installed two "slimhole" design submersible pumps at Crossroads in January and March 2014. As a result of the losses incurred on the Crossroads #202 well in the first quarter of 2014, the Company decided to sell the field to settle the liabilities that accumulated as a result of the re-drill and workover.

*Netback* – As a result of the average oil price decreasing and increased workover expense in 2014, the operating netback for the twelve months ended December 31, 2014 decreased to \$5.67 per Boe compared to \$40.28 per Boe for the same period in 2013.

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*Field Expenses:* Field expenses for the twelve months ended December 31, 2014 and 2013 were each \$1.4 million. During the first quarter of 2015, the Company has significantly reduced its field expense overhead, including personnel reductions and the closing of its Midland office.

**General & Administrative**

General and administrative expenses for the year ended December 31, 2014, increased \$0.4 million (or 13.2 %) to \$3.8 million when compared 2013. General and administrative expenses increased in the fourth quarter for severance costs associated with the prior chief executive officer and a vice president in December related to existing employment contracts. During the first quarter of 2015, the Company has significantly reduced its general and administrative expenses and reduced its overall headcount to seven employees and subleased its corporate office in Houston and moved to smaller quarters.

**Disposition of Oil and Gas Properties**

On October 16, 2014, the Company sold all of its interest in the Crossroads oilfield, located in Lea County, New Mexico to an unrelated third party group consisting of Desert Production, Inc. of Midland, Texas and Penroc Oil Corporation of Hobbs, New Mexico for \$10.0 million cash. The Company recognized a gain on the disposition of \$1.2 million, including a broker's fee of \$210,000. The sale of the field was completed following acceptance for filing of the transaction by the TSX Venture Exchange. In addition, the Company sold certain non-core property interests in Texas for approximately \$0.4 million in February 2014, and recognized a loss of \$1.1 million. As a result of the decrease in crude oil production associated with these dispositions and declining oil prices, the Company's operations are limited to those that are necessary to sustain production and as a result, the Company has limited its remedial operations, and has reduced personnel and overhead in order to adjust to reduced cash flows.

**Depreciation, Depletion & Amortization**

Depreciation, depletion and amortization expense for the year ended December 31, 2014, decreased by approximately \$0.5 million (or 25.5 %) to \$1.5 million, when compared to the same period in 2013. The decrease in depletion expense for 2014 was due to the decrease in production related to the oilfield dispositions discussed above. Depreciation, depletion, and amortization expense for the three months ended December 31, 2014 and 2013 were \$0.3 million and \$0.5 million, respectively.

**Gain (Loss) on Financial Instruments**

The Company realized gains of \$0.3 million on NYMEX WTI settlements related to its crude oil derivative contracts for the year ended December 31, 2014. This compared to \$0.3 million realized losses for the comparable period in 2013. In October 2014 following the sale of the Crossroads field, the Company sold the remainder of its collar derivative contract (November 2014 – April 2015) representing 36,200 Bbls to Shell Trading Risk Management, LLC for approximately \$278,000. At December 31, 2014, the remaining crude oil derivative contract represented an unrealized loss of \$0.04 million.

**Financing Costs and Other, net**

Financing costs were \$0.6 million and \$0.7 million for the years ended December 31, 2014 and 2013, respectively, principally represent accretion of asset retirement obligations and amortization of letter of credit fees. The \$0.1 million decrease in 2014 over 2013, is related to amortization of letter of credit during 2013.

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**Foreign Exchange Gain/Loss**

The Company's functional currency and presentational currency, as determined under IAS 21, *The Effects of Changes in Foreign Exchange Rates*, is the United States dollar. All of the Company's operating expenses and capital expenditures are paid in the United States dollar except for general and administrative expense of the Canadian parent entity and all historical equity issuances of the Canadian parent which are denominated in Canadian dollars. There will continue to be an impact from currency translation and exchange gains and losses, but we believe this translation will have a small impact on our financial results. The average Canadian/US dollar exchange rate was \$0.91 and \$0.97 for the years ended December 31, 2014 and 2013, respectively.

**Earnings before Interest, Taxes, Depreciation, Depletion and Amortization (EBITDA) Reconciliation**

<i>In thousands</i>	Three Months Ended		Year Ended	
	December 31,		December 31,	
	2014	2013	2014	2013
Net loss before tax	\$ (644)	\$ (491)	\$ (6,439)	\$ (2,131)
<i>Adjustments:</i>				
(Gain) on disposition of assets	(1,188)	-	(106)	-
Depreciation, depletion, and amortization	290	521	1,509	2,026
Foreign currency translation (gain) loss	(13)	47	(7)	45
Stock-based compensation	-	-	-	125
Unrealized loss (gain) on financial instruments	(378)	90	39	207
Financing costs and other, net	143	119	631	708
<b>EBITDA</b>	<b>\$ (1,790)</b>	<b>\$ 286</b>	<b>\$ (4,373)</b>	<b>\$ 980</b>

**Operating Netbacks and Production by Field**

The table below summarizes the operating netbacks for the comparable periods in the aggregate and by field for the years ended December 31, 2014 and 2013.

**Operating Netback Per Gross Boe:**

<i>(In US dollars)</i>		Three Months Ended,		Year Ended	
		December 31,		December 31,	
		2014	2013	2014	2013
<b>Oil &amp; Gas Sales Volumes</b>					
Oil equivalent	<i>Boe's</i>	10,264	33,152	92,874	145,130
<b>Average prices</b> <sup>1</sup>					
Oil equivalent	<i>\$/Boe</i>	\$ 68.70	\$ 91.94	\$ 86.15	\$ 90.51
<b>Less:</b>					
Royalties, net	<i>\$/Boe</i>	(12.63)	(19.63)	(15.72)	(17.28)
Production taxes	<i>\$/Boe</i>	(5.61)	(7.61)	(7.21)	(7.46)
Production costs	<i>\$/Boe</i>	(33.96)	(14.02)	(20.08)	(17.35)
Workover expense	<i>\$/Boe</i>	(5.76)	(18.71)	(37.46)	(8.13)
<b>Operating Netback</b> <sup>2</sup>	<i>\$/Boe</i>	\$ 10.74	\$ 31.97	\$ 5.67	\$ 40.28

<sup>1</sup> Average prices are after deduction of transportation costs and do not include net realized gains (losses) of \$0.3 and (\$0.3) million on derivative contracts for the year ended December 31, 2014 and 2013, respectively.

<sup>2</sup> Operating netback equals crude oil and natural gas sales less royalties, operating costs and transportation costs calculated on a Boe basis.

<sup>3</sup> Net of related production taxes. <sup>4</sup> Crossroads field produced for half a month in the fourth quarter 2014.

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Operating netback for the year ended December 31, 2014, decreased \$34.61 per gross Boe (or 85.9 %) to \$5.67, compared to \$40.28 per gross Boe for the same period in 2013, principally due to decreased production associated with workovers, declining crude prices and the disposition of producing property interests. For the same reasons, fourth quarter netbacks in 2014 decreased \$21.23 per gross Boe (or 66.4 %) to \$10.74, compared to \$31.97 per gross Boe realized in the fourth quarter of 2013.

**LIQUIDITY AND CAPITAL RESOURCES**

As of December 31, 2014, the Company had unrestricted cash of \$4.1 million and restricted cash balances of \$5.5 million. On April 9, 2015 the Company announced a private placement of approximately \$5.5 million expected to be completed in 2015, management's estimate of the additional funds necessary for limited activities in 2015. The Company has planned expenditures of \$2.7 million in 2015 for the Milnesand and Chaveroo fields before any development drilling is commenced.

In 2014, the cost to recover the Crossroads #202 well was \$3.4 million, which seriously affected the Company's financial condition and ultimately required the sale of the Crossroads field. The financial impact limited the Company's ability to fund any well servicing and maintenance activities normally required to sustain remaining production. On October 16, 2014, the Company sold its interests in the Crossroads field for net proceeds of \$9.7 million (see Property and Equipment footnote in the Notes to Consolidated Financial Statements for the Year Ended December 31, 2014). The proceeds were used to pay the outstanding payables arising from the costs incurred on the Crossroads #202 well. The Company has significantly reduced its operating costs, its personnel and overhead.

In September 2014, the Company announced that it has entered into a letter of intent with Schlumberger Technology Corporation (Schlumberger) to conduct an in-depth technical evaluation of the potential redevelopment of the Milnesand and Chaveroo oil fields, located in Chaves and Roosevelt Counties, New Mexico. Schlumberger completed its activities in January 2015.

In order to provide the necessary funds to develop its projects, the Company is considering all available sources of financing to develop its projects, including equity, bank and mezzanine debt, asset sales and joint venture arrangements. The Company expects that financing of drilling activities will require dilution of equity interests or higher cost debt financing and will require that the development of these fields command a high rate of return on investment. The Company will continue to focus on operations activities that further its objectives of positive operating cash flows and further its strategic objective of increasing production in one or more of its oil fields.

**QUARTERLY RESULTS OF OPERATIONS AND SELECT FINANCIAL DATA**

**Summary of Quarterly Information:**

**Quarterly Revenue, Loss and Earnings Per Share:**

<i>(In thousands except per share amounts)</i>	2013				2014			
	First	Second	Third	Fourth	First	Second	Third	Fourth
Revenues	\$ 2,977	\$ 3,176	\$ 3,935	\$ 3,048	\$ 2,366	\$ 2,510	\$ 2,420	\$ 705
Net comprehensive income (loss)	\$ (989)	\$ (358)	\$ (292)	\$ (492)	\$ (4,554)	\$ (1,267)	\$ 24	\$ (644)
Per share - basic	\$ (0.01)	\$ (0.00)	\$ (0.00)	\$ (0.00)	\$ 0.03	\$ 0.01	\$ (0.00)	\$ (0.00)
Per share - diluted	\$ (0.01)	\$ (0.00)	\$ (0.00)	\$ (0.00)	\$ 0.03	\$ 0.01	\$ (0.00)	\$ (0.00)

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Revenue varies directly with the average price of oil received and production volumes. The following table summarizes the average received prices and gross sales volumes for the three month periods indicated:

**Quarterly Average Prices Received and Sales Volumes:**

	2013				2014			
	First	Second	Third	Fourth	First	Second	Third	Fourth
Average price received	\$80.09	\$88.48	\$101.13	\$91.94	\$90.00	\$90.33	\$84.81	\$ 68.70
Sales volume	37,170	35,902	38,907	33,152	26,290	27,784	28,535	10,264

The changes in the results in the above quarterly table reflects more or less operational activity arising from planned and unplanned activities, such as regulatory requirements, changes in prices, availability of oil field services and/or weather related downtime, thereby affecting the level of workover and maintenance activity in each of the oilfields. The decrease in crude oil sales volume in the fourth quarter 2014 is principally due to the sale of the Crossroads field on October 16, 2014. The Crossroads field was the Company's largest producing field. The increase in crude oil sales volume during the second quarter of 2014 was due to the increase in production from wells that were offline during the prior quarter, principally at the Crossroads field. The decrease in production in the first quarter of 2014 was associated with wells off production in the Crossroads field. The decrease in crude oil sales volumes in the fourth quarter of 2013 was principally due to severe weather conditions causing the Company to shut-in multiple wells during the latter part of the quarter coupled with the loss of crude oil production of the Crossroads #202 well starting at the beginning of October. In addition to the increase in third quarter 2013 oil prices, production also increased in the quarter as a result of returning two shut-in wells to production in the Crossroads field following the addition of a second water injection well in the field. The decrease in sales volumes in the second quarter of 2013 is due to two producing wells being shut-in at the Crossroads oilfield in early February in order to reduce water disposal costs until the conversion of another well to a water injector was complete.

Revenue decreased in the fourth quarter 2014 related to the significant decrease in sales volumes as well as a decrease in sales price of \$23.24 (or 25.3 %) to \$68.70 per Boe. The decrease in revenue in the third quarter 2014 is due to the decrease in the average received price. Revenue increased in the second quarter of 2014 primarily due to an increase in crude oil sales volume. Revenue decreased in the first quarter 2014 principally due to decreased production. Net loss increased in the first quarter of 2014 principally related to increased workover expenses and loss on sale of assets. Fourth quarter 2013 net loss increased \$0.2 million over the third quarter of 2013 principally due a 14.8% reduction in sales volumes related to the Crossroads #202, colder weather and a decrease in average sales prices. The decrease in the second quarter of 2013 net loss as compared to the first quarter of 2013 was principally due to an increase in revenue of \$0.2 million, reflecting increased crude oil prices, as well as a decrease in production costs of \$0.3 million, general and administrative expenses of \$0.1 million, loss on financial instruments of \$0.3 million and financing costs of \$0.1 million offset by increase in workover and field expenses of \$0.4 million.

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**Selected Annual Information**

The following information is presented from annual information in the Company's audited financial statements for the periods indicated and prepared on the basis of the accounting principles effective for such period, as indicated:

**Three Year Select Financial Data:**

<i>(In thousands except per share amounts)</i>	Year Ended December 31, <sup>(1)</sup>		
	2014	2013	2012
Revenues	\$ 8,001	\$ 13,136	\$ 11,659
Net comprehensive loss	\$ (6,439)	\$ (2,131)	\$ (5,526)
Net loss per common share	\$ (0.04)	\$ (0.01)	\$ (0.03)
Loss per share basic and fully diluted	\$ (0.04)	\$ (0.01)	\$ (0.03)
Total assets	\$ 58,588	\$ 65,575	\$ 72,769
Total non-current financial liabilities	\$ 24,972	\$ 23,074	\$ 26,007

<sup>(1)</sup> The selected annual information was prepared in accordance with IFRS. Amounts are denominated in US dollars, which the Company determined under International Accounting Standard (IAS) 21 is its functional currency.

Revenues decreased in 2014 associated with the declining crude oil prices and crude oil production. Revenue growth in 2013 compared to 2012 was associated with higher sales volumes (12.7% increase over 2012) and higher average selling prices (7.8% increase over 2012). Losses in 2014 were associated with large workover costs associated with the Crossroads field, which was sold in October 2014. In addition, 2013 net losses decreased due to significant reductions in workover expenses (72.2% under 2012) and reduced lifting costs associated with three new wells drilled in the Milnesand field during 2012. Changes in noncurrent liabilities were principally associated with the Company's changes in estimates used in determining asset retirement obligations.

**EQUITY PLACEMENTS**

The Company has not had any equity placements since 2010. There are no outstanding Common stock purchase warrants at December 31, 2014. On April 9, 2015 the Company announced a private placement of approximately \$5.5 million to be completed in 2015 subject to approval of the TSX Venture Exchange.

*Share Consolidation.* - Effective January 15, 2015, the Directors of the Company authorized the implementation of a share consolidation of one new common share for 10 old shares of the Company's common shares. The Company's shares began trading on the post-consolidation basis on January 21, 2015 (see consolidated financial statements for the year ended December 31, 2014, footnote 12 – Equity Instruments).

**Kinder Morgan CO<sub>2</sub> Gas Purchase Contract**

In March 2010, the Company executed a cancellable five-year CO<sub>2</sub> purchase and delivery agreement with Kinder Morgan CO<sub>2</sub> Company, L.P. (Kinder Morgan) for the purchase of CO<sub>2</sub> by the Company for use in the Company's tertiary oil projects in the Permian Basin. The contract represents a take or pay commitment for a total of 27.4 bcf of

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CO<sub>2</sub> to be purchased over a five year period commencing no later than January 1, 2018 (as amended February 28, 2014). The maximum daily rate required to be purchased under the contract is 20 million cubic feet per day during the third year. The purchase commitment and obligation to pay, as amended, is cancellable on or before December 31, 2016, with no termination penalty. The cost of CO<sub>2</sub> will fluctuate based on the price of oil plus transportation tariffs.

**Regulatory Compliance in New Mexico**

The Company's operating subsidiaries, primarily Ridgeway and EOR Operating, conduct their operations under the oversight of multiple federal and state agencies. The Company's Chaveroo field, because of the age and condition of its production facilities and wells, is operated by Ridgeway, which is both the federal and State of New Mexico operator of record. The Company's other principal oil fields are operated by EOR Operating Company, which is both the federal and State of New Mexico operator of record. Future development is dependent upon the Company's operating subsidiaries negotiating agreed compliance orders with the New Mexico Oil Conservation Division for the Milnesand and Chaveroo fields.

**DISCLOSURE OF CONTROLS, PROCEDURES AND INTERNAL CONTROLS OVER FINANCIAL REPORTING**

As a TSX-Venture issuer, the Company's officers are not required to certify the design and evaluation of operating effectiveness of the Company's disclosure controls and procedures ("DC&P") or its internal controls over financial reporting ("ICFR"). The Company maintains DC&P designed controls to ensure that information required to be disclosed in reports filed or submitted is accumulated and communicated to management, including the Chief Executive Officer and the Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure. In addition, the Chief Executive Officer and the Chief Financial Officer have designed controls over financial reporting to provide reasonable assurance regarding the reliability of financial reporting and the preparation of consolidated financial statements for external purposes in accordance with generally accepted accounting principles. Due to its size, the small number of employees, the scope of its current operations, its limited liquidity and capital resources, there are inherent limitations on the Company's ability to design and implement on a cost effective basis the DC&P and ICFR procedures, the effect of which may result in additional risks related to the quality, reliability, transparency and timeliness of its interim filings and other reports. There have been no changes in ICFR during the year ended December 31, 2014.

**OFF-BALANCE SHEET ARRANGEMENTS**

The Company does not have any special purpose entities nor is it party to any arrangements that would be excluded from the consolidated balance sheet.

**RELATED PARTY TRANSACTIONS**

During 2014, the Company paid a \$50,000 due diligence fee to a company controlled by a director of the Company in connection with a proposed credit facility. There were no related party transactions for the year ended December 31, 2013.

**CRITICAL ACCOUNTING ESTIMATES**

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are

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recognized in the year in which the estimates are reviewed and for any future years affected. Significant judgments, estimates and assumptions made by management in these consolidated financial statements are outlined below:

*Oil and natural gas reserves* - Certain depletion, depreciation, and impairment and asset retirement obligation charges are measured based on the Company's estimate of oil and gas reserves and resources. The estimation of proved and probable reserves and resources is an inherently complex process and involves the exercise of professional judgment. Oil and natural gas reserves have been evaluated at December 31, 2014 and December 31, 2013 by independent petroleum engineers in accordance with National Instruments 51-101 "*Standards of Disclosure for Oil and Gas Activities*".

Oil and natural gas reserve estimates are based on a range of geological, technical and economic factors, including projected future rates of production, estimated commodity prices, engineering data, and the timing and amount of future expenditures, all of which are subject to uncertainty. Assumptions reflect market and regulatory conditions existing at the reporting date, which could differ significantly from other points in time throughout the year, or future periods. Changes in market and regulatory conditions and assumptions can materially impact the estimation of net reserves and resources.

*Impairment of assets* - The Company evaluates its assets for possible impairment at the CGU level. The determination of CGUs requires judgment in defining the smallest grouping of integrated assets that generate identifiable cash inflows that are largely independent of the cash inflows of other assets or groups of assets. The allocation of assets into CGUs have been determined based on similar geological structure, shared infrastructure, geographical proximity, commodity type, the existence of active markets, similar exposure to market risks, and the way in which management monitors the operations.

The recoverable amounts of CGUs and individual assets have been determined based on the higher of fair value less costs to sell model and value in-use model. The key assumptions the Company uses in estimating future cash flows for recoverable amounts are: anticipated future commodity prices, expected production volumes, future operating and development costs, estimates of inflation on costs and expenditures, expected income taxes and discount rates. In addition, the Company considers the current environmental, social and governance issues affecting its property interests and operations, including the current legislative and regulatory activity affecting the permitting and approval of its projects and operations. Changes to these assumptions will affect the estimated recoverable amounts attributed to a CGU or individual assets and may then require a material adjustment to their related carrying value.

*Asset retirement obligations* - The Company estimates and recognizes liabilities for future asset retirement obligations and restoration of exploration and evaluation assets, and for oil and gas development and producing assets. These provisions are based on estimated costs, which take into account the anticipated method and extent of restoration, technological advances and the possible future use of the asset. Actual costs are uncertain and estimates can vary as a result of changes to relevant laws and regulations, the emergence of new restoration techniques, operating experience and prices. The expected timing of future retirement and restoration may change due to these factors, as well as affect the estimates of reserve life. Changes to assumptions related to future expected costs, discount rates and timing may have a material impact on the amounts presented. Effective with the transition to IFRS, the Company made a policy choice available under existing standards to use a risk-free rate for discounting asset retirement obligations.

## **NEW AND FUTURE CHANGES IN ACCOUNTING POLICIES**

### ***IFRS 9***

IFRS 9, "Financial Instruments", is the first phase of the IASB's project to replace IAS 39, "Financial Instruments: Recognition and Measurement". IFRS 9 replaces the current multiple classification and measurement models for financial assets with a single model that has only two classification categories: amortized cost and fair value, and provides additional guidance for financial liabilities. The standard is required to be adopted in 2015. The Company has not yet assessed the impact of the standard or determined whether it will adopt the standard early.

### ***IFRIC 21***

In May 2013, the ISAB issued IFRIC Interpretation 21, "Levies", which provides clarification on accounting for levies imposed by a government in accordance with legislation and confirms that a liability is recognized only when the triggering event specified in the legislation occurs. The Company adopted the interpretation on January 1, 2014, which did not have a material impact on the Company's financial statements.

### ***IAS 32***

In January 2012, the IASB issued an amendment IAS 32, "Financial Instruments: Presentations", to establish principles for presenting financial instruments as either liabilities or equity and for offsetting financial assets and financial liabilities. The amendment was adopted and applied on January 1, 2014, and did not have a material impact on the Company's financial statements.

### ***IAS 36***

In May 2013, the IASB issued Amendments to IAS 36, "Recoverable Amount Disclosures for Non-Financial Assets", which reduce the circumstances in which the recoverable amount of CGUs is required to be disclosed and clarify the disclosures required when an impairment loss has been recognized or reversed in the period. The Company adopted and applied the amendment on January 1, 2014. The retrospective application did not have a material impact on the financial statements.

## **POTENTIAL RISKS AND UNCERTAINTIES**

The resource industry is highly competitive and, in addition, exposes the Company to a number of risks. Resource exploration and development involves a high degree of risk, which even a combination of experience, knowledge and careful evaluation may not be able to overcome. It is also highly capital intensive and the ability to complete a development project may be dependent on the Company's ability to raise additional capital. In certain cases, this may be achieved only through joint ventures or other relationships, which would reduce the Company's ownership interest in the project. There is no assurance that development operations will prove successful.

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**OTHER MD&A INFORMATION NOT DISCLOSED ELSEWHERE**

**Disclosure of Share Capital**

Authorized capital:

25 million preference shares of no par value  
Unlimited common shares of no par value

Issued and outstanding at April 30, 2015:

1,000 preference shares (held by a wholly-owned subsidiary of the Company)  
16,018,631 common shares issued

Since no additional warrant activity has occurred through April 30, 2015, the table depicted in 1“Equity Placements” represents all remaining warrant obligations to date.

Common stock options outstanding at April 30, 2015 were as follows:

**Stock Options Outstanding - Common Stock:**

<b>Number Authorized</b>	<b>Date of Agreement</b>	<b>Exercise or Issue Price</b>	<b>Expiry Date</b>
100,000	June 7, 2010	\$3.00	June 7, 2015
25,000	November 17, 2010	\$2.20	November 17, 2015
85,000	April 14, 2011	\$2.50	April 14, 2016
20,000	May 3, 2011	\$2.50	May 3, 2016
62,500	February 15, 2012	\$1.60	February 15, 2017
7,500	August 1, 2012	\$1.50	August 1, 2017
97,500	January 14, 2013	\$1.00	January 14, 2018
7,500	March 19, 2013	\$1.10	March 19, 2018
<b>405,000</b>			

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**Forward-Looking Statements**

Certain statements contained in this Management's Discussion and Analysis and in certain documents incorporated by reference into this Management's Discussion and Analysis, contain estimates and assumptions which management are required to make regarding future events and may constitute forward-looking statements within the meaning of applicable securities laws. Management's assessment of future operations, drilling and development plans and timing thereof, other capital expenditures and timing thereof, methods of financing capital expenditures and the ability to fund financial liabilities, expected commodity prices and the impact on the Company, and the impact of the adoption of future changes in accounting standards may constitute forward-looking statements under applicable securities laws and necessarily involve risks including, without limitation, risks associated with oil and gas exploration, development, exploitation, the flexibility of capital funding plans and the source of funding therefore; production, marketing and transportation, loss of markets, volatility of commodity prices, the effect of the Company's risk management program, including the impact of derivative financial instruments; currency fluctuations, imprecision of reserve estimates, environmental risks, competition from other producers, inability to retain drilling rigs and other services, incorrect assessment of the value of acquisitions, failure to realize the anticipated benefits of acquisitions, the inability to fully realize the benefits of the acquisitions, delays resulting from or inability to obtain required regulatory approvals and ability to access sufficient capital from internal and external sources.

All statements other than statements of historical fact may be forward-looking statements. Forward-looking statements are often, but not always, identified by the use of words such as "seek", "anticipate", "plan", "continue", "estimate", "expect", "may", "will", "project", "predict", "potential", "targeting", "intend", "could", "might", "should", "believe" and similar other expressions. These statements involve known and unknown risks, uncertainties and other factors that may cause actual results or events to differ materially from those anticipated in such forward-looking statements. The Company believes that the expectations reflected in these forward-looking statements are reasonable but no assurance can be given that these expectations will prove to be correct and such forward-looking statements included in, or incorporated by reference into, this MD&A should not be unduly relied upon. These statements speak only as of the date of this MD&A, as the case may be. The Company does not intend, and does not assume an obligation, to update these forward-looking statements, except as required by securities law.

In particular, this MD&A and the documents incorporated by reference include, but are not limited to, forward-looking statements pertaining to the following:

- the quantity of reserves and contingent resources;
- crude oil, natural gas, CO<sub>2</sub> and helium operations and production levels;
- capital expenditure programs, including drilling programs, asset retirement and abandonment activities and pipeline construction projects, and the timing and method of financing thereof;
- projections of market prices and costs;
- supply, demand and pricing for crude oil, natural gas, and CO<sub>2</sub>;
- expectations regarding the Company's ability to raise capital and to continually add to reserves through acquisitions and development
- drilling inventory, drilling plans and timing of drilling, re-completion and tie-in of wells;
- plans for production facilities construction and completion and the timing and method of funding thereof;
- productive capacity of wells, anticipated or expected production rates and anticipated dates of commencement of production;
- drilling, completion and facilities costs;
- results of various projects of the Company;
- timing of receipt of regulatory approvals;
- timing and effect of production increases and the related effect and timing on operating costs per BOE;

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- ability to lower cost structure in certain projects of the Company;
- growth expectations within the Company;
- timing of development of undeveloped reserves;
- the tax horizon and tax related implications of the Company;
- supply and demand for oil, natural gas liquids and natural gas;
- the performance and characteristics of the Company's oil and natural gas properties;
- the Company's acquisition strategy, the criteria to be considered in connection therewith and the benefits to be derived therefrom;
- the impact of federal and state governmental regulation on the Company, either directly or relative to other oil and gas issuers of similar size;
- realization of the anticipated benefits of acquisitions and dispositions;
- weighting of production between different commodities;
- expected levels of royalty rates, production and workover costs, office field expenses, general and administrative costs, costs of services and other costs and expenses; and
- benefits or costs related to settlement of financial instruments
- treatment under government regulation and taxation, including carbon taxation regimes

Although the Company 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. The Company cannot guarantee future results, levels of activity, performance, or achievements. Moreover, neither the Company nor any other person assumes responsibility for the outcome of the forward-looking statements. Many of the risks and other factors are beyond the Company's control, which could cause actual results to differ materially from those anticipated in these forward-looking statements as a result of risk factors as set forth, but not limited to, those below and elsewhere in this MD&A:

- volatility in market prices for oil, natural gas, and CO<sub>2</sub>;
- liabilities and risks inherent in oil and natural gas operations;
- uncertainties associated with estimating reserves;
- competition for capital, acquisitions of reserves, undeveloped lands and skilled personnel;
- incorrect assessments of the value of acquisitions;
- incorrect assessments of the recoverability of asset costs and investments;
- geological, technical, drilling and processing problems; and
- governmental, regulatory and taxation regimes.

**ABBREVIATIONS**

**Crude Oil and Natural Gas Liquids**

Bbl	barrel
Bbls	barrels
BBls/d	barrels per day
BOEPD	barrel of oil equivalent per day
MMbbls	million barrels
Mbbls	thousand barrels

**Carbon Dioxide and Natural Gas**

Bcf	billion cubic feet
CO <sub>2</sub>	carbon dioxide
Mcf	thousand cubic feet
MMcf	million cubic feet
Mcf/d	thousand cubic feet per day
MMcf/d	million cubic feet per day
Tcf	trillion cubic feet

API	American Petroleum Institute
Boe	Barrel of oil equivalent of natural gas and crude oil on the basis of one boe for six mcf of natural gas and one boe for forty- two gallons of plant products (these conversion factor are an industry accepted norm and is not based on either energy content or current prices)
Contingent resource	Those quantities of petroleum which are estimated, on a given date, to be potentially recoverable from known accumulations, but which are not currently considered to be commercially recoverable.
DD&A	Depreciation, depletion and amortization
DOE	United States Department of Energy
EBITDA	Income before income taxes, depletion, depreciation, amortization and accretion and often referred to as 'cash flow from operations'
EOR	Enhanced oil recovery, typically any method of economically removing oil incremental to that produced by primary or conventional improved-recovery methods
MBoe	1,000 barrels of oil equivalent
Net revenue	Gross revenue less all taxes, royalties and lease operating expenses
NI 51-101	National Instrument 51-101 Standards of Disclosure for Oil and Gas Activities adopted by the Canadian Securities Administrators
Primary recovery	Production in which only existing natural energy sources in the reservoir provide for movement of well fluids.
Permian Basin	A large crude oil and natural gas producing area representing a sedimentary basin dating from the Permian geologic period and covering an area extending from West Texas to eastern New Mexico
Reserves	Estimated remaining quantities of oil and natural gas and related substances anticipated to be recoverable from known accumulations, from a given date forward based on (i) analysis of drilling, geophysical and engineering data; (ii) the use of established technology; (iii) specified economic conditions, which are generally accepted as being reasonable, and shall be disclosed; and (iv) a remaining reserve life of 50 years. These definitions and disclosures are in accordance with the definitions, procedures and standards contained in the Canadian Oil and Gas Evaluation (COGE) Handbook and the Canadian Securities Administrators NI 51-101.

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Secondary recovery      Any method by which an essentially depleted reservoir is restored to producing status by the injection of liquids or gases (from external sources) into the formation, thereby effecting a restoration of reservoir energy which moves the unrecoverable secondary reserves through the reservoir to the wellbore.

Tertiary recovery      Any of various methods, chiefly reservoir drive mechanisms and enhanced recover techniques, designed to improve the flow of hydrocarbons from the reservoir to the wellbore to recover more oil after the primary and secondary methods (water and gas floods) are uneconomic.

\$                              United States dollars

C\$                             Canadian dollars