

## **Brownstone Energy Inc.**

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

---

**For the quarter ended: September 30, 2014**

**Date of report: November 27, 2014**

This management's discussion and analysis of the financial condition and results of operation ("MD&A") of Brownstone Energy Inc. ("Brownstone" or the "Company") should be read in conjunction with Brownstone's unaudited interim condensed consolidated financial statements ("interim consolidated statements") and notes thereto as at and for the three months ended September 30, 2014 and the annual consolidated financial statements as at and for the year ended June 30, 2014. The same accounting policies and methods of computation were followed in the preparation of the interim consolidated statements as were followed in the preparation and described in note 3 of the annual consolidated financial statements as at and for the year ended June 30, 2014, except for those described under the "Change in Accounting Policies" section elsewhere in this MD&A.

Unless indicated otherwise, all financial data in this MD&A has been prepared in accordance with International Financial Reporting Standards ("IFRS") issued by the International Accounting Standards Board ("IASB") and interpretations of the International Financial Reporting Interpretations Committee ("IFRIC"). All dollar amounts in this MD&A are reported in Canadian dollars unless otherwise indicated.

#### **Caution Regarding Forward-Looking Information:**

Certain information contained in this MD&A constitutes forward-looking information, which is information relating to future events or the Company's future performance and which is inherently uncertain. All information other than statements of historical fact may be forward-looking information. Forward-looking information is often, but not always, identified by the use of words such as "seek", "anticipate", "budget", "plan", "continue", "estimate", "expect", "forecast", "may", "will", "project", "predict", "potential", "targeting", "intend", "could", "might", "should", "believe" and similar words or phrases (including negative variations) suggesting future outcomes or statements regarding an outlook. Forward-looking information contained in this MD&A includes, but is not limited to the Company's expectations regarding its exploration and development activities, including expectations regarding the timing, costs and results of seismic acquisition, drilling and other activities, and future production volumes and sales, receipt of regulatory and governmental approvals, the Company's future working capital requirements, including its ability to satisfy such requirements, the exposure of its financial instruments to various risks and its ability to manage those risks, the Company's ability to use tax resource pools and loss carry-forwards and changes in accounting policies.

Forward-looking information involves 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 information. The Company believes the expectations reflected in the forward-looking information are reasonable but no assurance can be given that these expectations will prove to be correct and readers are cautioned not to place undue reliance on forward-looking information contained in this MD&A. Some of the risks and other factors which could cause results to differ materially from those expressed in the forward-looking information contained in this MD&A include, but are not limited to: risks relating to oil and gas exploration activities generally, including the availability and cost of seismic, drilling and

other equipment; our ability to complete our capital programs; geological, technical, drilling and processing problems, including the availability of equipment and access to properties; our ability to secure adequate transportation for our products; potential losses which would stem from any disruptions in production, including work stoppages or other labour difficulties, or disruptions in the transportation network on which we are reliant; potential delays or changes in plans with respect to exploration or development projects or capital expenditures; our ability and the ability of our partners to attract and retain the necessary labour required to explore and develop our projects; potential conflicting interests with our joint venture partners; our failure or the failure of the holder(s) of licenses or leases to meet specific requirements of such licenses or leases; the failure by counterparties to make payments or perform their operational or other obligations in compliance with the terms of contractual arrangements between us and such counterparties; adverse claims made in respect of our properties or assets; operating hazards and other difficulties inherent in the exploration for and production and sale of crude oil and natural gas; political and economic conditions in the countries in which our property interests are located; obtaining the necessary financing for operations, our ability to generate taxable income from operations, fluctuations in the value of our portfolio investments due to market conditions and/or company-specific factors, fluctuations in prices of commodities underlying our interests and portfolio investments, and other risks included elsewhere in this MD&A under the heading "Risks" and in the Company's public disclosure documents filed with certain Canadian securities regulatory authorities and available under the Company's profile at [www.sedar.com](http://www.sedar.com).

Readers are cautioned that the foregoing lists of factors are not exhaustive. Although the Company has attempted to identify important factors that could cause actual events and results to differ materially from those described in the forward-looking information, there may be other factors that cause events or results to differ from those intended, anticipated or estimated. The forward-looking information contained in this MD&A are made as of the date hereof and the Company undertakes no obligation to update publicly or revise any forward-looking information, whether as a result of new information, future events or otherwise, except as otherwise required by law. All of the forward-looking information contained in this MD&A is expressly qualified by this cautionary statement.

### **Nature of the Business:**

Brownstone Energy Inc. ("Brownstone" or the "Company") is a Canadian-based, energy-focused company with direct and indirect interests in oil and gas exploration projects. By owning and managing a diversified portfolio of energy-based projects, Brownstone provides shareholders with a unique energy alternative. Its common shares are publicly-traded on the TSX Venture Exchange ("TSXV") under the symbol "BWN" and on the OTCQX under the symbol "BWSOF".

### **Summary:**

- As at September 30, 2014, the Company has working capital of \$8,460,463 as compared to working capital of \$9,172,740 as at June 30, 2014, a decrease of 8%, primarily due to the decrease in the fair value of the Company's investment portfolio and the payment of net cash calls in Colombia during the current quarter.
- As at September 30, 2014, exploration and evaluation assets decreased by 38% to \$3,032,361 as compared to \$4,911,743 as at June 30, 2014. The decrease was primarily due to the impairment charge of \$2,071,157 on the Company's USA properties offset by a foreign currency translation gain of \$185,057 during the current quarter. See the Exploration and evaluation assets section.

- On September 1, 2014, the Gabriella license (in Israel) expired without further extension being granted, due to the milestones in the work program not being achieved. The Company and the joint operating partners of the Gabriella Block are filing an appeal with the Israeli Ministry.
- On October 15, 2014, the Yitzhak license (in Israel) expired. The Company and its joint operating partners of the Yitzhak Block are awaiting formal notice from the Israeli Ministry and evaluating the options available to them, including the filing of an extension with the Israeli Ministry.

### **Going concern uncertainty:**

The Company has incurred a loss in the three months ended September 30, 2014 of \$2,767,253 (three months ended September 30, 2013 - \$517,924) and has an accumulated deficit of \$110,105,646 (June 30, 2014 - \$107,338,393). The Company is in the early exploration and development stage and is subject to risks and challenges similar to other companies in a comparable stage of exploration. These risks include, but are not limited to, dependence on key individuals, successful exploration and the ability to secure adequate financing to meet the minimum capital required to successfully complete the projects, political risk relating to maintaining property licenses in good standing and continuing as a going concern. Management estimates that the funds available as at September 30, 2014 will not be sufficient to meet the Company's potential capital expenditures through September 30, 2015. The Company will have to raise additional funds to continue operations. Although the Company has been successful in raising funds to date, there can be no assurance that adequate funding will be available in the future, or available on terms acceptable to the Company. Failure to meet its funding commitments with its partners may result in the loss of the Company's exploration and evaluation interests.

The challenges of securing requisite funding beyond September 30, 2014 and the continued estimated operating losses cast significant doubt on the Company's ability to continue as a going concern. The consolidated financial statements do not include any adjustments relating to the recoverability and classification of recorded asset amounts or to the amounts or classification of liabilities that might be necessary should the Company not be able to continue as a going concern.

### **Exploration and evaluation assets:**

All of the Company's oil and gas activities are conducted jointly with others. The Company enters into exploration agreements with other parties, pursuant to which Brownstone may earn interests in the underlying exploration and evaluation assets by issuing common shares and/or making cash payments and/or incurring expenditures in varying amounts by varying dates. Failure by the Company to issue such shares, make such cash payments or incur such expenditures can result in a reduction or loss of the Company's interests.

The Company's accounts reflect only its interests in its oil and gas activities. The following is a summary of the Company's exploration and evaluation assets:

	Colombia \$	Israel (a) \$	USA (b) \$	Canada \$	Argentina (c) \$	Total \$
<b>Balance at July 1, 2013</b>	1,051,200	9,664,918	4,376,697	1,130,468	1,051,200	17,274,483
Net additions <sup>1</sup> :	306,317	(706,143)	(126,018)	12,689	(112,956)	(626,111)
Disposals	-	-	(270,170)	-	-	(270,170)
Impairment of exploration and evaluation assets	(1,372,310)	(9,236,915)	-	(1,143,154)	(87,056)	(11,839,435)
Foreign currency translation	14,793	278,140	71,247	-	8,796	372,976
<b>Balance at June 30, 2014</b>	-	-	4,051,756	3	859,984	4,911,743
Net additions <sup>1</sup> :	-	-	<b>6,718</b>	-	-	<b>6,718</b>
Impairment of exploration and evaluation assets	-	-	<b>(2,071,157)</b>	-	-	<b>(2,071,157)</b>
Foreign currency translation	-	-	<b>142,203</b>	-	<b>42,854</b>	<b>185,057</b>
<b>Balance at September 30, 2014</b>	-	-	<b>2,129,520</b>	<b>3</b>	<b>902,838</b>	<b>3,032,361</b>

<sup>1</sup> Net additions reflects expenditures on exploration and evaluation assets less revenue received from sales of natural gas, natural gas liquids, and oil generated during long-term production testing (if any) and reversals of outstanding cash calls previously capitalized.

(a) Israel:

As at June 30, 2014, the Company had the following participating interests in Israel and is required to fund its share of the participating interests:

	Gabriella Block	Yitzhak Block
Participating Interest	15%	15%

The Gabriella license expired on September 1, 2014 without further extension being granted by the Ministry of Energy and Water of the State of Israel ("Ministry"), due to the milestones in the work program not being achieved. The Company has been notified by the operator of the Block that they are appealing to the Ministry the decision to rescind the Gabriella license.

The Yitzhak license expired on October 15, 2014. The Company and its joint operating partners of the Yitzhak Block are awaiting formal notice from the Ministry and evaluating the options available to them, including the filing of an extension with the Ministry. The Yitzhak Block was the Company's remaining oil and gas project in Israel.

(b) USA:

The Company has participating interests of between 10% to 28.57% in various acreages in the Piceance/Uinta basin in the USA and is required to fund its share of the participating interests.

During the three months ended September 30, 2014, included in net additions was \$17,946 (year ended June 30, 2014 - \$260,493) in gross revenue (net of royalties) from the sale of natural gas, natural gas liquids, and oil generated during long-term production testing.

In June 2014, the Company closed the sale of 13% of its 28.57% interests in two oil and gas leases comprising the Kokopelli project in Colorado (and 65% of its 28.57% working interest in the initial well drilled in 2013) with a further 52% of the Company's 28.57% interests subject to an earn-in by the purchaser. The Company now has a 24.85% carried working interest in a

US\$16,000,000 drilling and completion program planned for 2014-2015 to be funded 100% by the purchaser of the assets. If the earn-in conditions are satisfied, the Company will have a 10% working interest in the Kokopelli project. The Company believes the earn-in conditions will be satisfied by December 31, 2014. During the three months ended September 30, 2014, the Company recorded an impairment charge on its USA properties of \$2,071,157 to its estimated recoverable amount of \$2,129,520 (US\$1,900,000). The Company has impaired the USA properties by 50% for which management believes the assets could be sold in a comparable arm's length transaction, less estimated costs to sell. The impairment was recognized upon a review of the Company's participating interests in the USA properties.

(c) Argentina:

The Company has a 25% interest in the Vaca Mahuida Block in the Province of Rio Negro, Argentina. Under the terms of the participation agreement governing Brownstone's interest, the Company is required to fund 50% of the costs to be incurred in the conduct of the work program on the property.

During the year ended June 30, 2014, the Company agreed to relinquish its 25% working interest to Petrolifera Petroleum (Americas) Limited Sucursal Argentina, the operator of the Block for net cash consideration of US\$805,530. The net cash consideration settled all outstanding liabilities and no further liabilities will occur in respect of the Block. As at September 30, 2014, the value of the 25% working interest in Argentina was \$902,838 (June 30, 2014 - \$859,984). The relinquishment is conditional upon granting by the Province of Rio Negro of an exploitation concession on the Vaca Mahuida Block to Petrolifera. As at the filing date of these consolidated financial statements, the concession has not been awarded by the Province and there is no certainty that it will be awarded.

## Investments:

The fair value and cost of investments are as follows:

	Fair Value	Cost
<b>September 30, 2014</b>	<b>\$ 4,172,900</b>	<b>\$ 10,403,180</b>
June 30, 2014	3,707,817	9,746,424

As at September 30, 2014, the original cost of investments exceeded fair value by \$6,230,280 as compared to \$6,038,607 as at June 30, 2014. The increase for the three months ended September 30, 2014 was primarily due to the disposal of investments, realizing a loss of \$377,387 and from the net change in unrealized losses on investments of \$190,642.

The fair value of the Company's investments as reflected in its consolidated financial statements and calculated in accordance with IFRS and its accounting policies may differ from the actual proceeds of disposition that would be realized by the Company. For example, the amounts at which the Company's publicly-traded investments could be disposed of currently may differ from fair values based on market quotes, as the value at which significant ownership positions are sold is often different than the quoted market price due to a variety of factors such as premiums paid for large blocks or discounts due to illiquidity.

## Results of Operations

The Company's selected quarterly results for the eight most recently completed interim financial periods are as follows:

	<b>Quarter ended</b>			
	<b>September 30, 2014</b>	June 30, 2014	March 31, 2014	December 31, 2013
Net investment gains (losses)	\$ (568,029)	\$ 290,489	\$ 249,270	\$ (81,206)
Net profit (loss) for the period	(2,767,253)	(10,943,929)	201,169	(2,095,191)
Total comprehensive income (loss) for the period	(2,601,876)	(11,296,308)	755,342	(1,604,098)
Earnings (loss) per share based on loss for the period – basic and diluted	(0.02)	(0.08)	0.00	(0.02)

  

	September 30, 2013	June 30, 2013	March 31, 2013	December 31, 2012
Net investment gains (losses)	\$ 429,186	\$ (231,949)	\$ (410,312)	\$ (674,534)
Net loss for the period	(517,924)	(32,396,668)	(1,327,113)	(6,040,709)
Total comprehensive loss for the period	(843,909)	(31,404,339)	(380,017)	(5,488,984)
Loss per share based on loss for the period – basic and diluted	(0.00)	(0.25)	(0.01)	(0.05)

No dividends were declared by the Company during any of the periods indicated.

### Three months ended September 30, 2014 and 2013:

For the three months ended September 30, 2014, the Company generated net realized losses on disposal of investments of \$377,387, as compared to nil for the three months ended September 30, 2013. The net realized losses in the current quarter was a result of the disposition of two of the Company's investments.

For the three months ended September 30, 2014, the Company recorded a net change in unrealized losses on investments of \$190,642 as compared to a net change in unrealized gains on investments of \$429,186 for the three months ended September 30, 2013. The net change in unrealized gains on investments in the current period related to the net write-down to market on the Company's investments offset by the reversal of previously recognized net unrealized losses on disposal of investments.

For the three months ended September 30, 2014, the Company recorded interest and other income of \$73,267 as compared to \$4,006 for the three months ended September 30, 2013. Interest income is primarily composed of interest income earned on cash deposits. In the current period, interest income included \$73,056 (US\$66,342) from the settlement in full with the operator of Block 21 (Colombia) of a letter of credit that was called in October 2013 by the Agencia Nacional de Hidrocarburos ("ANH"), the oil and gas agency of the Colombian government.

For the three months ended September 30, 2014, operating, general and administrative expenses decreased by \$653,314 to \$186,932 from \$840,246 for the three months ended September 30, 2013. The decrease was primarily due to an increase in foreign exchange gains and a decrease in salaries and consulting fees as discussed below.

The following is the breakdown of the Company's operating, general and administrative expenses for the indicated three month periods ended September 30. Details of the changes follow the table:

	2014	2013
Salaries, consulting and administrative fees (a)	\$ 237,657	\$ 432,955
Professional fees (b)	74,098	54,596
Other office and general	23,414	66,390
Stock-based compensation expense	10,217	49,275
Transaction costs	8,117	-
Travel and promotion	7,465	16,074
Other employment benefits	4,657	6,536
Shareholder relations, transfer agent and filing fees	(1,156)	4,616
Foreign exchange loss (gain) (c)	(177,537)	209,804
	<b>\$ 186,932</b>	<b>\$ 840,246</b>

- (a) Salaries, consulting and administrative fees decreased by \$195,298 for the three months ended September 30, 2014 as compared to the three months ended September 30, 2013. The decrease was due to a reduction of consultants and the amount of consultancy fees paid in the current quarter.
- (b) Professional fees increased by \$19,502 for the three months ended September 30, 2014 as compared to the three months ended September 30, 2013, primarily due to one-time legal fees of \$49,477 relating to the settlement with the operator of Block 21 (Colombia) of a letter of credit that was called in October 2013 by the ANH. Overall, professional fees decreased in the current period due to a reduction in the oil and gas activities of the Company's foreign subsidiaries.
- (c) During the three months ended September 30, 2014, the Company had a foreign exchange gain of \$177,537 as compared to foreign exchange loss \$209,804 for the three months ended September 30, 2013. The Company experienced a foreign exchange gain due to the decrease in the value of the Canadian dollar versus the U.S. dollar during the quarter, which increased the Canadian dollar value of the Company's U.S. dollar denominated monetary assets.

For the three months ended September 30, 2014, the Company recorded an impairment on exploration and evaluation assets of \$2,071,157 as compared to \$87,056 for the three months ended September 30, 2013. In the current period, the Company recorded an impairment on its properties in the USA. See "Exploration and evaluation assets" section.

For the three months ended September 30, 2014, the Company recorded an income tax expense of \$14,402 as compared to \$23,814 for the three months ended September 30, 2013. The income tax expense was due to the recording of an accrual of minimum income tax payable due in Colombia.

Net loss for the three months ended September 30, 2014 was \$2,767,253 (\$0.02 per share) as compared to \$517,924 (\$0.00 per share) for the three months ended September 30, 2013.

For the three months ended September 30, 2014, the Company recorded a gain from the exchange differences on translation of foreign operations of \$165,377 resulting in total comprehensive loss for the period of \$2,601,876. The gain from the exchange differences on translation of foreign operations was primarily due to the decrease in the value of the Canadian dollar versus the U.S. dollar during the quarter, which increased the Canadian dollar value of the Company's U.S. dollar denominated exploration and evaluation assets held by foreign subsidiaries. For the three months ended September 30, 2013, the Company recorded a loss from the exchange differences on translation of foreign operations of \$325,985 resulting in total comprehensive loss for the period of \$843,909.

## Cash Flows

### Three months ended September 30, 2014 and 2013:

During the three months ended September 30, 2014, the Company generated cash of \$619,641 in operating activities as compared to using cash of \$890,226 during the three months ended September 30, 2013. In the current period, the Company received \$671,354 (US\$609,658) for the settlement with the operator of Block 21 (Colombia) of a US\$567,027 letter of credit that was called in October 2013 by the ANH.

During the three months ended September 30, 2014, net cash used in financing activities was \$130,285 as compared to nil during the three months ended September 30, 2013. During the three months ended September 30, 2014, financing activities related cash amounts held at brokers.

During the three months ended September 30, 2014, net cash used in investing activities was \$1,261,603 as compared to \$1,033,051 during the three months ended September 30, 2013. During the three months ended September 30, 2014, the Company spent cash on expenditures on exploration and evaluation assets of \$228,491 as compared to cash expenditures of \$1,117,578 during the three months ended September 30, 2013, a decrease that continues to reflect the Company's decreased oil and gas activities. During the three months ended September 30, 2014, the Company had proceeds on the disposal of investments of \$423,744 and purchased \$1,456,856 of investments.

For the three months ended September 30, 2014, the Company had a net decrease in cash and cash equivalents of \$772,247 as compared to \$1,923,277 for the three months ended September 30, 2013. For the three months ended September 30, 2014, the Company also had a loss from the exchange rate changes on its foreign operations' cash balances of \$19,680, leaving a cash and cash equivalents balance of \$4,585,356 as at September 30, 2014 as compared to an exchange gain of \$20,702, leaving a cash and cash equivalents balance of \$7,692,489 as at September 30, 2013.

### Segmented information:

Reportable segments are defined as components of an enterprise about which separate financial information is available, that are evaluated regularly by the chief operating decision maker in deciding how to allocate resources and in assessing performance. All of the Company's operations relate to direct and indirect investments in the oil and gas sector. The Company's significant segments consist of six distinct geographic areas: Colombia, Israel, Canada, United States, Argentina and Brazil. There were no changes in the reportable segments since June 30, 2014.

The accounting policies applied to Brownstone's operating segments are the same as those described in the summary of significant accounting policies except that certain expenses and other items are not allocated to the individual operating segments when determining income or loss, but are attributed to the Canadian operations where the corporate head office is located.



The following is segmented information as at and for the three months ended September 30, 2014:

	Three months ended September 30, 2014		As at September 30, 2014		
	Interest and other income	Net loss for the period	Exploration and evaluation assets	Other assets	Total assets
Canada and other	\$ 73,267	\$ 586,742	\$ 3	\$ 8,724,284	\$ 8,724,287
Israel	-	8,558	-	12,401	12,401
United States	-	2,082,132	2,129,520	14,115	2,143,635
Colombia	-	87,719	-	292,625	292,625
Argentina	-	1,932	902,838	8,231	911,069
Brazil	-	170	-	128,576	128,576
	<b>\$ 73,267</b>	<b>\$ 2,767,253</b>	<b>\$ 3,032,361</b>	<b>\$ 9,180,232</b>	<b>\$ 12,212,593</b>

The following is segmented information for the three months ended September 30, 2013 and as at June 30, 2014:

	Three months ended September 30, 2013		As at June 30, 2014		
	Interest and other income	Net loss for the period	Exploration and evaluation assets	Other assets	Total assets
Canada and other	\$ 1,644	\$ 287,621	\$ 3	\$ 9,570,543	\$ 9,570,546
Israel	1,478	14,961	-	17,458	17,458
United States	-	-	4,051,756	66,235	4,117,991
Colombia	884	102,591	-	407,888	407,888
Argentina	-	112,751	859,984	5,471	865,455
Brazil	-	-	-	136,277	136,277
	<b>\$ 4,006</b>	<b>\$ 517,924</b>	<b>\$ 4,911,743</b>	<b>\$ 10,203,872</b>	<b>\$ 15,115,615</b>

### Liquidity and capital resources:

<b>Consolidated statements of financial position highlights</b>		
	<b>September 30, 2014</b>	<b>June 30, 2014</b>
Cash and cash equivalents	\$ 4,585,356	\$ 5,377,283
Investments, at fair value	4,172,900	3,707,817
Exploration and evaluation assets	3,032,361	4,911,743
Total assets	12,212,593	15,115,615
Total liabilities	719,769	1,031,132
Share capital and contributed surplus	121,145,273	121,135,056
Foreign currency translation reserve	453,197	287,820
Deficit	(110,105,646)	(107,338,393)
Working Capital	8,460,463	9,172,740

Accounts payable and accrued liabilities decreased by \$311,363 to \$719,769 as at September 30, 2014 as compared to \$1,031,132 as at September 30, 2013. As at September 30, 2014, the accounts payable and accrued liabilities included \$620,217 for exploration and evaluation cash calls as compared to \$841,989 as at June 30, 2014.

The Company has committed and is required to meet all of its drilling and related expenditures as they become due to maintain the Company's interests in its oil and gas properties (see "Exploration and evaluation assets" section). These exploration and evaluation assets' obligations are not fixed and cannot be pre-determined with certainty. Failure to meet the obligations may result in the dilution or loss of the Company's interests.

The Company's cash and cash equivalents and investments as at September 30, 2014 would be sufficient to meet the Company's current liabilities. As at September 30, 2014, the Company had working capital of \$8,460,463 as compared to working capital of \$9,172,740 as at June 30, 2014. The decrease in working capital since June 30, 2014 was primarily due to the decrease in the fair value of the Company's investment portfolio and the payment of Colombian exploration and evaluation cash calls during the three months ended September 30, 2014.

The Company continues to have no long-term debt. In order to meet its operating and capital expenditure obligations as they become due, Brownstone will have to rely on external sources of capital. The Company expects to have to raise additional funds through debt and/or equity financings to meet its obligations and has completed and will continue to consider, where warranted, strategic dispositions of certain of its interests in order to raise funds and/or reduce its capital expenditure requirements. The Company's ability to access the debt and equity markets and sell property interests when required will depend upon factors beyond its control, such as economic and political conditions that may affect the capital markets generally and the oil and gas industry specifically, including conditions pertaining to the countries in which it operates. The Company's inability to raise sufficient capital to fund its operations and growth may result in the loss of some or all of the Company's interests and, accordingly, could have a material adverse effect on the Company's business, financial condition, and results of operations, and its ability to continue as a going concern.

#### Related party transactions:

All transactions with related parties have occurred in the normal course of operations and are recorded at the exchange amount, which is the amount of consideration established and agreed to by the related parties.

- (a) Compensation to key management personnel and directors during the three months ended September 30 were as follows:

Type of expense	2014	2013
Salaries and consulting fees	\$ 144,188	\$ 269,187
Other short-term benefits	3,974	5,499
Stock-based compensation expense	8,400	40,836
	\$ 156,561	\$ 315,522

Key management personnel are the Chairman and Chief Executive Officer, Chief Financial Officer and Vice President, Corporate & Legal Affairs. In the prior year, key management personnel also included the President and Chief Operating Officer who resigned on May 31, 2014.

- (b) There were no options granted during the current period. During the three months ended September 30, 2013, the Company granted 2,550,000 options to directors and officers of the Company, with an exercise price of \$0.10 per share and expiring on September 9, 2018.

**Off-Balance sheet arrangements:**

As at September 30, 2014, the Company does not have any off-balance sheet arrangements that have, or are reasonable likely to have, a current or future effect on the results of operations or financials condition of Brownstone.

**Management of capital:**

There were no changes in the Company's approach to capital management during the three months ended September 30, 2014. The Company's capital includes equity comprised of share capital, contributed surplus, foreign currency translation reserve, and deficit. To date, the Company has not declared any cash dividends to its shareholders as part of its capital management program. The Company's current capital resources are sufficient to discharge its liabilities as at September 30, 2014.

**Risk management:**

(a) Market risk:

There were no changes in the way the Company manages market risk during the three months ended September 30, 2014. The Company manages market risk by having a portfolio which is not singularly exposed to any one issuer; however, its investment activities are currently concentrated primarily in the oil and gas resource industry.

The following table shows the estimated sensitivity of the Company's after-tax net loss for the three months ended September 30, 2014 from a change in the closing trade price of the Company's investments with all other variables held constant as at September 30, 2014:

Percentage of change in closing trade price	Decrease in net after-tax loss from % increase in closing trade price	Increase in net after-tax loss from % decrease in closing trade price
2%	\$ 72,400	\$ (72,400)
4%	144,800	(144,800)
6%	217,199	(217,199)
8%	289,599	(289,599)
10%	361,999	(361,999)

The following table shows the estimated sensitivity of the Company's after-tax net loss for the three months ended September 30, 2013 from a change in the closing trade price of the Company's investments with all other variables held constant as at September 30, 2013:

Percentage of change in closing trade price	Decrease in net after-tax loss from % increase in closing trade price	Increase in net after-tax loss from % decrease in closing trade price
2%	\$ 36,372	\$ (36,372)
4%	72,745	(72,745)
6%	109,117	(109,117)
8%	145,490	(145,490)
10%	181,862	(181,862)

(b) Currency risk:

The Company presently holds funds in Canadian dollars but a significant amount of its costs are denominated in U.S. dollars, Colombian pesos, and Argentinean pesos. The Company does not engage in any hedging activities to mitigate its foreign exchange risk. A change in the foreign exchange rate of the Canadian dollar versus another currency may increase or decrease the value of the Company's financial instruments. The Company does not hedge its foreign currency exposure.

The following assets and liabilities were denominated in foreign currencies:

	September 30, 2014	June 30, 2014
Denominated in U.S. dollars:		
Cash and cash equivalents	\$ 4,394,831	\$ 5,163,293
Prepays and receivables	33,827	221,862
Income tax receivable	227,685	242,537
Exploration and evaluation assets	3,032,358	4,911,740
Accounts payable and accrued liabilities	(658,500)	(966,052)
Net assets denominated in U.S. dollars	<u>7,030,201</u>	<u>9,573,380</u>
Denominated in Brazilian reals:		
Cash and cash equivalents	<u>128,576</u>	136,277
Net assets denominated in Brazilian reals	<u>128,576</u>	<u>136,277</u>
Denominated in Argentinean pesos:		
Cash and cash equivalents	<u>8,231</u>	5,471
Net assets denominated in Argentinean pesos	<u>8,231</u>	<u>5,471</u>
Denominated in Colombian pesos:		
Cash and cash equivalents	<u>38,336</u>	6,407
Net assets denominated in Colombian pesos	<u>38,336</u>	<u>6,407</u>

The following table shows the estimated sensitivity of the Company's total comprehensive loss for the three months ended September 30, 2014 from a change in the U.S. dollar exchange rate in which the Company has significant exposure with all other variables held constant as at September 30, 2014:

Percentage change in U.S. dollar exchange rate	Decrease in total comprehensive loss from an increase in % in the U.S. dollar exchange rate	Increase in total comprehensive loss from a decrease in % in the U.S. dollar exchange rate
2%	\$ 103,344	\$ (103,344)
4%	206,688	(206,688)
6%	310,032	(310,032)
8%	413,376	(413,376)
10%	<u>516,720</u>	<u>(516,720)</u>

The following table shows the estimated sensitivity of the Company's total comprehensive loss for the year ended June 30, 2014 from a change in the U.S. dollar exchange rate in which the Company has significant exposure with all other variables held constant as at June 30, 2014:

Percentage change in U.S. dollar exchange rate	Decrease in total comprehensive loss from an increase in % in the U.S. dollar exchange rate	Increase in total comprehensive loss from a decrease in % in the U.S. dollar exchange rate
2%	\$ 140,729	\$ (140,729)
4%	281,457	(281,457)
6%	422,186	(422,186)
8%	562,915	(562,915)
10%	703,643	(703,643)

**Risks:**

Brownstone's financial condition, results of operation and business are subject to certain risks, which may negatively affect them. Certain of these risks are described below in addition to elsewhere in this MD&A.

(a) Exploration and Development

The business of exploring for, developing and producing oil and gas involves a high degree of risk. Oil and gas reserves may never be found or, if discovered, may not be result in production at reasonable costs or profitability. The business of exploring, developing and producing is also capital intensive and, to the extent that cash flows from operating activities and external sources become limited or unavailable, the ability of Brownstone and of its operating partners to meet their respective financial obligations which are necessary to maintain their interests in the underlying properties could be impaired, resulting in those of the interests.

(b) Investment Risks:

The Company acquires securities of public and private companies from time to time, which are primarily junior or small-cap resource companies. The market values of these securities can experience significant fluctuations in the short and long term due to factors beyond the Company's control. Market value can be reflective of the actual or anticipated operating results of the companies and/or the general market conditions that affect the oil and gas sector as a whole, such as fluctuations in commodity prices and global political and economical conditions. The Company's investments are carried at fair value, and unrealized gains/losses on the securities and realized losses on the securities sold could have a material adverse impact on the Company's operating results. The recent decline in stock prices of the types of companies in which the Company invests have been very significant and such prices might take an extended time, to recover if they do at all.

(c) Dependence Upon Operating Partners:

Brownstone's oil and gas activities are conducted through partners in respect of which the Company is not the operator. Brownstone is dependent upon its operating partners for the financial and technical support, which they contribute to the Company's oil and gas properties. If Brownstone's operating partners are unable to fulfill their own contractual obligations, the

Company's interests could be jeopardized, resulting in project delays, additional costs and loss of the interests.

(d) Environmental:

The Company's oil and gas operations are subject to environmental regulations in the jurisdictions in which it operates. Environmental legislation is evolving in a manner which will likely require stricter standards and enforcement, increased costs, increased fines and penalties for non-compliance, more stringent environmental assessments of proposed projects and a heightened degree of responsibility for companies and their officers, directors and employees. There is no assurance that future changes in environmental regulation, if any, will not adversely affect the Company's operations. Environmental hazards may exist on the properties in which the Company holds interests which are presently unknown to the Company and which have been caused by previous or existing owners or operators of the properties or by illegal mining activities.

(e) Governmental:

Government approvals and permits are often generally required in connection with the Company's operations. To the extent such approvals are required and not obtained, the Company may be delayed or prohibited from proceeding with planned exploration or development of properties. Amendments to current laws, regulations and permits governing operations and activities of oil and gas companies, or more stringent implementation thereof, could have a material adverse impact on the Company and cause increases in capital expenditures or require abandonment or delays in development of new properties. Although the governments of the various countries in which Brownstone operates have been stable recently, there is no assurance that political and economic conditions will remain stable. Political and economic instability may impede the Company's ability to continue its exploration activities in the manner currently contemplated.

(f) Foreign Operations:

The Company is exposed to risks of political instability and changes in government policies, laws and regulations in every country in which the Company has oil and gas interests. The Company holds interests in Argentina, Colombia, Israel and in other jurisdictions that may be affected in varying degrees by political stability, government regulations relating to the oil and gas industry and foreign investment therein. Any changes in regulations or shifts in political conditions are beyond the Company's control and may adversely affect the Company's business. The Company's operations may be affected in varying degrees by government regulations, including those with respect to restrictions on production, price controls, export controls, income taxes, expropriation of property, employment, land use, water use, environmental legislation and mine safety. There is no assurance that permits can be obtained, or that delays will not occur in obtaining all necessary permits or renewals of such permits for existing properties or additional permits required in connection with future exploration and development programs. In the event of a dispute arising at the Company's foreign operations, the Company may be subject to the exclusive jurisdiction of foreign courts or may not be successful in subjecting foreign persons to the jurisdiction of courts in Canada. The Company may also be hindered or prevented from enforcing its rights with respect to a government entity or instrumentality because of the doctrine of sovereign immunity.

(g) Fluctuations in Crude Oil, Natural Gas, and Natural Gas Liquid Prices:

The price of the Company's common shares, and consolidated financial results and exploration, development and other oil and gas activities may in the future be significantly and adversely affected by declines in the price of crude oil, natural gas, and/or natural gas liquid (collectively "oil and gas"). The price of oil and gas fluctuates widely and is affected by numerous factors beyond the Company's control, such as interest rates, exchange rates, inflation or deflation, fluctuation in the value of the US dollar and foreign currencies, global and regional supply and demand, the political and economic conditions and production costs of major oil and gas producing countries throughout the world, and the cost of substitutes, inventory levels and carrying charges. Future material price declines could cause continued development of and commercial production from the properties in which the Company holds an interest to be impracticable. Depending on the price of oil and gas, cash flow from the Company's operations may not be sufficient and the Company could be forced to discontinue production and may lose the Company's interest in, or may be forced to sell, some of the Company's properties. Future production from the Company's properties is dependent upon the price of oil and gas being adequate to make these properties economic.

**Changes in Accounting Policies:**

Except as described below, the same accounting policies and methods of computation were followed in the preparation of the interim consolidated statements as were followed in the preparation and described in note 3 of the annual consolidated financial statements as at and for the year ended June 30, 2014.

Effective July 1, 2014, the Company has adopted the following new and revised standard, along with any consequential amendments. These changes were made in accordance with the applicable transitional provisions.

- (a) *Investment Entities* (Amendments to IFRS 10, IFRS 12 and IAS 27) - These amendments are effective for annual periods beginning on or after January 1, 2014 and provide an exception to the consolidation requirement for entities that meet the definition of an investment entity under IFRS 10. The exception to consolidation requires investment entities to account for subsidiaries at fair value through profit or loss.

The Company has assessed and determined that the amendments to IFRS 10, IFRS 12 and IAS 27 will not result in any change in the accounting or disclosures for its subsidiaries.

**Critical accounting estimates:**

The preparation of the consolidated financial statements in conformity with IFRS requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

Critical accounting estimates used in the preparation of the Company's interim financial statements include the Company's valuation of its privately-held investments, estimate of recoverable fair value on exploration assets, the valuation related to the Company's deferred tax assets ("DTA") and deferred

tax liabilities ("DTL"), and the Company's estimate of inputs for the calculation of the fair value of stock-based compensation expense, the Company's own warrants and broker warrants, and unlisted warrants of public companies held by Brownstone.

Valuation of privately-held investments:

The valuation of these investments ("private investments") requires management to assess the current financial status and prospects of private investments based upon potentially incomplete or unaudited financial information provided by the investee company, on management's general knowledge of the private investment's activities, and on any political or economic events that may impact upon the private investment specifically, and to attempt to quantify the impact of such events on the fair value of the investment. In addition to any events or circumstances that may affect the fair value of a particular private investment, management can consider general market conditions that may affect the fair value of either a particular private investment or of a group, segment or complete portfolio of private investments.

Changes in the fair value of our private investments for company-specific reasons have tended to be infrequent. Changes as a result of general market conditions may be more frequent from period to period during times of significant volatility, however, given the relatively small size of our private investment portfolio, such changes are not expected to have a material impact on our financial condition or operating results. For the three months ended September 30, 2014 and 2013, the Company had no change in unrealized gains or losses on investments relating to its private company investments.

Estimate of recoverable fair value on exploration and evaluation assets:

The costs of acquiring interests in exploration and evaluation assets are carried at cost until they are brought into production, at which time they are depleted on a unit-of-production method based on estimated recoverable proven oil and gas reserves. The Company's recorded value of exploration assets is based on historical costs that it expects to be recoverable in the future. The Company operates in an industry that is exposed to a number of risks and uncertainties, including exploration risk, development risk, commodity price risk, operating risk, political, ownership, funding, and currency risks, as well as environmental risk and overall economic conditions. All of these factors are potentially subject to significant change, out of the Company's control, and such changes are not determinable. Additionally, failure to conduct additional work on the Company's exploration properties may result in their loss. Accordingly, there is always the potential for a material adjustment to the value assigned to exploration assets.

At each reporting period, the Company's management reviews the status of all of its exploration properties, taking into account all of the factors noted above, in order to make an estimate of the recoverable value of each property. When management believes that the value of a property has been impaired, the Company will write down the value of the property to management's estimate of its recoverable value. As well, if the Company determines that an exploration project is not viable due to the risks described above or to unsatisfactory drill results, the Company will write-off the carrying value of the property. During the three months ended September 30, 2014, the Company recorded an impairment of \$2,071,157 (three months ended September 30, 2013 – impairment of \$87,056) on its exploration and evaluation assets to its net realizable value.



Deferred tax assets:

Deferred tax is provided using the statement of financial position method on temporary differences at the reporting date between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes.

DTL are recognized for all taxable temporary differences and DTA are recognized for all deductible temporary differences, carry forward of unused tax credits and unused tax losses. The Company does not record DTA to the extent that it considers it is not more likely than not that deductible temporary differences, the carry forward of unused tax credits and unused tax losses can be utilized.

Management determined, based upon expectations for future taxable income, that it believes that it is not more likely than not it will realize the tax benefits of the DTA during the next several years.

Stock-based Compensation Expense/Warrants and Broker Warrants:

The Company uses the Black-Scholes option pricing model to calculate stock-based compensation expense and the fair value of the warrants and broker warrants issued under the Company's private placements. The model requires six key inputs: exercise price, market price at date of issue, risk free interest rate, expected dividend yield, expected life and expected volatility. The first two inputs are facts rather than estimates, while the risk free interest rate, expected life, expected volatility and expected dividend yield (estimated at 0% based on the Company's history of not paying any dividends) are based on the Company's estimates. A shorter expected life of the option, lower volatility number or higher dividend yield used would result in a decrease in stock-based compensation expense. A longer expected life of the option or a higher volatility number used would result in an increase in stock-based compensation expense. The Company is also required to estimate the future forfeiture rate of options based on historical information in its calculation of stock-based compensation expense. These estimates involve considerable judgment and are, or could be, affected by significant factors that are out of the Company's control.

During the three months ended September 30, 2014, there were no stock options granted by the Company.

During the year ended June 30, 2014, the Company granted 2,980,000 stock options exercisable at \$0.10 per share expiring on September 9, 2018.

The fair value of the options granted during the year ended June 30, 2014 was estimated at the date of grant using the Black-Scholes option valuation model with the following assumptions:

Black-Scholes option valuation model assumptions used (weighted average)	
Expected volatility	<b>111.4%</b>
Expected dividend yield	<b>0%</b>
Risk-free interest rate	<b>1.8%</b>
Expected option life in years	<b>3.8 years</b>
Expected forfeiture rate	<b>4.9%</b>
Fair value per stock option granted on September 10, 2013	<b>\$ 0.04</b>

The expected volatility is based on the historical volatility over the life of the option at Brownstone's share price. The Company has not paid any cash dividends historically and has no plans to pay cash dividends in the foreseeable future. The risk-free interest rate is based on the yield of Canadian

Benchmark Bonds with equivalent terms. The expected option life in years represents the period of time that options granted are expected to be outstanding based on historical options granted.

Valuation of Unlisted Warrants of Public Companies:

The Company uses the Black-Scholes option pricing model to calculate the fair value of unlisted warrants of public companies if there are sufficient and reliable observable market inputs; if no such market inputs are available, the warrants are valued at intrinsic value. The model requires six key inputs: risk free interest rate, exercise price, market price at date of issue, expected dividend yield, expected life and expected volatility. The first four inputs are facts rather than estimates, while the expected life, expected volatility and expected dividend yield (estimated at 0% based on the Company's history of not paying any dividends) are based on the Company's estimates. A shorter expected life of the warrant, lower volatility number or higher dividend yield used would result in a decrease in the fair value of the warrant. A longer expected life of the warrant or a higher volatility number used would result in an increase in the fair value of the warrant. These estimates involve considerable judgment and are, or could be, affected by significant factors that are out of the Company's control. As at September 30, 2014 and June 30, 2014, there were not sufficient reliable observable market inputs and thus, the Company valued the warrants in its portfolio using their intrinsic value.

**Outstanding Share Data:**

Subsequent to September 30, 2014, 60,000 options at a weighted average exercise price of \$0.73 per share expired unexercised.

As at November 27, 2014, the number of common shares of the Company outstanding and the number of common shares issuable pursuant to other outstanding securities of Brownstone are as follows:

<b>Common shares</b>	<b>Number</b>
Outstanding	<b>129,794,289</b>
Issuable under options	<b>11,571,680</b>
<b>Total diluted common shares</b>	<b>141,365,969</b>

Refer to note 6 of the notes to the consolidated financial statements as at and for the three months ended September 30, 2014 for details of the Company's share capital as at September 30, 2014.

**Additional Information:**

Additional information relating to Brownstone maybe found on the Company's website at [www.brownstoneenergy.com](http://www.brownstoneenergy.com) or under the Company's profile on SEDAR at [www.sedar.com](http://www.sedar.com).