

# Management's Report

The management of Headwater Exploration Inc. has prepared the accompanying financial statements of Headwater Exploration Inc. in accordance with IFRS Accounting Standards as issued by the International Accounting Standards Board ("IFRS"). Financial and operating information presented throughout the regulatory filings is consistent with that shown in the financial statements.

Management is responsible for the integrity and objectivity of the financial information. Where necessary, the financial statements include estimates that are based on management's informed judgments. Internal control systems are designed and maintained to provide reasonable assurance that assets are safeguarded, transactions are properly authorized and reliable accounting records are produced for financial purposes.

KPMG LLP, an independent firm of Chartered Professional Accountants was appointed by the Company's shareholders to conduct an audit of the financial statements. Their examination included such tests and procedures as they considered necessary to provide reasonable assurance that the financial statements are presented fairly in accordance with IFRS.

The Board of Directors is responsible for ensuring that management fulfills its responsibilities for financial reporting and internal controls. It exercises its responsibilities primarily through the Audit Committee, which is comprised of three independent directors. The Committee meets regularly with management and with the independent auditors to satisfy itself that management's responsibilities are properly discharged, to review the financial statements and to recommend that the financial statements be presented to the Board of Directors for approval.

The Audit Committee has reviewed the financial statements and recommended their approval to the Board of Directors. The Board of Directors has approved the financial statements for issuance to the Company's shareholders.

(signed) "Jason Jaskela"

Jason Jaskela  
President and Chief Executive Officer

(signed) "Ali Horvath"

Ali Horvath, CPA, CA  
Chief Financial Officer

March 5, 2026



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## INDEPENDENT AUDITOR'S REPORT

To the Shareholders of Headwater Exploration Inc.

### ***Opinion***

We have audited the financial statements of Headwater Exploration Inc. (the Entity), which comprise:

- the statements of financial position as at December 31, 2025 and December 31, 2024
- the statements of income and comprehensive income for the years then ended
- the statements of changes in shareholders' equity for the years then ended
- the statements of cash flows for the years then ended
- and notes to the financial statements, including a summary of material accounting policy information

(Hereinafter referred to as the “financial statements”).

In our opinion, the accompanying financial statements present fairly, in all material respects, the financial position of the Entity as at December 31, 2025 and December 31, 2024, and its financial performance and its cash flows for the years then ended in accordance with IFRS Accounting Standards as issued by the International Accounting Standards Board.

### ***Basis for Opinion***

We conducted our audit in accordance with Canadian generally accepted auditing standards. Our responsibilities under those standards are further described in the “***Auditor’s Responsibilities for the Audit of the Financial Statements***” section of our auditor’s report.

We are independent of the Entity in accordance with the ethical requirements that are relevant to our audit of the financial statements in Canada and we have fulfilled our other ethical responsibilities in accordance with these requirements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.



## ***Key Audit Matters***

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the financial statements for the year ended December 31, 2025. These matters were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

We have determined the matters described below to be the key audit matters to be communicated in our auditor's report.

### ***Assessment of the impact of estimated proved and probable oil and natural gas reserves on depletion expense for the Alberta cash-generating unit ("CGU")***

#### ***Description of the matter***

We draw attention to note 2, note 3 and note 6 to the financial statements. Depletion of oil and natural gas properties is calculated using the unit-of-production basis over the estimated proved and probable oil and natural gas reserves before royalties. Depletion is calculated at the CGU level and takes into account expenditures incurred to date together with forecasted future development costs to develop the proved plus probable oil and natural gas reserves. The Entity recorded depletion expense related to its oil and natural gas properties of \$126 million for the year ended December 31, 2025, of which a portion relates to the Alberta CGU.

The estimate of proved and probable oil and natural gas reserves for the Alberta CGU requires the expertise of an independent third party reserve evaluator and includes significant assumptions related to:

- Forecasted oil and natural gas commodity prices
- Forecasted production
- Forecasted operating costs
- Forecasted royalty costs
- Forecasted future development costs.

The Entity engages an independent third party reserve evaluator to estimate the proved and probable oil and natural gas reserves for the Alberta CGU.

#### ***Why the matter is a key audit matter***

We identified the assessment of the impact of estimated proved and probable oil and natural gas reserves on depletion expense for the Alberta CGU as a key audit matter. Significant auditor judgement was required to evaluate the results of our audit procedures regarding the estimate of proved and probable oil and natural gas reserves for the Alberta CGU.



### ***How the matter was addressed in the audit***

The primary procedures we performed to address this key audit matter included the following:

We assessed the depletion expense calculation for compliance with IFRS Accounting Standards as issued by the International Accounting Standards Board.

With respect to the estimate of proved and probable oil and natural gas reserves for the Alberta CGU:

- We evaluated the competence, capabilities and objectivity of the independent third party reserve evaluator engaged by the Entity
- We compared the forecasted oil and natural gas commodity prices to those published by other independent third party reserve evaluators
- We compared the 2025 actual production, operating costs, royalty costs and development costs of the Entity to those estimates used in the prior year's estimate of proved oil and natural gas reserves to assess the Entity's ability to accurately forecast
- We evaluated the appropriateness of forecasted production and forecasted operating costs, royalty costs and future development cost assumptions by comparing to 2025 actual results. We took into account changes in conditions and events affecting the Entity to assess the adjustments or lack of adjustments made by the Entity in arriving at the assumptions.

### ***Other Information***

Management is responsible for the other information. Other information comprises the information included in Management's Discussion and Analysis.

Our opinion on the financial statements does not cover the other information and we do not and will not express any form of assurance conclusion thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information identified above and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit and remain alert for indications that the other information appears to be materially misstated.

We obtained the information included in Management's Discussion and Analysis as at the date of this auditor's report. If, based on the work we have performed on this other information, we conclude that there is a material misstatement of this other information, we are required to report that fact in the auditor's report.

We have nothing to report in this regard.



## ***Responsibilities of Management and Those Charged with Governance for the Financial Statements***

Management is responsible for the preparation and fair presentation of the financial statements in accordance with IFRS Accounting Standards as issued by the International Accounting Standards Board, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, management is responsible for assessing the Entity's ability to continue as a going concern, disclosing as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Entity or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Entity's financial reporting process.

## ***Auditor's Responsibilities for the Audit of the Financial Statements***

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion.

Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with Canadian generally accepted auditing standards will always detect a material misstatement when it exists.

Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements.

As part of an audit in accordance with Canadian generally accepted auditing standards, we exercise professional judgment and maintain professional skepticism throughout the audit.

We also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion.

The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Entity's internal control.



- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Entity's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Entity to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.
- Provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.
- Determine, from the matters communicated with those charged with governance, those matters that were of most significance in the audit of the financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our auditor's report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

*KPMG LLP*

Chartered Professional Accountants

The engagement partner on the audit resulting in this auditor's report is Shane Doig.

Calgary, Canada

March 5, 2026

# HEADWATER EXPLORATION INC.

## Statements of Financial Position

	December 31, 2025	December 31, 2024
<i>(thousands)</i>	\$	\$
<b>ASSETS</b>		
<b>Current assets</b>		
Cash and cash equivalents	99,655	142,694
Restricted cash (note 18)	2,350	350
Accounts receivable (note 16)	53,003	58,623
Financial derivative receivable (note 16)	393	3,088
Inventories	1,078	1,193
Prepays and deposits	1,562	1,701
<b>Total current assets</b>	<b>158,041</b>	<b>207,649</b>
Exploration and evaluation assets (note 5)	44,113	30,089
Property, plant and equipment (note 6)	790,753	712,020
Other assets	2,260	2,878
<b>Total assets</b>	<b>995,167</b>	<b>952,636</b>
<b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>		
<b>Current liabilities</b>		
Accounts payable and accrued liabilities (note 16)	65,695	70,846
Stock-based compensation payable (note 10)	28,711	14,768
Financial derivative liability (note 16)	1,225	2,847
Current portion of lease liability	959	631
Current income tax liability (note 11)	790	14,673
Dividends payable (note 9)	26,154	23,776
Repayable contribution (note 8)	4,556	1,373
<b>Total current liabilities</b>	<b>128,090</b>	<b>128,914</b>
Lease liability	1,325	2,089
Financial derivative liability (note 16)	-	382
Stock-based compensation payable (note 10)	11,266	6,913
Decommissioning liability (note 7)	35,177	48,603
Repayable contribution (note 8)	7,202	10,916
Deferred income tax liability (note 11)	63,952	55,360
<b>Total liabilities</b>	<b>247,012</b>	<b>253,177</b>
<b>Shareholders' Equity</b>		
Capital stock (note 9)	487,378	486,984
Contributed surplus	10,792	10,969
Retained earnings	249,985	201,506
<b>Total shareholders' equity</b>	<b>748,155</b>	<b>699,459</b>
<b>Total liabilities and shareholders' equity</b>	<b>995,167</b>	<b>952,636</b>

Commitments (note 18)  
Subsequent events (note 19)

*See accompanying notes to the financial statements*

Approved on behalf of the Board of Directors:

(signed) "Chandra Henry"  
Chandra Henry, CPA, CA, Director

(signed) "Neil Roszell"  
Neil Roszell, Executive Chairman

# HEADWATER EXPLORATION INC.

## Statements of Income and Comprehensive Income

	Year ended December 31,	
	2025	2024
<i>(thousands, except per share data)</i>	\$	\$
<b>REVENUE</b>		
Sales (note 12)	618,280	619,804
Royalties	(103,987)	(108,307)
	514,293	511,497
Gains (losses) on financial derivatives (note 16)	(7,197)	1,179
	507,096	512,676
<b>EXPENSES</b>		
Blending and transportation	70,858	68,063
Production	61,349	54,551
General and administrative	12,396	10,992
Stock-based compensation (note 10)	26,011	12,004
Depletion and depreciation (note 6)	127,037	124,883
Exploration and evaluation expense (note 5)	8,256	-
	305,907	270,493
Interest income and other expense (note 13)	837	3,306
Income before income taxes	202,026	245,489
Current income tax expense (note 11)	40,220	51,962
Deferred income tax expense (note 11)	8,599	5,499
	48,819	57,461
<b>Net income and comprehensive income</b>	<b>153,207</b>	<b>188,028</b>
Net income per share (note 9)		
Basic	0.64	0.80
Diluted	0.64	0.80

*See accompanying notes to the financial statements*

# HEADWATER EXPLORATION INC.

## Statements of Cash Flows

	Year ended December 31,	
	2025	2024
<i>(thousands)</i>	\$	\$
<b>OPERATING</b>		
Net income	153,207	188,028
Items not involving cash:		
Unrealized losses on financial derivatives (note 16)	691	3,803
Stock-based compensation	26,011	12,004
Depletion & depreciation	127,037	124,883
Exploration and evaluation expense	8,256	-
Non-cash finance charges	2,756	2,435
Income tax expense	48,819	57,461
Restricted cash (note 18)	(2,000)	-
Settlement of decommissioning liability (note 7)	(332)	(95)
Income taxes paid (note 15)	(54,103)	(59,686)
Change in non-cash operating working capital (note 15)	(13,205)	(12,096)
Cash flows provided by operating activities	297,137	316,737
<b>FINANCING</b>		
Payment of lease liability	(840)	(292)
Proceeds from exercise of stock options (note 9)	-	551
Dividends paid (note 9)	(102,350)	(94,919)
Purchase of common shares for cancellation (note 9)	(7,654)	-
Share issue costs (note 9)	(30)	-
Proceeds from (repayments of) repayable contribution (note 8)	(1,417)	1,417
Cash flows used in financing activities	(112,291)	(93,243)
<b>INVESTING</b>		
Capital expenditures – exploration and evaluation (note 5)	(41,168)	(44,524)
Capital expenditures – property, plant and equipment (note 6)	(187,120)	(178,342)
Government grant (note 8)	-	354
Change in non-cash investing working capital (note 15)	403	(4,340)
Cash flows used in investing activities	(227,885)	(226,852)
Change in cash and cash equivalents	(43,039)	(3,358)
Cash and cash equivalents, beginning of year	142,694	146,052
Cash and cash equivalents, end of year	99,655	142,694

*See accompanying notes to the financial statements*

# HEADWATER EXPLORATION INC.

## Statements of Changes in Shareholders' Equity

	Notes	Capital stock	Contributed surplus	Retained earnings	Total shareholders' equity
<i>(thousands)</i>		\$	\$	\$	\$
<b>Balance at January 1, 2024</b>		<b>483,013</b>	<b>18,970</b>	<b>108,515</b>	<b>610,498</b>
Exercise of stock options	9	3,971	(3,420)	-	551
Stock-based compensation	10	-	7,284	-	7,284
Reclassification to stock-based compensation payable	10	-	(11,865)	-	(11,865)
Net income		-	-	188,028	188,028
Dividends declared	9	-	-	(95,037)	(95,037)
<b>Balance at December 31, 2024</b>		<b>486,984</b>	<b>10,969</b>	<b>201,506</b>	<b>699,459</b>
<b>Balance at January 1, 2025</b>		<b>486,984</b>	<b>10,969</b>	<b>201,506</b>	<b>699,459</b>
Exercise of stock options	9	331	(331)	-	-
Stock-based compensation	10	-	154	-	154
Net income		-	-	153,207	153,207
Dividends declared	9	-	-	(104,728)	(104,728)
Purchase of common shares for cancellation	9	(7,654)	-	-	(7,654)
Issued on land acquisition	9	7,740	-	-	7,740
Share issue costs, net of deferred tax	9	(23)	-	-	(23)
<b>Balance at December 31, 2025</b>		<b>487,378</b>	<b>10,792</b>	<b>249,985</b>	<b>748,155</b>

*See accompanying notes to the financial statements*

# HEADWATER EXPLORATION INC.

## Notes to the Financial Statements

As at and for the years ended December 31, 2025 and 2024

*(All tabular amounts in thousands, unless otherwise stated)*

### 1. NATURE OF OPERATIONS AND GENERAL INFORMATION

Headwater Exploration Inc. (“Headwater” or the “Company”) is a Canadian resource company engaged in the exploration for and development and production of petroleum and natural gas in Canada. Headwater is a public company existing under the Alberta Business Corporations Act with common shares listed on the Toronto Stock Exchange (“TSX”) under the symbol “HWX”.

Headwater’s principal place of business is located at 1400, 215 – 9<sup>th</sup> Avenue S.W., Calgary, Alberta, T2P 1K3 and its registered office is located at 2400, 525 - 8<sup>th</sup> Avenue S.W., Calgary, Alberta, T2P 1G1.

### 2. BASIS OF PREPARATION

#### *Statement of compliance*

These audited annual financial statements have been prepared in accordance with IFRS Accounting Standards as issued by the International Accounting Standards Board (“IFRS”). The accounting policies discussed in note 3 have been consistently applied for all periods presented in these financial statements.

These audited annual financial statements were approved and authorized for issue by the Company’s Board of Directors on March 5, 2026.

#### *Basis of measurement, functional and presentation currency*

These audited annual financial statements have been prepared on a historical cost basis except for certain financial instruments and the stock-based compensation payable which are measured at fair value through profit or loss and inventories which are measured at the lower of cost and net realizable value.

The financial statements are presented in Canadian dollars, which is the Company’s functional currency.

#### *Use of estimates and judgments*

The preparation of the Company’s financial statements in accordance with IFRS requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Such estimates and assumptions are evaluated at each reporting date and are based on management’s experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. Estimates are more difficult to determine, and the range of potential outcomes can be wider, in periods of higher volatility and uncertainty. The impacts of various events such as the Russian invasion of Ukraine, middle eastern conflicts and the United States interventions in Venezuela, along with the imposition of United States tariffs on Canadian imported goods and their impact on energy markets and general market conditions, increased interest and inflation rates and supply chain uncertainties have created a higher level of volatility and uncertainty. Management has, to the extent reasonable, incorporated known facts and circumstances into the estimates made however, actual results could differ from those estimates and those differences could be material. The Company has also identified the below as an area requiring significant judgments, assumptions or estimates:

### *Climate change and alternative energy sources*

The following provides certain disclosures as to the impact of climate change on the amounts recorded in the financial statements as at and for the year ended December 31, 2025. The below is not a comprehensive list or analysis of all climate change impacts and risks.

Emissions, carbon and other regulations impacting climate and climate related matters are constantly evolving. In recent years, the Canadian Sustainability Standards Board (“CSSB”) worked to advance and adopt Canadian climate-related reporting standards based on international climate-related reporting standards. In addition, the Canadian Securities Administrators (“CSA”) had begun their own consultation process to determine how CSSB's reporting standards would be translated into reporting requirements for reporting issuers and the timing for the implementation of such mandatory reporting requirements; however, on April 23, 2025, the CSA announced that it would be pausing work on the development of new climate related reporting requirements due to current global economic and geopolitical uncertainty and rising competitive concerns for Canadian issuers. The CSA has noted that it expects to revisit the adoption of climate related disclosures in the future. To the extent that any new climate or sustainability related standards are adopted in the future, the Company would likely incur additional costs to comply with such standards.

The Company has considered the impact of the evolving worldwide demand for energy and global advancement of alternative sources of energy that are not sourced from fossil fuels in its assessment as a possible indication of impairment of its oil and gas properties. The Company completed the analysis of triggers for impairment as at December 31, 2025, and climate risk/climate change, in of itself, did not result in the Company completing an impairment test. The Company has considered the impact of the evolving worldwide demand for energy and global advancement of alternative sources of energy that are not sourced from fossil fuels in its assessment of depletion on its oil and gas properties. Depletion of the Company's oil and gas properties was based on proved and probable reserves, the life of which is generally less than 40 years. The ultimate period in which global energy markets can transition from carbon-based sources to alternative energy is highly uncertain, however, the majority of the Company's proved and probable reserves per the 2025 reserve report should be realized prior to the elimination of carbon-based energy. At this time, the Company has not capped its reserve life for purposes of calculating depletion expense, however, this estimate will be monitored as the energy evolution continues.

The Company engages a third-party external reserve engineer to prepare the reserve report. The reserve report includes anticipated impacts from emissions related taxes, most notably the reserve report includes estimated carbon tax related to the Company's operations consistent with the Emissions Management and Climate Resilience Act (Alberta).

The evolving energy transition and general public sentiment to the oil and gas industry may result in reduced access to capital markets. Management will continue to adjust the capital structure as necessary in response to changing industry conditions.

The Company maintains insurance coverage that provides a level of insurance for certain events that may arise due to climate change factors; however, the Company's insurance program is subject to limits and various restrictions. No claims were made under the Company's insurance policies in 2025 with respect to climate related matters.

#### a) Critical Judgments in Applying Accounting Policies

##### *Determination of cash-generating units (“CGU”) and impairment*

The determination of what constitutes a CGU used to test the recoverability of the carrying values of the Company's oil and gas properties is subject to management's judgment. Judgments are made in regard to shared infrastructure, geographical proximity, petroleum type and similar exposure to market risks and materiality. The asset composition of a CGU can directly impact the recoverability of the assets included therein.

Judgments are required to assess when impairment indicators exist, and when impairment testing is required.

### *Exploration and evaluation (“E&E”) assets*

The application of the Company’s accounting policy for E&E assets requires management to make certain judgments as to whether economic quantities of reserves have been found. Judgment is also required to determine the level at which E&E is assessed for impairment; for Headwater, the recoverable amount of E&E assets is assessed at a CGU level.

#### b) Key Sources of Estimation Uncertainty

##### *Recoverability of asset carrying value and the impact of reserves on depletion and the evaluation of the recoverable amount of a CGU*

At each reporting date, the Company assesses its property, plant and equipment and E&E assets to determine if there is any indication that the carrying amount of the assets may not be recoverable. Determination as to whether and how much an asset is impaired involves management’s estimates on highly uncertain matters. The key estimates used in the determination of cash flows from crude oil and natural gas reserves and the volume of proved and probable crude oil and natural gas reserves include the following:

- i) Reserves and forecasted production – assumptions that are valid at the time of reserve estimation may change significantly when new information becomes available. Changes in future price estimates, production levels or results of future drilling may change the economic status of reserves and may ultimately result in reserve revisions.
- ii) Forecasted crude oil and natural gas prices – commodity prices can fluctuate for a variety of reasons including supply and demand fundamentals, inventory levels, exchange rates, weather, and economic and geopolitical factors.
- iii) Discount rate – the discount rate used to calculate the net present value of cash flows is based on estimates of an approximate industry peer group weighted average cost of capital. Changes in the general economic environment could result in significant changes to this estimate.
- iv) Forecasted operating and royalty costs and future development costs – estimates concerning future drilling and infrastructure costs and production costs required to operate the assets are used in the cash flow model.

Changes in circumstances may impact these estimates which could have a material financial impact in future periods.

Reserves estimates also have a material financial impact on depletion expense and decommissioning liabilities, all of which could have a material impact on financial results. These reserve estimates are evaluated by third-party reserve evaluators at least annually, who work with information provided by the Company to establish reserve determinations in accordance with National Instrument 51-101 - Standards of Disclosure for Oil and Gas Activities (“NI 51-101”). Changes in circumstances may impact these estimates which could have a material financial impact in future periods.

##### *Decommissioning liabilities*

The decommissioning costs which will ultimately be incurred by the Company are uncertain and estimates can vary in response to many factors including changes to regulatory requirements, changes to relevant legal requirements, the emergence of new restoration techniques or experience at other production sites. The expected timing can also change in response to changes in reserves, changes in laws and regulations or the rate of the energy transition. As a result, there could be significant adjustments to the provisions established which could materially affect future financial results. Judgments include the most appropriate discount rate to use, which management has determined to be a risk-free rate, as well as the underlying cost estimates as they are derived from a combination of published industry benchmarks as well as site specific information.

##### *Valuation of financial instruments*

The estimated fair values of the Company’s financial derivative commodity contracts are subject to measurement uncertainty due to the estimation of future crude oil and natural gas commodity prices and volatility.

### *Valuation of performance share units ("PSUs")*

The estimate of stock-based compensation in respect of the Company's PSUs is dependent on the performance multiplier estimated by management.

## **3. SUMMARY OF MATERIAL ACCOUNTING POLICIES**

The following accounting policies have been applied consistently for all periods presented in these audited annual financial statements.

### a) Joint interest

A portion of the Company's exploration, development and production activities is conducted jointly with others through an unincorporated joint venture. These financial statements reflect only the Company's proportionate interest of these jointly controlled assets and the proportionate share of the relevant revenue and related costs.

### b) Financial instruments

Headwater's financial assets and liabilities are classified into two categories: amortized cost and at fair value through profit or loss ("FVTPL"). The classification of financial assets is determined by the characteristics of the contractual cash flows. Headwater does not classify any of its financial instruments as fair value through other comprehensive income.

Financial assets and liabilities are measured at fair value on initial recognition, which is typically the transaction price, unless a financial instrument contains a significant financing component.

#### i) Financial assets at amortized cost

Financial assets at amortized cost include cash and cash equivalents, restricted cash, accounts receivable and deposits. Accounts receivable are financial assets held to collect contractual cash flows that represent payments of principal and interest only. The carrying values of these financial assets approximate fair values because of the short term to maturity.

The Company measures expected credit losses using a lifetime expected loss allowance for accounts receivable with expected lifetime losses recognized from initial recognition. Each period, Headwater assesses the expected credit losses on a forward-looking basis.

#### ii) Financial liabilities at amortized cost

Financial liabilities at amortized cost include accounts payable and accrued liabilities and dividends payable. The carrying values of these financial liabilities approximate fair values because of the short term to maturity. The repayable contribution is also recorded at amortized cost and its carrying value approximates its fair value.

#### iii) Fair value through profit or loss

The Company's financial derivative contracts are classified as fair value through profit or loss and are recognized at fair value based on quoted market prices at each reporting date. The Company does not apply hedge accounting to its derivative instruments.

### c) E&E assets

Once the legal right to explore has been acquired, costs directly associated with an exploration activity are capitalized as E&E assets and grouped by licensed exploration area. Costs are capitalized until the technical feasibility and commercial viability of extracting a mineral resource are demonstrable and the presence of

reserves has been established, after which capitalized costs are transferred to property, plant and equipment following an assessment for impairment.

The Company assesses E&E assets for impairment at a CGU level. E&E assets are not depleted.

d) Property, plant and equipment (“PP&E”)

*Oil and gas properties*

PP&E primarily consists of crude oil and natural gas development and production assets and is measured at cost less accumulated depletion and depreciation and accumulated impairment losses and reversals. These costs include property acquisitions, development drilling, completion and equipping costs, infrastructure costs, estimated decommissioning liabilities, directly attributable overhead and administration costs and transfers from E&E.

Costs incurred subsequent to the determination of technical feasibility and commercial viability and the costs of replacing parts of PP&E are recognized as oil and gas properties only when they increase the future economic benefits embodied in the specific asset to which they relate. All other expenditures are recognized in net income as incurred.

*Depletion and depreciation*

Depletion of oil and gas properties is calculated using the unit-of-production basis over the estimated proved plus probable oil and gas reserves before royalties, as determined, at least annually, by qualified independent reserves engineers. Depletion is calculated at the CGU level and takes into account expenditures incurred to date together with forecasted future development costs to develop the proved plus probable oil and gas reserves.

e) Income taxes

Deferred income tax is recognized for the temporary differences between the tax basis and carrying value of assets and liabilities. Deferred income tax is measured using the enacted or substantively enacted tax rates expected to be in effect when the deferred income tax assets are estimated to be realized or the deferred income tax liabilities are estimated to be settled.

Current income tax expense is the expected taxes payable on taxable income for the period, using tax rates enacted or substantively enacted at the reporting date.

f) Decommissioning liabilities

A decommissioning liability is recognized for the present value of the future cost of abandoning oil and gas wells or facilities and is calculated based on management’s best estimate of the expenditure using a combination of publicly available industry benchmarks and internal site-specific information. A decommissioning liability is recognized only when a legal or constructive obligation exists. The liability is measured at each reporting date at the fair value of the estimated expenditures expected to settle the obligation using a risk-free interest rate. An equivalent amount is capitalized as part of PP&E and depleted along with the related asset.

Changes in the estimated timing of settlement or future cash flows are dealt with prospectively by recording an adjustment to the decommissioning liability and a corresponding adjustment to the related asset. The unwinding of the discount on the decommissioning liability is included as accretion on decommissioning liability in interest income and other expense in the Statement of Income and Comprehensive Income. Actual expenditures are charged against the liability as incurred.

g) Revenue recognition

The Company generates revenue from the sale of commodities which include crude oil, natural gas and natural gas liquids (“NGLs”). Revenue is recorded when control is transferred to the buyer which is usually when legal title passes to the external party. The transaction price for variable priced contracts is based on the commodity price index, adjusted for quality, delivery location and other factors, whereby each component

of the pricing formula can be either fixed or variable, depending on the contract terms. The amount of revenue recognized is based on the agreed upon transaction price, whereby any variability in revenue relates specifically to the Company's efforts to transfer production, and therefore the resulting revenue is allocated to the production delivered in the period during which the variability occurs. As a result, none of the variable consideration is considered constrained.

Headwater's crude oil, natural gas and NGLs revenue do not contain significant financing components and payments are typically due 25 days following the month of delivery.

Each contract is evaluated based on the nature of the performance obligations, including the Company's role as either principal or agent. Where the Company acts as principal, revenue is recognized on a gross basis. Where the Company acts as agent, revenue is recognized on a net basis.

#### h) Transportation and blending

Transportation services procured by Headwater are recognized in blending and transportation expense.

Headwater is required to purchase commodity products from third parties to utilize in blending activities. Headwater subsequently sells the blended products to its customers. These transactions are presented in revenue with the related expense included in blending and transportation expense recognized in the Statement of Income and Comprehensive Income.

The costs associated with the transportation of crude oil, natural gas and NGLs, including the cost of diluent used in blending, are recognized when the product is sold.

#### i) Impairment of non-financial assets

At each reporting date, the Company assesses whether there is an indication that an asset or CGU may be impaired or that historical impairment may be reversed. A CGU includes a group of assets that generates cash flows that are largely independent of the cash inflows from other groups of assets. A CGU may also include certain aggregated E&E assets. If any indication of impairment exists, the Company estimates the asset's or CGU's recoverable amount. The recoverable amount is the higher of an asset's or CGU's fair value less costs of disposal ("FVLCD") and its value-in-use. When the carrying amount of an asset or CGU exceeds its recoverable amount, the asset is written down to its recoverable amount with the impairment loss recognized in the Statement of Income and Comprehensive Income.

A previously recognized impairment loss is reversed if there has been a change in the assumptions used to determine the asset's or CGU's recoverable amount when the impairment loss was initially recognized. However, the amount of the impairment loss reversal is limited so that the carrying amount of the asset does not exceed its recoverable amount, nor exceed the carrying amount that would have been recognized, net of depletion expense, had no impairment loss been recognized for the asset in prior years. Any reversal of previously recognized impairment losses is recognized in the Statement of Income and Comprehensive Income.

#### j) Stock-based compensation

Restricted share units ("RSUs") and PSUs are cash-settled. The fair value of the liability is determined based on the Company's closing share price on the financial reporting date. For PSUs, the amount of stock-based compensation payable and related expense is adjusted based on a performance multiplier ranging from 0 to 2 times, which is based on certain corporate performance measures, as determined by the Board of Directors. During the year ended December 31, 2024, the Board of Directors approved the change in form of settlement for the Company's PSUs from equity to cash.

The Company capitalizes a portion of stock-based compensation for RSUs and PSUs that is directly attributable to development activities.

Deferred share units ("DSUs") are also cash-settled. The fair value of the liability is determined based on the Company's closing share price on the financial reporting date.

k) Net income per share

Basic net income per share is computed by dividing net income by the weighted average number of common shares outstanding during the year. For the diluted net income per share calculation, the weighted average number of common shares outstanding is adjusted for the potential number of common shares which may have a dilutive effect on net income per share. The weighted average number of diluted shares is calculated in accordance with the treasury stock method. The treasury stock method assumes that the proceeds received from the exercise of all potentially dilutive instruments are used to repurchase common shares at the average market price.

l) Share repurchases under Normal Course Issuer Bid (“NCIB”)

Shares that are repurchased for cancellation are accounted for as a reduction to capital stock. Total consideration includes commissions and a 2% federal tax accrued on the purchase, which is charged against capital stock.

#### 4. SUMMARY OF NEW ACCOUNTING POLICIES AND DISCLOSURES

##### *Recently announced accounting pronouncements*

IFRS 18 “Presentation and disclosure in financial statements” has been issued which will replace IAS 1 “Presentation of financial statements”. The new standard will introduce new totals, subtotals, and categories for income and expenses in the statements of income and comprehensive income, as well as requiring disclosure about management-defined performance measures and additional requirements regarding the aggregation and disaggregation of certain information. IFRS 18 is effective for annual periods beginning on or after January 1, 2027 and will be applied retroactively. The Company is currently evaluating the impact of adopting IFRS 18 on the financial statements.

Amendments to IFRS 9 “Financial Instruments and IFRS 7 Financial Instruments: Disclosures” have been issued with the intention to clarify the date of recognition and derecognition of some financial assets and liabilities. The amendments are effective January 1, 2026, with early adoption permitted. The Company is currently evaluating the impact of these amendments on the financial statements.

#### 5. EXPLORATION AND EVALUATION ASSETS

E&E assets consist of the Company’s undeveloped land, seismic and drilling costs for projects in which technical feasibility or commercial viability has yet to be determined.

The following table reconciles the movements of the Company’s E&E assets for the years:

	December 31, 2025	December 31, 2024
	\$	\$
Balance, beginning of year	30,089	17,930
Additions <sup>(1)</sup>	48,908	44,524
E&E expense	(8,256)	-
Transfers to PP&E (note 6)	(26,628)	(32,365)
Balance, end of year	44,113	30,089

(1) Includes non-cash consideration of \$7.7 million pursuant to a purchase and sale agreement which closed on September 25, 2025. The fair value was determined using Headwater’s closing share price on the closing date. (See note 9).

During the year ended December 31, 2025, the company recognized \$8.3 million of E&E expense related to its Saskatchewan assets.

## 6. PROPERTY, PLANT AND EQUIPMENT

The Company's PP&E includes oil and gas properties and corporate assets. Oil and gas properties include the Company's interest in developed petroleum and natural gas properties, as well as interests in facilities and pipelines.

The following table reconciles the movements of the Company's PP&E balance for the years:

	Oil and gas properties	Corporate	Total
Cost	\$	\$	\$
Balance at December 31, 2023	1,103,098	2,873	1,105,971
Additions	181,531	34	181,565
Transfers from E&E (note 5)	32,365	-	32,365
Changes in decommissioning liability (note 7)	6,302	-	6,302
Balance at December 31, 2024	1,323,296	2,907	1,326,203
Additions	193,058	36	193,094
Transfers from E&E (note 5)	26,628	-	26,628
Changes in decommissioning liability (note 7)	(14,781)	-	(14,781)
Balance at December 31, 2025	1,528,201	2,943	1,531,144
<b>Accumulated depletion, depreciation and impairment</b>			
Balance at December 31, 2023	487,227	2,369	489,596
Depletion or depreciation expense	124,519	68	124,587
Balance at December 31, 2024	611,746	2,437	614,183
Depletion or depreciation expense	126,147	61	126,208
Balance at December 31, 2025	737,893	2,498	740,391
Net book value at December 31, 2024	711,550	470	712,020
Net book value at December 31, 2025	790,308	445	790,753

Future development costs required to develop proved plus probable reserves in the amount of \$587.7 million were included in the depletion calculation for the Company's oil and gas properties for the year ended December 31, 2025 (December 31, 2024 – \$367.7 million).

The Company capitalized \$4.9 million of general and administrative costs for the year ended December 31, 2025 (December 31, 2024 – \$4.4 million) and capitalized \$6.0 million of stock-based compensation expense for the year ended December 31, 2025 (December 31, 2024 – \$3.2 million).

### **Indicators of Impairment**

The Company concluded there are no indicators of impairment for its PP&E assets as at December 31, 2025 and 2024.

## 7. DECOMMISSIONING LIABILITY

The following table reconciles the movements of the Company's decommissioning liability for the years:

	December 31, 2025	December 31, 2024
	\$	\$
Balance, beginning of year	48,603	40,951
Additions	8,773	10,725
Settlements	(332)	(95)
Change in estimate <sup>(1)</sup>	(23,554)	(4,423)
Accretion (note 13)	1,687	1,445
Balance, end of year	35,177	48,603
Key assumptions		
Risk free rate	3.9%	3.3%
Inflation rate	2.0%	1.8%

- (1) Relates to changes in the risk-free rate, inflation rate, time to abandonment and cost estimates. Of this amount, a \$12.9 million downward revision is the result of a change in cost estimates underpinned by a decrease to the industry's abandonment cost benchmarks, a \$6.2 million downward revision relates to changes in time to abandonment, a \$6.5 million downward revision is a result of an increase in risk-free rate over the year from 3.3% at December 31, 2024 to 3.9% at December 31, 2025 and a \$2.0 million upward revision is a result of an increase in the inflation rate over the year from 1.8% at December 31, 2024 to 2.0% at December 31, 2025.

The underlying cost estimates are derived from a combination of published industry benchmarks as well as site specific information. The Company has estimated the net present value of its total asset retirement obligations to be \$35.2 million as at December 31, 2025 (December 31, 2024 - \$48.6 million). The total future inflated and undiscounted amount of estimated cash flows required to settle these obligations is \$147.1 million (December 31, 2024 - \$134.2 million). Management estimates the settlement of these obligations will occur over the next 30 to 40 years.

Accretion of decommissioning liabilities is due to the passage of time and is presented within interest income and other expense in the Statement of Income and Comprehensive Income.

## 8. REPAYABLE CONTRIBUTION (NRCan ERF)

In 2022 and 2023, the Company received approval of a total of four claims pursuant to a repayable contribution agreement with the Department of Natural Resources Canada ("NRCan"), under the Emissions Reduction Fund ("ERF") Onshore Program. All funds have been received by the Company with respect to the four claims.

NRCan has provided financial assistance by way of a partially repayable interest-free loan to the Company for its working interest in the joint Marten Hills natural gas processing plant and gathering system, as well as for gas conservation equipment associated with the Company's wholly owned oil processing facility in Marten Hills. Headwater will repay 80% of the financial assistance pursuant to the terms and conditions of the agreement, with the remaining 20% being non-repayable. The repayable portion of the funds received are to be repaid as follows: 10% was repaid on June 30, 2025, with the remaining 33% to be repaid on June 30, 2026, and 57% on June 30, 2027.

Headwater accounts for the non-repayable portion and benefit of the interest-free period of the financial assistance as a government grant. Government grants are recognized when there is reasonable assurance that the grant will be received, and all conditions associated with the grant are met. As this grant relates to the Company's PP&E, the grant is recorded as a reduction to the asset's carrying amount and is depreciated over the useful life of the asset. For the year ended December 31, 2023, \$2.5 million was recognized as an offset against PP&E.

The Company has recognized a repayable contribution of \$12.8 million, undiscounted, and \$11.8 million, discounted, as at December 31, 2025 (December 31, 2024 - \$14.2 million and \$12.3 million respectively), with respect to claims submitted to the ERF and confirmed by NRCan. The Company discounts the repayable contribution at a weighted average interest rate of 7.7%.

	December 31, 2025	December 31, 2024
	\$	\$
Balance, beginning of year	12,289	11,405
Repayment	(1,417)	-
Interest (note 13)	886	884
Balance, end of year	11,758	12,289
Current portion of repayable contribution	4,556	1,373
Long-term portion of repayable contribution	7,202	10,916

The Company is in compliance with all terms and conditions of the repayable contribution agreement.

## 9. CAPITAL STOCK

- a) Authorized – unlimited common shares without nominal or par value.
- b) Issued and outstanding

	December 31, 2025		December 31, 2024	
	Number of shares	Amount	Number of shares	Amount
		\$		\$
Balance, beginning of year	237,757	486,984	236,580	483,013
Exercise of stock options	53	331	1,177	3,971
Purchase of common shares for cancellation	(1,047)	(7,654)	-	-
Issued on land acquisition <sup>(1)</sup>	1,000	7,740	-	-
Share issue costs, net of deferred tax	-	(23)	-	-
Balance, end of year	237,763	487,378	237,757	486,984

(1) During the year ended December 31, 2025, Headwater issued 1.0 million common shares as consideration for certain E&E assets (See note 5).

### **Stock Options**

During the year ended December 31, 2025, 177 thousand stock options were exercised for 53 thousand common shares on a cashless basis. Contributed surplus related to the options exercised of \$331 thousand was transferred to capital stock.

During the year ended December 31, 2024, 2.2 million stock options were exercised for 1.0 million common shares on a cashless basis, and 144 thousand stock options were exercised for 144 thousand common shares for total proceeds of \$551 thousand. Contributed surplus related to the options exercised of \$3.4 million was transferred to capital stock.

- c) NCIB

On May 1, 2025, Headwater announced TSX approval of its NCIB to purchase for cancellation up to 19,020,755 common shares during the period commencing on May 6, 2025, and terminating on the earlier of: (i) the date on which the Company has acquired all common shares sought pursuant to the NCIB; or (ii) to May 5, 2026, unless earlier terminated at the option of the Company, upon prior notice being given to the TSX.

During the year ended December 31, 2025, Headwater utilized its NCIB which resulted in approximately 1.05 million common shares being purchased for cancellation at an average price of \$7.30 per common share for total consideration of \$7.7 million. Total consideration includes commissions and a 2% federal tax accrued on the purchase, which is charged against capital stock.

d) Dividends

During the year ended December 31, 2025, the Company declared \$104.7 million (year ended December 31, 2024 - \$95.0 million) related to its quarterly cash dividend. Included in current liabilities is the dividend payable of \$26.2 million for the dividend declared on October 29, 2025, and paid out on January 15, 2026.

The Company increased its quarterly cash dividend to \$0.11 per common share (\$0.44 per common share annualized) effective for the dividend paid on April 15, 2025 to shareholders of record at the close of business on March 31, 2025.

e) Per share amounts

Basic per share amounts are calculated using the weighted average number of shares outstanding. The Company uses the treasury stock method to determine the impact of dilutive securities. The reconciling items between basic and diluted average common shares outstanding are stock options, RSUs, PSUs and accrued dividends on RSUs and PSUs.

	December 31, 2025	December 31, 2024
Weighted average shares outstanding		
Basic	237,877	236,386
Diluted	239,882	236,447

## 10. STOCK-BASED COMPENSATION

a) Stock-based compensation expense

The following table summarizes the breakdown of stock-based compensation expense for the years:

	December 31, 2025	December 31, 2024
	\$	\$
Stock options	-	201
Deferred share units	2,563	1,138
Share awards	29,422	13,888
Capitalized stock-based compensation	(5,974)	(3,223)
Total stock-based compensation expense	26,011	12,004

b) Share awards

The Company has an awards plan (the "Awards Plan") which provides for grants of RSUs and PSUs to officers, employees and consultants of the Company. Generally, one third of the RSUs will vest on each of the first, second and third anniversaries of the date of grant and all PSUs will vest on the third anniversary of the date of grant, unless otherwise determined by the Board of Directors.

### ***PSUs (Cash-Settled)***

On November 7, 2024, the Board of Directors approved the cash settlement of PSUs. Previously, these awards had been accounted for as equity-settled. As a result of this modification to the Company's outstanding PSUs from equity-settled to cash-settled, the fair value of the awards previously expensed was reclassified from contributed surplus to stock-based compensation payable. Subsequent to modification, the grant date fair value is used to record the cost of the PSUs and any subsequent remeasurement of the liability is also recognized in the Statement of Income and Comprehensive Income. The amount of stock-based compensation payable and related expense is adjusted based on a performance multiplier ranging from 0 to 2 times.

The following table summarizes the changes in the PSU liability for the years:

	December 31, 2025	December 31, 2024
	\$	\$
Balance, beginning of year	16,952	-
Reclassified from contributed surplus	-	11,865
Increase in liability/fair value adjustment <sup>(1)</sup>	26,916	5,087
Payout <sup>(2)</sup>	(10,982)	-
Balance, end of year	32,886	16,952
Current portion of stock-based compensation payable	22,445	10,652
Long-term portion of stock-based compensation payable	10,441	6,300

(1) Includes dividend and estimated performance multiplier adjustments.

(2) Includes dividend adjustment and an incremental 698 thousand units cash settled pursuant to a performance multiplier adjustment.

The PSU liability as at December 31, 2025 of \$32.9 million is based on a fair value of \$9.37 per PSU which is the Company's closing share price on December 31, 2025.

The following table summarizes the changes in the number of outstanding PSUs for the years:

	December 31, 2025	December 31, 2024
Outstanding, beginning of year	3,116	1,917
Granted	1,441	1,199
Forfeited	(7)	-
Released upon vesting	(821)	-
Outstanding, end of year <sup>(1)</sup>	3,729	3,116

(1) An incremental 1.1 million PSUs are expected to be settled in cash, pursuant to an estimated performance multiplier, for PSUs vesting in the year ended December 31, 2026.

### **RSUs (Cash-Settled)**

During the year ended December 31, 2023, the Board of Directors approved the cash settlement of RSUs.

The following table summarizes the changes in the RSU liability for the years:

	December 31, 2025	December 31, 2024
	\$	\$
Balance, beginning of year	1,850	1,188
Increase in liability/fair value adjustment <sup>(1)</sup>	2,352	1,718
Payout <sup>(1)</sup>	(1,459)	(1,056)
Balance, end of year	2,743	1,850
Current portion of stock-based compensation payable	1,918	1,237
Long-term portion of stock-based compensation payable	825	613

(1) Includes dividend adjustment.

The RSU liability as at December 31, 2025 of \$2.7 million is based on a fair value of \$9.37 per RSU which is the Company's closing share price on December 31, 2025.

The following table summarizes the changes in the number of outstanding RSUs for the years:

	December 31, 2025	December 31, 2024
Outstanding, beginning of year	432	377
Granted	253	207
Forfeited	(37)	(14)
Released upon vesting	(205)	(138)
Outstanding, end of year	443	432

c) Deferred share units

The Company has a DSU plan (the “DSU Plan”) which provides for grants of DSUs to non-management directors. Each DSU vests on the date of grant; however, settlement of the DSU occurs when the individual ceases to be a director of the Company. DSUs are to be settled in cash or by payment in common shares acquired through the facilities of the TSX. It is the intention of the Company to settle DSUs in cash.

The following table summarizes the changes in the DSU liability for the years:

	December 31, 2025	December 31, 2024
	\$	\$
DSUs, beginning of year	2,879	1,741
Increase in liability/fair value adjustment <sup>(1)</sup>	2,563	1,138
Payout <sup>(1)</sup>	(1,094)	-
DSUs, end of year	4,348	2,879
Current portion of stock-based compensation payable	4,348	2,879

(1) Includes dividend adjustment.

The DSU liability as at December 31, 2025, of \$4.3 million is based on a fair value of \$9.37 per DSU, which is the Company’s closing share price on December 31, 2025.

The following table summarizes the changes in the number of outstanding DSUs for the years:

	December 31, 2025	December 31, 2024
Outstanding, beginning of year	400	264
Granted	161	136
Released	(152)	-
Outstanding, end of year	409	400

d) Stock options

The Company has an old and new stock option plan (the “Option Plans”) under which options to purchase common shares of the Company may be granted to directors, officers, employees and consultants of the Company. The exercise price of each option granted is based on the closing price of the common shares on the TSX on the trading day prior to the date the option was granted. Options granted generally vest as to one third of the number granted on each of the first, second and third anniversaries of the date of grant over a three-year period and expire four to five years after the grant date. The Company does not intend to grant any further options under the Option Plans.

The following table summarizes the changes in stock options outstanding during the years:

	December 31, 2025		December 31, 2024	
	Number of options	Weighted average exercise price	Number of options	Weighted average exercise price
Options outstanding, beginning of year	177	\$ 4.56	2,508	\$ 3.88
Exercised <sup>(1)</sup>	(177)	\$ 4.56	(2,331)	\$ 3.82
Options outstanding, end of year	-	-	177	\$ 4.56
Options exercisable, end of year	-	-	177	\$ 4.56

(1) The Company's weighted average share price, at the date of exercise, for stock options exercised during the year ended December 31, 2025 was \$6.53 per common share (year ended December 31, 2024 - \$7.27 per common share).

There were no options granted in the years ended December 31, 2025 or 2024.

## 11. INCOME TAXES

The following table reconciles income taxes calculated at the weighted average Canadian statutory rate with the actual provision for deferred income taxes per the Statement of Income and Comprehensive Income:

	December 31, 2025	December 31, 2024
	\$	\$
Net income before income taxes	202,026	245,489
Blended Canadian statutory tax rate	23.16%	23.16%
Expected income tax expense	46,789	56,855
Increase (decrease) resulting from:		
Non-deductible expenses	214	264
Change in tax rates	(4)	(10)
Other	1,820	352
Total income tax expense	48,819	57,461
Current income tax expense	40,220	51,962
Deferred income tax expense	8,599	5,499

The Canadian statutory tax rate per the rate reconciliation above represents the weighted average combined federal and provincial corporate tax rate. The federal corporate tax rate is 15.0% and the annual average provincial tax rate in Alberta and New Brunswick is 8.0% and 14.0%, respectively.

The deferred income tax liability is comprised of the following as at December 31, 2025 and December 31, 2024:

	December 31, 2024	Movement through Statement of Income and Comprehensive Income	Movement through Shareholders' Equity	December 31, 2025
Deferred income tax liability	\$	\$	\$	\$
Current assets	20	(1)	-	19
Lease liability	41	41	-	82
E&E/PP&E/decommissioning liability	(60,476)	(13,034)	-	(73,510)
Net financial derivative liability	33	160	-	193
Share issue costs	-	(1)	7	6
Tax asset related to share awards	5,022	4,236	-	9,258
	(55,360)	(8,599)	7	(63,952)

	December 31, 2023	Movement through Statement of Income and Comprehensive Income	Movement through Shareholders' Equity	December 31, 2024
Deferred income tax liability				
	\$	\$	\$	\$
Current assets	24	(4)	-	20
Lease liability	16	25	-	41
E&E/PP&E/decommissioning liability	(51,073)	(9,403)	-	(60,476)
Net financial derivative liability	(852)	885	-	33
Share issue costs/transaction costs	249	(249)	-	-
Tax asset related to share awards	1,775	3,247	-	5,022
	(49,861)	(5,499)	-	(55,360)

The amount and timing of reversals of temporary differences will be dependent on a number of factors, including the nature and timing of future capital expenditures and the Company's future operating results.

## 12. SALES

The following table presents the Company's sales disaggregated by revenue source:

	December 31, 2025	December 31, 2024
	\$	\$
Heavy oil	585,695	604,153
Natural gas	26,881	12,285
Natural gas liquids ("NGLs")	4,174	1,959
Gathering, processing and transportation	1,530	1,407
	618,280	619,804

Primarily all of the Company's heavy oil, natural gas and NGL revenues for the years ended December 31, 2025 and December 31, 2024 are derived from variable priced contracts based on index prices.

Included in accounts receivable as at December 31, 2025 was \$52.2 million (December 31, 2024 - \$56.1 million) of accrued heavy oil, natural gas and NGLs sales related to December 2025 production.

## 13. INTEREST INCOME AND OTHER EXPENSE

Interest income and other expense consists of the following:

	December 31, 2025	December 31, 2024
	\$	\$
Interest income	3,596	5,705
Foreign exchange gains	10	36
Accretion on decommissioning liability (note 7)	(1,687)	(1,445)
Interest on repayable contribution (note 8)	(886)	(884)
Interest on lease liability	(196)	(106)
	837	3,306

- (1) Included within non-cash finance charges in the statement of cash flows are unrealized foreign exchange gains (losses), accretion on decommissioning liability, interest on repayable contribution and interest on lease liability.

#### 14. EXPENSES BY NATURE

In the Company's Statement of Income and Comprehensive Income, items are primarily disclosed by nature except for employee compensation which is included in production expense, general and administrative expenses and stock-based compensation expense as follows:

	December 31, 2025	December 31, 2024
	\$	\$
Production	555	475
General and administrative	9,664	7,490
Stock-based compensation	26,011	12,004
	36,230	19,969

#### 15. SUPPLEMENTAL CASH FLOW INFORMATION

	December 31, 2025	December 31, 2024
	\$	\$
Change in non-cash operating working capital:		
Accounts receivable	4,470	(14,146)
Inventories	115	(405)
Prepays and deposits	139	(240)
Accounts payable and accrued liabilities	(4,394)	3,751
Settlement of stock-based compensation	(13,535)	(1,056)
	(13,205)	(12,096)
Change in non-cash investing working capital:		
Accounts receivable	1,160	2,280
Accounts payable and accrued liabilities	(757)	(6,620)
	403	(4,340)
Cash income taxes paid	54,103	59,686
Cash standby and debt fees paid	305	280
Cash interest received	4,093	6,140

#### 16. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT

Financial instruments of the Company include cash and cash equivalents, restricted cash, accounts receivable, financial derivative receivable/liability, deposits, accounts payable and accrued liabilities, dividends payable and repayable contribution. The Company is exposed to financial risks arising from its financial assets and liabilities that include credit risk and liquidity risk in addition to the market risks associated with commodity prices and foreign exchange rates.

a) Risk management

i) Commodity price risk

Headwater enters into financial derivative commodity contracts to manage the risks associated with fluctuations in commodity prices. All such transactions are conducted in accordance with the Company's established risk management policies. The Company does not use derivative financial instruments for speculative purposes.

The Company had the following outstanding financial derivative commodity contracts as at December 31, 2025:

Commodity	Index	Type	Term	Daily Volume	Contract Price
Natural Gas	AGT <sup>(1)</sup>	Fixed	Jan 2026	7,000 mmbtu	Cdn\$15.23/mmbtu
Natural Gas	AGT	Fixed	Feb 2026	6,000 mmbtu	Cdn\$14.99/mmbtu
Natural Gas	AGT	Fixed	Mar 2026	4,500 mmbtu	Cdn\$13.91/mmbtu
Natural Gas	AGT	Fixed	Apr 2026	5,000 mmbtu	Cdn\$5.31/mmbtu
Crude Oil	WCS Basis <sup>(2)</sup>	Differential	Jan 2026 - Dec 2026	2,000 bbl	US\$13.00/bbl
Natural Gas	AECO 5A	Fixed	Apr 2026 - Oct 2026	2,000 GJ	Cdn\$2.93/GJ

(1) AGT = Algonquin city-gates daily

(2) WCS = Western Canadian Select

The following financial derivatives gains (losses) are reflected in the Statement of Income and Comprehensive Income:

	December 31, 2025	December 31, 2024
	\$	\$
Financial derivatives gains (losses):		
- realized gains (losses)	(6,506)	4,982
- unrealized losses	(691)	(3,803)
<b>Financial derivatives gains (losses)</b>	<b>(7,197)</b>	<b>1,179</b>

The following table summarizes the fair value of the Company's financial derivative contracts as at December 31, 2025 and the change in fair value for the year:

	Commodity contracts	Foreign exchange contracts	Total
	\$	\$	\$
Net financial derivative asset, December 31, 2023	3,662	17	3,679
Unrealized change in fair value <sup>(1)</sup>	(3,803)	(17)	(3,820)
Net financial derivative liability, December 31, 2024	(141)	-	(141)
Unrealized change in fair value	(691)	-	(691)
<b>Net financial derivative liability, December 31, 2025</b>	<b>(832)</b>	<b>-</b>	<b>(832)</b>

(1) Unrealized change in fair value related to the Company's foreign exchange contracts is included in interest income and other expense.

For the Company's commodity contracts, the fair value of the net financial derivative liability of \$832 thousand as at December 31, 2025, is based on estimated future crude oil and natural gas prices as of that date. The fair values of these financial derivative commodity contracts are sensitive to changes in the crude oil and natural gas reference prices. Holding other assumptions constant, if the AECO 5A and AGT price increased by 10% and the WCS differential to WTI decreased by 10%, the fair value of the financial derivative liability would increase (decrease) by \$2.4 million.

Financial derivative receivables and liabilities are only offset if Headwater has the current legal right to offset and intends to settle on a net basis. The Company offsets when the counterparty, commodity, currency and timing of settlement are the same.

## ii) Foreign currency risk

As of April 1, 2024, all of Headwater's revenue contracts are settled in Canadian dollars. However, the Company is exposed to fluctuations in the Canadian to U.S. dollar exchange rate given realized pricing is directly influenced by U.S. dollar denominated benchmark pricing and from exposure to its U.S. dollar denominated WCS commodity contracts. Headwater may decide to mitigate a portion of this risk by periodically entering into foreign exchange contracts. As at December 31, 2025, Headwater did not have any foreign exchange contracts outstanding.

### ***Fair Value Measurement***

The Company classifies fair value measurements using a fair value hierarchy that reflects the significance of the inputs used in making the measurements. The Company maximizes the use of observable inputs when preparing calculations of fair value, where possible. The fair value hierarchy has the following levels:

- Level 1 – Values are used based on unadjusted quoted prices available in active markets for identical assets and liabilities as of the reporting date.
- Level 2 – Values are based on inputs, including forward prices for commodities, time value and volatility factors, which can be substantially observed or corroborated in the marketplace. Prices in Level 2 are either directly or indirectly observable as of the reporting date.
- Level 3 – Values are based on prices or valuation techniques that are not based on observable market data.

The fair value of cash and cash equivalents, restricted cash, accounts receivable, deposits, accounts payable and accrued liabilities and dividends payable approximate their carrying value due to the short term to maturity of these instruments. The carrying amount of the repayable contribution was discounted at an estimated market rate upon its initial recognition. The carrying value at December 31, 2025 and 2024 approximates the fair value.

The Company's financial derivative receivable/liability is considered Level 2 in the fair value hierarchy.

## iii) Credit risk

As at December 31, 2025, the carrying amount of cash and cash equivalents, restricted cash, accounts receivable, financial derivative receivable and deposits represent the Company's maximum credit exposure. The Company's cash and cash equivalents are held on deposit with Canadian chartered banks. The Company's financial derivative receivable is outstanding from Canadian chartered banks.

Headwater's receivables from its crude oil and natural gas sales are subject to normal credit risk. During the year ended December 31, 2025, four counterparties (2024 – four counterparties) made up the majority of the Company's sales. Headwater mitigates the risk of loss by ensuring its counterparties are credit-worthy or investment grade as ranked by reputable credit agencies, or by periodically entering into parental guarantees. Headwater historically has not experienced any collection issues. Payment of crude oil and natural gas sales occurs on the 25<sup>th</sup> day following the month of sale. As a result, the majority of the Company's receivables have been collected subsequent to December 31, 2025.

Headwater's receivables from its joint venture partners are also subject to normal credit risk. Headwater's joint venture partners are highly credit-worthy or investment grade.

At December 31, 2025 and December 31, 2024, the average expected credit loss on the Company's accounts receivable was \$nil. Trade receivables generally have a 30-day term and the majority have been collected subsequent to year-end. As at December 31, 2025, the Company's receivables consisted of \$52.2 million (December 31, 2024 - \$56.1 million) from crude oil and natural gas marketers, \$nil (December 31, 2024 - \$0.1 million) from commodity contract counterparties, \$0.8 million (December 31, 2024 - \$1.9 million) from its joint venture partners and \$nil (December 31, 2024 - \$0.5 million) related to accrued interest and other.

#### iv) Liquidity risk

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they become due. The Company manages liquidity risk through its working capital and an actively managed operating and capital expenditure budgeting process. The Company entered into a \$100.0 million credit facility in the fourth quarter of 2022 and increased the associated borrowing base from \$100.0 million to \$200.0 million in the second quarter of 2024, to add further liquidity. As at December 31, 2025, the Company was holding cash of \$99.7 million.

#### **Credit Facilities**

The Company has a senior secured revolving syndicated credit facility with the National Bank of Canada and the Bank of Montreal (“the Lenders”). The credit facility is comprised of extendible revolving credit facilities consisting of a \$20.0 million operating facility and an \$80.0 million syndicated facility. Headwater also has an uncommitted accordion feature that provides the Company with the ability to access an incremental \$100.0 million, subject to certain conditions including approval from the Lenders.

As at December 31, 2025, Headwater had not drawn on the credit facility.

The credit facilities have a revolving period of 364 days, extendible annually at the request of the Company, subject to approval of the Lenders. If not extended, the credit facilities will automatically convert to a term loan and all outstanding obligations will be repayable one year after the expiry of the revolving period. The borrowing base is subject to semi-annual redeterminations occurring by May 31st and by November 30th of each year. The credit facilities are secured by a demand debenture in the amount of \$500 million. Repayments of principal are not required until the maturity date, provided that the borrowings do not exceed the authorized borrowing base and the Company is in compliance with all covenants, representations and warranties.

The credit facility bears interest at a floating market rate with margins charged by the Lenders linked to the Company’s senior debt to EBITDA ratio. EBITDA, for the purposes of calculating the senior debt to EBITDA ratio, is calculated as net income adjusted for non-cash items, interest expense and income taxes. Senior debt, for the purposes of calculating the senior debt to EBITDA ratio, is calculated as any debt of the Company excluding the financial derivative liability and repayable contribution.

The credit facility is not subject to any financial covenants. Additionally, distributions are permitted subject to compliance with a Board of Directors approved distributions policy.

#### b) Management of capital

The Company’s objectives when managing capital are to i) deploy capital to provide an appropriate return on investment to its shareholders; ii) maintain financial flexibility in order to preserve the Company’s ability to meet financial obligations; and iii) maintain a capital structure that provides financial flexibility to execute strategic acquisitions. To aid in managing the capital structure, the Company monitors adjusted working capital and adjusted funds flow from operations.

During the year ended December 31, 2025, the Company declared \$104.7 million related to its quarterly cash dividend (year ended December 31, 2024 – \$95.0 million). The Company increased its quarterly cash dividend to \$0.11 per common share, from \$0.10 per common share, effective for the dividend paid on April 15, 2025 to shareholders of record at the close of business on March 31, 2025. Included in current liabilities is \$26.2 million for the dividend declared on October 29, 2025, and paid out on January 15, 2026.

On May 1, 2025, Headwater announced TSX approval of Headwater’s NCIB to purchase for cancellation up to 19,020,755 common shares during the period commencing on May 6, 2025.

The Company’s strategy is designed to maintain a flexible capital structure consistent with the objectives as stated above and to respond to changes in economic conditions and the risk characteristics of the underlying crude oil and natural gas assets. Key indicators of changing economic conditions include adjusted working capital and adjusted funds flow from operations. Headwater considers its capital structure to include shareholders’ equity and working capital. In order to maintain or adjust its capital structure, the Company may from time to time issue new

common shares, seek debt financing, change its future return of capital policy and adjust its capital spending to manage working capital.

In order to facilitate the management of its capital expenditures and working capital, the Company prepares annual budgets which are updated quarterly depending upon varying factors including current and forecast crude oil and natural gas prices, capital expenditures and general industry conditions. The annual and updated budgets are approved by the Board of Directors.

i) Adjusted working capital

Management considers adjusted working capital to be a key measure to assess the Company's liquidity and capital management.

	December 31, 2025	December 31, 2024
	\$	\$
Working capital	29,951	78,735
Repayable contribution	(7,202)	(10,916)
Financial derivative receivable	(393)	(3,088)
Financial derivative liability	1,225	2,847
Adjusted working capital	23,581	67,578

ii) Adjusted funds flow from operations

Management considers adjusted funds flow from operations to be a key measure to assess the Company's management of capital. Adjusted funds flow from operations is an indicator as to whether adjustments are necessary to the level of capital expenditures. For example, in periods where adjusted funds flow from operations is negatively impacted by reduced commodity pricing, capital expenditures may need to be reduced or curtailed to preserve the Company's capital structure and return of capital policy. Management believes that by excluding the impact of changes in non-cash working capital and restricted cash and adjusting for current income taxes in the period, adjusted funds flow from operations provides a useful measure of Headwater's ability to generate the funds necessary to manage the capital needs of the Company. In addition to being a capital management measure, adjusted funds flow from operations is used by management to assess the Company's financial performance.

	December 31, 2025	December 31, 2024
	\$	\$
Cash flows provided by operating activities	297,137	316,737
Changes in non-cash working capital	13,205	12,096
Current income taxes	(40,220)	(51,962)
Income taxes paid	54,103	59,686
Restricted cash	2,000	-
Adjusted funds flow from operations	326,225	336,557

Adjusted working capital and adjusted funds flow from operations are not standardized measures and, therefore, may not be comparable with the calculation of similar measures of other entities.

## 17. RELATED PARTY TRANSACTIONS

The following table presents the remuneration accrued to key management personnel and the Board of Directors through the years:

	December 31, 2025	December 31, 2024
	\$	\$
Wages and benefits	6,967	4,472
Directors' compensation	228	205
Stock-based compensation	26,947	11,586
	34,142	16,263

Wages and benefits to key management personnel include salary, bonus and benefits accrued during the year. Directors' compensation includes cash compensation accrued during the year to directors who elected to receive their annual retainer in the form of cash compensation. Stock-based compensation includes non-cash expenses, including amounts capitalized to PP&E, accrued under the Company's DSU Plan and Awards Plan for both key management personnel and directors of the Company.

## 18. COMMITMENTS

As at March 5, 2026, the Company is committed to future payments under the following agreements:

	Total	2026	2027	2028	2029	2030	Thereafter
	\$	\$	\$	\$	\$	\$	\$
Transportation and operating Lease <sup>(1)</sup>	234,283	30,693	32,389	32,748	31,598	23,673	83,182
Repayable contribution <sup>(2)</sup>	1,641	448	455	463	275	-	-
	12,751	4,675	8,076	-	-	-	-

(1) Relates to variable operating costs, which are a non-lease component of the Company's head office lease.

(2) Relates to scheduled undiscounted re-payments of federal government funding under the terms of the repayable contribution agreement with NRCan. See note 8.

(3) Excludes leases accounted for under IFRS 16.

### a) Letter of credit and restricted cash

As at December 31, 2025, the Company had a standby letter of credit issued by a Canadian chartered bank in the amount of \$350 thousand (2024 – \$350 thousand) relating to a transportation arrangement. The standby letter of credit is supported by cash and is recorded in restricted cash in the Statement of Financial Position. As at December 31, 2025, the Company held restricted cash with in a Canadian chartered bank in the amount of \$2.0 million (2024 – \$nil) relating to collateral for certain financial derivative commodity contracts with a counterparty.

## 19. SUBSEQUENT EVENTS

### a) Dividend

On March 5, 2026, the Company declared a cash dividend of \$0.11 per common share. The dividend will be paid on April 15, 2026, to shareholders of record at the close of business on March 31, 2026.

### b) Financial derivative commodity contracts:

Subsequent to December 31, 2025, Headwater entered into the following commodity contracts:

Commodity	Index	Type	Term	Daily Volume	Contract Price
Natural Gas	AECO 5A	Fixed	Apr 2026 – Oct 2026	1,000 GJ	Cdn\$2.26/GJ
Natural Gas	AGT	Fixed	Dec 2026 – Mar 2027	2,500 mmbtu	Cdn\$15.75/mmbtu
Crude Oil	WTI	Fixed	Mar 2026 - Dec 2026	2,500 bbl	Cdn\$95.03/bbl