



Prairie Provident Resources Inc.

Consolidated Financial Statements

As at and for the Year Ended December 31,
2017

Dated: March 28, 2018

INDEPENDENT AUDITORS' REPORT

To the Shareholders of Prairie Provident Resources Inc.

We have audited the accompanying consolidated financial statements of Prairie Provident Resources Inc., which comprise the consolidated statements of financial position as at December 31, 2017 and 2016, and the consolidated statements of loss and comprehensive loss, changes in equity, and cash flows for the years then ended, and a summary of significant accounting policies and other explanatory information.

Management's responsibility for the consolidated financial statements

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

Auditors' responsibility

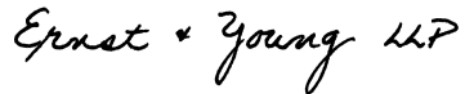
Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditors consider internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements 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. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

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

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of Prairie Provident Resources Inc. at December 31, 2017 and 2016, and its financial performance and its cash flows for the years then ended in accordance with International Financial Reporting Standards.



Calgary, Canada
March 28, 2018

Chartered Professional Accountants

CONSOLIDATED STATEMENTS OF FINANCIAL POSITION

As at (\$000s)	Note	December 31, 2017	December 31, 2016
ASSETS			
Cash and cash equivalents	18	3,564	7,926
Restricted cash	8, 18	4,881	—
Accounts receivable	18	8,654	8,535
Inventory		697	521
Prepaid expenses and other assets		897	557
Derivative instruments – current	18	895	—
Total current assets		19,588	17,539
Exploration and evaluation	6	26,420	26,437
Property and equipment	7	217,035	203,381
Derivative instruments	18	192	—
Other assets		272	478
Total assets		263,507	247,835
LIABILITIES			
Accounts payable and accrued liabilities	18	20,894	21,919
Flow-through share premium		711	390
Derivative instruments	18	4,156	2,311
Current portion of decommissioning liability	10	2,300	3,500
Warrant liability	9	533	—
Total current liabilities		28,594	28,120
Long-term debt	8	55,760	15,047
Derivative instruments	18	2,258	3,800
Decommissioning liabilities	10	110,534	94,220
Other liabilities		4,193	4,062
Total liabilities		201,339	145,249
Commitments and contingencies	20		
SHAREHOLDERS' EQUITY			
Share capital	11	121,546	115,062
Warrants		337	—
Contributed surplus		928	514
Accumulated deficit		(61,068)	(13,266)
Accumulated other comprehensive income (“AOCI”)		425	276
Total equity		62,168	102,586
Total liabilities and shareholders' equity		263,507	247,835

See accompanying notes to the consolidated financial statements.

Approved by the Board of Directors,

(signed)
Patrick McDonald
 Chair of the Board of Directors and Director

(signed)
Ajay Sabherwal
 Chair of the Audit Committee and Director

CONSOLIDATED STATEMENTS OF LOSS AND COMPREHENSIVE LOSS

For the years ended

(\$000s)	Note	December 31, 2017	December 31, 2016
REVENUE			
Oil and natural gas revenue		79,011	42,748
Royalties		(10,373)	(4,893)
Oil and natural gas revenue, net of royalties		68,638	37,855
Unrealized gain (loss) on derivative instruments	18	783	(19,274)
Realized gain on derivative instruments	18	4,926	9,743
		74,347	28,324
EXPENSES			
Operating	15	38,650	23,417
General and administrative	16	10,218	10,830
Depletion and depreciation	7	34,875	21,344
Exploration and evaluation	6	4,877	58
(Gain) loss on sale of properties	5	(853)	73
Gain on business combination	4	(3,893)	—
Impairment loss	6, 7	34,177	26,723
Gain on foreign exchange		(1,621)	(9,510)
Finance costs	17	5,114	13,119
Reorganization		—	392
Transaction costs	4	1,075	2,288
Total expenses		122,619	88,734
Net loss before taxes		(48,272)	(60,410)
Current taxes	13	7	(14)
Deferred tax recovery	13	(477)	—
Net tax recovery		(470)	(14)
Net loss		(47,802)	(60,396)
Other comprehensive income			
Items that will not be reclassified to net loss:			
Actuarial gain on employee post-retirement benefit plan	3(j)	149	276
Comprehensive loss		(47,653)	(60,120)
Net loss per share – basic & diluted			
	11	(0.42)	(0.62)

See accompanying notes to the consolidated financial statements.

CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY

(\$000s)	Note	Share Capital	Warrants	Contributed Surplus	Accumulated Deficit	AOCI	Total Equity
Balance at January 1, 2017		115,062	—	514	(13,266)	276	102,586
Issuance of common share	11	7,204	337	—	—	—	7,541
Share issuance costs	11	(1,065)	—	—	—	—	(1,065)
Share-based compensation	12	—	—	803	—	—	803
Settlement of restricted share units	11	389	—	(389)	—	—	—
Withholding taxes on settlement of restricted share units	11	(44)	—	—	—	—	(44)
Actuarial gain on post- retirement benefit plan		—	—	—	—	149	149
Net loss		—	—	—	(47,802)	—	(47,802)
Balance at December 31, 2017		121,546	337	928	(61,068)	425	62,168

(\$000s)	Note	Share Capital	Contributed Surplus	Accumulated Deficit	AOCI	Total Equity
Balance at January 1, 2016		73,912	1,024,623	(1,172,884)	287	(74,062)
Issued for the Business Combination	11	38,735	—	—	—	38,735
Issued in exchange of the Preferred Shares	11	193,851	—	—	—	193,851
Issuance of common shares for cash	11	4,556	—	—	—	4,556
Share issuance costs	11	(519)	—	—	—	(519)
Share-based compensation		—	430	—	—	430
Settlement of restricted share units		3,382	(3,382)	—	—	—
Withholding taxes on settlement of restricted share units		(285)	—	—	—	(285)
Actuarial gain on post- retirement benefit plan		—	—	—	276	276
Net loss		—	—	(60,396)	—	(60,396)
Reduction of share capital		(198,570)	(1,021,157)	1,220,014	(287)	—
Balance at December 31, 2016		115,062	514	(13,266)	276	102,586

See accompanying notes to the consolidated financial statements.

CONSOLIDATED STATEMENTS OF CASH FLOWS

For the years ended (\$000s)	Note	December 31, 2017	December 31, 2016
OPERATING ACTIVITIES			
Net loss		(47,802)	(60,396)
Adjustments for non-cash items:			
Impairment loss	6, 7	34,177	26,723
Unrealized (gain) loss on derivative instruments	18	(783)	19,274
Depletion and depreciation	7	34,875	21,344
Exploration and evaluation	6	4,877	58
Accretion and financing charges		2,146	12,389
Unrealized gain on foreign exchange		(1,519)	(9,613)
(Gain) loss on sale of property and equipment		(853)	73
Gain on business combination		(3,893)	—
Gain on warrant liability		(46)	—
Deferred tax expense		(477)	—
Share-based compensation	12	687	395
Amortization of deferred cost		611	332
Settlement of decommissioning liabilities	10	(5,136)	(4,540)
Other, net		258	(433)
Change in non-cash working capital	14	(501)	2,539
Net cash from operating activities		16,621	8,145
FINANCING ACTIVITIES			
Debt issuance costs		(3,179)	(190)
Issuance of common shares	11	8,340	4,945
Share issuance costs	11	(1,065)	(519)
Withholding taxes on settlement of restricted share units	11	(44)	(285)
Change in Senior Note borrowings		20,629	—
Change in Revolving Facility borrowings		39,963	—
Change in Amended Credit Facility borrowings		(15,500)	15,458
Net cash from financing activities		49,144	19,409
INVESTING ACTIVITIES			
Exploration and evaluation expenditures	6	(13,385)	(28,741)
Property and equipment expenditures	7	(10,191)	(6,122)
Acquisitions – business combination		(40,894)	—
Cash acquired on business combination	1, 4	—	249
Asset dispositions (net of acquisitions)		383	20
Change in non-cash working capital	14	(1,159)	1,945
Net cash used in investing activities		(65,246)	(32,649)
Change in cash and restricted cash		519	(5,095)
Cash and restricted cash beginning of year		7,926	13,021
Cash and cash equivalents end of year		8,445	7,926

See accompanying notes to the consolidated financial statements.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the years ended December 31, 2017 and 2016

1. REPORTING ENTITY

Prairie Provident Resources Inc. (“PPR” or the “Company”) was incorporated under the laws of the province of Alberta on July 29, 2016. Its principal office is located at 640 – 5th Avenue S.W., Calgary, Alberta. The Company’s common shares are listed on the Toronto Stock Exchange under the symbol “PPR”.

PPR is an independent oil and natural gas exploration, development and production company. PPR’s reserves, producing properties and exploration prospects are located primarily in the provinces of Alberta, British Columbia and Quebec, and in the Northwest Territories. The Company conducts certain of its operating activities jointly with others through unincorporated joint arrangements and these consolidated annual financial statements reflect only the Company’s share of assets, liabilities, revenues and expenses under these arrangements. The Company conducts all of its principal business in one reportable segment.

On September 12, 2016, Lone Pine Resources Canada Ltd. (“LPR Canada”), Lone Pine Resources Inc. (“Lone Pine Resources”, collectively with LPR Canada, “Lone Pine”) and Arsenal Energy Inc. (“Arsenal”) completed a business combination by way of a plan of arrangement (the “Arrangement” or the “Transaction”) whereby the Arrangement brought together Lone Pine and Arsenal under a new parent corporation, PPR, of which Lone Pine and Arsenal became direct or indirect wholly-owned subsidiaries (see Note 4(b)).

The acquisition of Arsenal was accounted for as a business combination using the acquisition method of accounting whereby PPR is deemed to be the acquirer of the Arsenal business and the assets and liabilities assumed were recorded at their fair values (Note 4(b)). Transaction costs associated with the acquisition were expensed when incurred.

2. BASIS OF PRESENTATION

(a) Statement of Compliance

These annual financial statements have been prepared in accordance with IFRS as issued by the International Accounting Standards Board (“IASB”). The annual financial statements were approved and authorized for issue by the Board of Directors of PPR on March 28, 2018 (the “Financial Statements”).

The Company’s significant accounting policies under IFRS are presented in Note 3.

(b) Basis of Measurement

The Financial Statements have been prepared on the historical cost basis except for derivative instruments and warrant liability that are measured at fair value.

(c) Functional and Presentation Currency

The Financial Statements are presented in Canadian dollars, which is also the Company’s functional currency. All references to US\$ are to United States dollars.

(d) Use of Estimates and Judgements

The preparation of financial statements in conformity with IFRS requires management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, revenues and expenses. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimates are revised and in any future periods affected.

Information about significant areas of estimation uncertainty and critical judgements in applying accounting policies that have the most significant effect on the amounts recognized in the Financial Statements are as follows:

- PPR's oil and gas assets are grouped into cash generating units ("CGUs"). A CGU is the lowest level of integrated assets that generate identifiable cash inflows that are largely independent of the cash inflows of other assets or groups of assets. The allocation of assets into CGUs requires significant judgement and interpretations with respect to the integration between assets, geological formation, geographical proximity, the existence of common sales points and shared infrastructures and the way in which management monitors its operations. The recoverability of PPR's oil and gas assets is assessed at the CGU level, and therefore, the determination of a CGU costs could have a significant impact on impairment losses or impairment reversals;
- Reserves engineering is an inherently complex and subjective process of estimating underground accumulations of petroleum and natural gas. The process relies on interpretations of available geological, geophysical, engineering, economic and production data. The accuracy of a reserves estimate is a function of the quality and quantity of available data, the interpretation of that data, the accuracy of various economic assumptions and the judgement of those preparing the estimate. Because these estimates depend on many assumptions, all of which may differ from actual results, reserves estimates and estimates of future net revenue may be different from the sales volumes ultimately recovered and net revenues actually realized. Changes in market conditions, regulatory matters and the results of subsequent drilling, testing and production may require revisions to the original estimates. Estimates of reserves impact: (i) the assessment of whether or not a new well has found economically recoverable reserves; (ii) depletion rates; (iii) the determination of net recoverable amount of oil and gas properties for impairment assessment and measurement, (iv) purchase price allocation for business combinations, and (v) the determination of reserve lives which affect the timing of decommissioning activities, all of which could have a material impact on earnings and financial positions;
- Recoverable amounts calculated for impairment testing are based on estimates of future commodity prices, expected volumes, quantity of reserves and discount rates as well as future development costs and operating costs. These calculations require the use of estimates and assumptions, which by their nature, are subject to measurement uncertainty. In addition, judgement is exercised by management as to whether there have been indicators of impairment or of impairment reversal. Indicators of impairment or impairment reversal may include, but are not limited to a change in: market value of assets, estimate of future prices and costs, a change in estimated quantity of reserves and appropriate discount rates;
- Business combinations are accounted for using the acquisition method of accounting where the acquired assets, liabilities and consideration issued were all fair valued. The determination of fair value requires the use of assumptions and estimates related to future events. The valuation of property and equipment includes key assumptions and estimates related to oil and gas reserves acquired, forecasted commodity prices, expected production volumes, future development costs,

operating costs and discount rates. The valuation of exploration and evaluation assets includes key assumptions and estimates related to recent transactions on similar assets considering geographic location and risk profile. The valuation of the decommissioning liabilities and other liabilities includes estimates related to the timing and amount of anticipated cash outflows as well as for inflation rates and discount rates. For the Arrangement, as PPR common shares were issued in exchange for AEI's common shares, PPR common shares were fair valued with reference to PPR's enterprise value, which in turn was determined by fair valuing PPR's underlying assets and liabilities. Key assumptions used to fair value PPR's assets and liabilities were similar to those mentioned above. In addition, PPR's enterprise value was calibrated against trading metrics of recent market transactions for reasonableness. Changes in assumptions and estimates used in the determination of assets and liabilities acquired and consideration issued could result in changes to the values assigned to the assets, liabilities and goodwill or a bargain purchase gain. This could in turn impact future earnings or loss as a result of changes in the realization of asset value or the settlement of liabilities;

- Amounts recorded for decommissioning liabilities and the related accretion expense require the use of estimates with respect to the amount and timing of decommissioning expenditures, inflation rates and discount rates. Actual costs and cash outflows can differ from estimates because of changes in law and regulations, public expectations, market conditions, discovery and analysis of site conditions and changes in technology. Decommissioning liabilities are recognized in the period when it becomes probable that there will be a future cash outflow;
- Compensation costs recorded pursuant to share-based compensation plans are subject to the estimated fair values of the awards on the grant date and the estimated number of units that will ultimately vest. The Company uses the Black-Scholes option pricing model to estimate the fair value of options, which requires the Company to determine the most appropriate inputs including the expected life of the options, volatility, forfeiture rates and future dividends, which by nature are subject to measurement uncertainty. The determination of the fair value of performance share units requires the estimation of the performance multiplier from 0 to 2 on the grant date;
- Derivative risk management contracts are valued using valuation techniques with market observable inputs. The most frequently applied valuation techniques include Black-Scholes option pricing model and forward pricing and swap models. The models incorporate various inputs including the credit quality of counterparties, foreign exchange spot and forward rates, volatilities of commodity prices and forward rate curves of the underlying commodity. Changes in any of these assumptions would impact fair value of the risk management contracts and as a result, future net income and other comprehensive income;
- Tax interpretations, regulations and legislation in the various jurisdictions in which the Company operates are subject to change. The Company is also subject to income tax audits and reassessments which may change its provision for income taxes. Therefore, the determination of income taxes is by nature complex, and requires making certain estimates and assumptions. PPR recognizes net deferred tax benefit related to deferred tax assets to the extent that it is probable that the deductible temporary differences will reverse in the foreseeable future. Assessing the recoverability of deferred tax assets requires the Company to make significant estimates related to expectations of future taxable income. Estimates of future taxable income are based on forecast cash flows from operations and the application of existing tax laws in each jurisdiction. To the extent that future cash flows and taxable income differ significantly from estimates, the ability of the Company to realize the net deferred tax assets recorded at the reporting date could be impacted;
- The determination of fair value requires judgement and is based on market information, where available and appropriate. Fair value is best evidenced by an independent quoted market price for the same asset or liability in an active market. However, quoted market prices and active markets do not

always exist. In those instances, fair valuation techniques are used. The Company applies judgement in determining the most appropriate inputs and the weighting ascribed to each such input as well as its selection of valuation methodologies. The calculation of fair value is based on market conditions as at each reporting date, and may not be reflective of ultimate realizable value;

- Contingencies will only be resolved when one or more future events occur or fail to occur. The assessment of contingencies inherently involves the exercise of significant judgment and estimates of the outcome of future events; and
- Amounts recorded for capitalized general and administrative cost that is related to directly attributed supporting functions and activity to post license exploration and evaluation assets and to development and producing CGU properties requires the use of estimates and judgements and is by its nature subject to measurement uncertainty.

3. SIGNIFICANT ACCOUNTING POLICIES

The accounting policies set out below were applied consistently to all periods presented in these Financial Statements.

(a) Basis of Consolidation

At December 31, 2017, the Financial Statements included the accounts of PPR and its wholly owned subsidiaries, including Prairie Provident Resources Canada Ltd. ("PPR Canada"), Lone Pine Resources, Lone Pine Resources (Holdings) Inc., Arsenal, Arsenal Energy USA Inc. and Arsenal Energy Holdings Ltd. Subsidiaries are consolidated from the date the Company obtains control and continues to be consolidated until the date such control ceases. Control is achieved when PPR is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee. The financial statements of the subsidiaries are prepared for the same reporting period as the Company, using consistent accounting policies. All inter-entity transactions have been eliminated upon consolidation between PPR and its subsidiaries in these consolidated financial statements. PPR's operations are viewed as a single operating segment by the chief operating decision maker of the Company for the purpose of resource allocation and assessing performance.

Arsenal's operating results are included in these consolidated financial statements since September 12, 2016, the closing date of the Arrangement.

Historical financial information prior to the Arrangement represents the combined and consolidated results of Lone Pine. Lone Pine Resources and LPR Canada were controlled through direct and indirect ownership by a single majority investor and as such Lone Pine Resources and LPR Canada were under common control and therefore, are presented on a combined and consolidated basis for the periods prior to September 12, 2016 in these financial statements.

(b) Joint Arrangements

PPR conducts some of its oil and gas activities through joint operations. Joint operation is a type of joint arrangement over which two or more parties have joint control and rights to the assets and obligations for the liabilities, relating to the arrangement. Joint control is the contractually agreed sharing of control of an arrangement, which exists only when decisions about the relevant activities (being those that significantly affect the returns of the arrangement) require unanimous consent of the parties sharing control. PPR does not have any joint arrangements that are material to the Company, or that are structured using separate vehicles. In

relation to its interests in joint operations, PPR recognizes in the Financial Statements its share of assets, liabilities, revenues and expenses of the arrangements.

(c) Business Combinations

Business combinations are accounted for using the acquisition method of accounting. The fair value of the net assets acquired and the consideration transferred is measured at the acquisition date. Transaction costs related to business combinations are expensed when incurred.

If the fair value of the consideration exceeds the net identifiable assets acquired, it is recorded as goodwill. If the consideration is less than the fair value of the net identifiable assets acquired, the difference is recognized as a gain in the consolidated statement of income (loss).

(d) Revenue

Revenue from the sale of petroleum and natural gas is recognized when the risks and rewards of ownership have been substantially transferred and when the amount of revenue can be reliably measured. Royalty income is recognized as it accrues in accordance with the terms of the overriding royalty agreements.

(e) Exploration and Evaluation Assets and Property and Equipment

(i) Recognition and Measurement

Exploration and Evaluation (“E&E”) Assets

Pre-license costs are recognized in the consolidated statements of loss and comprehensive loss as incurred.

E&E costs, including the costs of acquiring licenses, obtaining geological and geophysical data, drilling and completing E&E wells, and building associated facilities are initially capitalized as E&E assets according to the nature of the expenditure. E&E assets may include estimated decommissioning costs associated with E&E decommissioning obligations. The costs are accumulated by well, field or exploration area pending determination of technical feasibility and commercial viability. E&E assets are not amortized.

The technical feasibility and commercial viability of extracting a hydrocarbon resource are considered to be determinable when proved and/or probable reserves are determined to exist. A review of each exploration license or field is carried out, at least annually, to ascertain whether proved and/or probable reserves have been discovered. Upon determination of proved and/or probable reserves, E&E assets attributable to those reserves are tested for impairment and if estimated recoverable amounts exceed carrying values the E&E assets, are transferred to petroleum and natural gas properties, within property and equipment assets. The cost of undeveloped land that expires and E&E expenditures determined to be unsuccessful are derecognized by recording exploration and evaluation expense.

Production and Development (“P&D”) Assets

P&D assets generally represent costs incurred in acquiring and developing proved and/or probable reserves, and bringing in or enhancing production from such reserves. Development costs include the initial purchase price and directly attributable costs relating to land and mineral leases, geological and seismic studies, property acquisitions, development drilling, construction of gathering systems and infrastructure facilities, decommissioning costs, transfers from E&E assets, and for qualifying assets, borrowing costs. These costs are accumulated on a field or an area basis (major components). The costs of the day-to-day servicing of property and equipment are recognized in operating expenses as incurred.

The production and development items of property and equipment, which includes oil and natural gas development, properties and production assets, are measured at cost less accumulated depletion and depreciation and accumulated impairment losses, net of impairment reversals. Development assets include certain stock equipment that is expected to be used in the normal course of P&D field development.

Gains and losses on disposal of an item of property and equipment, including petroleum and natural gas properties, are determined by comparing the net proceeds from disposal with the carrying amount of property and equipment and are recognized on a net basis on the consolidated statements of loss and comprehensive loss.

(ii) Depletion and Depreciation

The net carrying value of P&D assets is depleted using the unit-of-production method by reference to the ratio of production in the year to the related proved plus probable reserves, taking into account estimated future development costs necessary to convert those reserves into production. Future development costs are estimated taking into account the level of development required to produce the reserves. These estimates are prepared by independent reserve engineers at least annually.

Proved plus probable reserves are estimated annually by independent and qualified reserve evaluators and represent the estimated quantities of petroleum and natural gas which geological, geophysical and engineering data demonstrate with a specified degree of certainty to be recoverable in future years from known reservoirs and which are considered commercially producible.

Reserves are the remaining quantities of, petroleum and natural gas from known accumulations estimated to be recoverable from a given date forward. The estimates of reserves are determined from drilling, geological, geophysical and engineering data based on established technology and specified economic conditions. For depletion purposes, relative volumes of petroleum and natural gas production and reserves are converted at the energy equivalent conversion rate of six thousand cubic feet of natural gas to one barrel of crude oil.

For other assets, depreciation is recognized in profit or loss on a straight-line or declining-balance basis over the estimated useful life of each part of an item of property and equipment. Leasehold improvements are depreciated over the term of the lease. Leased assets are depreciated over the shorter of the lease term and their useful lives unless it is reasonably certain that the Company will obtain ownership by the end of the lease term.

Computer equipment is depreciated using the declining-balance basis at a rate of 30 percent per year. Office furniture is depreciated on a straight line basis over five years.

Depreciation methods, useful lives and residual values are reviewed at each reporting date.

(iii) Impairment

E&E Assets

E&E assets are assessed for impairment if: (i) sufficient data exists to determine technical feasibility and commercial viability; and (ii) at such time that facts and circumstances indicate that the carrying amount exceeds the recoverable amount. If the recoverable amount does not exceed the carrying amount, an impairment adjustment is recognized in net loss and comprehensive loss.

For the purposes of impairment testing, E&E assets are allocated to CGUs based on geographical proximity. E&E assets that are not related to established CGUs with reserves, such as undeveloped land holdings, seismic, equipment, and exploration drilling in Quebec, the Northwest Territories and other exploratory properties, are subject to impairment testing based on the nature and estimated recoverable amount of the respective cost components.

P&D Assets

PPR assesses, at each reporting date, whether there is an indication that an asset may be impaired. If any indication exists, the Company estimates the asset's recoverable amount. An asset's recoverable amount is the higher of an asset's fair value less cost of disposal ("FVLCD") and its value-in-use ("VIU"). The recoverable amount is determined for an individual asset, unless the asset does not generate cash inflows that are largely independent of those from other assets or groups of assets. In such case, an impairment test is performed at the CGU level. A CGU is a group of assets that PPR aggregates based on their ability to generate largely independent cash flows. As a result of the Arrangement (Note 1), the Company has reassessed its groupings of CGUs to incorporate the assets acquired. As a result, the Company added a new CGU, Princess. Other assets were grouped with previously existing CGUs considering the integration of assets, geological formation, geographical proximity, the existence of common sales points and shared processing facilities and the way in which management monitors its operations. As at December 31, 2017, the Company has five principal operating CGUs – Evi, Wheatland, Princess, Provost and Other.

Where the carrying amount of an asset or CGU exceeds its recoverable amount, the asset is considered impaired and is written down to its recoverable amount. To determine VIU, the Company estimates the present value of the future net cash flows expected to derive from the continued use of the asset or CGU. Discount rates that reflect the market assessments of the time value of money and the risks specific to the asset or CGU are used. In determining FVLCD, discounted cash flows and recent market transactions are taken into account, if available. These calculations are corroborated by valuation multiples or other available fair value indicators. For assets excluding goodwill, an assessment is made at each reporting date as to whether there is any indication that previously recognized impairment losses may no longer exist or may have decreased. If such indication exists, the previously recognized impairment loss is reversed. The reversal is limited such that the carrying amount of the asset does not exceed its recoverable amount, nor does it exceed the carrying amount that would have been determined, net of depreciation, had no impairment loss been recognized for the asset in prior periods.

(f) Financial Instruments

(i) Recognition and Measurement

PPR recognizes financial assets and financial liabilities, including derivatives, on the consolidated statements of financial position when the Company becomes a party to the contract. The Company initially measures all financial instruments at fair value. Subsequent measurement of the financial instrument is based on its classification. Financial assets are classified into the following categories: held for trading, available for sale, held-to-maturity investments and loans and receivables. Financial liabilities are classified as held for trading or other financial liabilities. PPR has not designated any financial asset or liability at fair value through profit or loss.

Financial assets and financial liabilities classified as held for trading are measured at fair value with changes in those fair values recognized in net income. Financial assets classified as either held-to-maturity or loans and receivables, and other financial liabilities are measured at amortized cost using the effective interest method of amortization. Under the effective interest rate method, any transaction fees, costs, discounts and premiums directly related to the financial instruments are recognized in comprehensive loss over the

expected life of the instrument. Financial assets classified as available-for-sale are measured at fair values with changes in those fair values recognized in other comprehensive loss.

(ii) Liabilities and Equity

Financial instruments are classified as a liability or equity based on the substance of the contractual arrangement. An instrument is classified as a liability if it is a contractual obligation to deliver cash or another financial asset, or to exchange financial assets or financial liabilities on potentially unfavorable terms. A contract is also classified as a liability if it is a non-derivative and could obligate the Company to deliver a variable number of its own shares or it is a derivative other than one that can be settled by the delivery of a fixed amount of cash or another financial asset for a fixed number of the Company's own equity instruments. An instrument is classified as equity if it evidences a residual interest in the Company's assets after deducting all liabilities.

(iii) Derivative Financial Instruments

As described in Note 18, derivative financial instruments are used by the Company to manage its exposure to market risks relating to commodity prices. The Company's policy is not to use derivative financial instruments for speculative purposes. The estimate of fair value of all derivative instruments is based on quoted market prices, or in their absence, third party market indications and forecasts and includes an estimate of the credit quality of counterparties to the derivative instruments. The estimated fair value of financial assets and liabilities is subject to measurement uncertainty.

The Company has not designated its financial derivative contracts as effective accounting hedges, and therefore has not applied hedge accounting, even though the Company considers all commodity contracts to be economic hedges. As a result, all financial derivative contracts are measured at fair value, with any gains and losses recorded in the statement of loss and comprehensive loss.

(iv) Derecognition of Financial Instruments

A financial liability is derecognized when the obligation under the liability is discharged, cancelled or expires. The difference between the carrying value of the liability and the ultimate consideration paid is recognized in the consolidated statement of loss and comprehensive loss. If equity instruments are issued to extinguish a financial liability, the equity instruments are treated as consideration paid and measured at their fair value at the date of extinguishment.

A financial asset is derecognized when (1) the rights to receive cash flows from the assets have expired or (2) the Company has transferred its rights to receive cash flows from the assets or has assumed an obligation to pay the received cash flows in full without material delay to a third party under a 'pass-through' arrangement; and either (a) the Company has transferred substantially all the risks and rewards of the assets, or (b) the Company has neither transferred nor retained substantially all the risks and rewards of the assets, but has transferred control of the asset.

(v) Impairment

A financial asset is assessed at each reporting date to determine whether there is objective evidence that it is impaired. A financial asset is considered impaired if objective evidence indicates that one or more events have had a negative effect on the estimated future cash flows of that asset. All impairment losses are recognized in profit or loss.

An impairment loss in respect of a financial asset measured at amortized cost is calculated as the difference between its carrying amount and the present value of the estimated future cash flows discounted at the original effective interest rate.

Individually significant financial assets are assessed for impairment on an individual basis. The remaining financial assets are assessed collectively in groups that have similar credit risk characteristics.

An impairment loss is reversed if the reversal can be related objectively to an event following recognition. For financial assets measured at amortized cost, the reversal is recognized in profit or loss.

(vi) Offsetting

Financial assets and liabilities are offset and the net amount reported in the statement of financial position when there is a legally enforceable right to offset the recognized amounts and there is an intention to settle on a net basis or realize the asset and settle the liability simultaneously.

(g) Fair Value Measurement

PPR measures derivatives at fair value at each balance sheet date and, for the purposes of impairment testing, uses FVLCD to determine the recoverable amount of some of its non-financial assets. Also, fair values of financial instruments measured at amortized cost are disclosed in Note 18. Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The fair value measurement is based on the presumption that the transaction to sell the asset or transfer the liability takes place either in the following markets that are accessible by the Company:

- the principal market for the asset or liability, or
- in the absence of a principal market, the most advantageous market for the asset or liability.

The fair value of an asset or a liability is measured using the assumptions that market participants would use when pricing the asset or liability, assuming that market participants act in their economic best interest. A fair value measurement of a non-financial asset takes into account a market participant's ability to generate economic benefits by using the asset in its highest and best use or by selling it to another market participant that would use the asset in its highest and best use. PPR uses valuation techniques that are appropriate in the circumstances and for which sufficient data are available to measure fair value, maximizing the use of relevant observable inputs and minimizing the use of unobservable inputs. All assets and liabilities for which fair value is measured or disclosed in the Financial Statements are categorized within the fair value hierarchy; described as follows, based on the lowest-level input that is significant to the fair value measurement as a whole:

- Level 1 — Quoted (unadjusted) market prices in active markets for identical assets or liabilities;
- Level 2 — Valuation techniques for which the lowest-level input that is significant to the fair value measurement is directly or indirectly observable; and
- Level 3 — Valuation techniques for which the lowest-level input that is significant to the fair value measurement is unobservable.

For assets and liabilities that are recognized in the financial statements on a recurring basis, PPR determines whether transfers have occurred between levels in the hierarchy by reassessing categorization (based on the lowest-level input that is significant to the fair value measurement as a whole) at the end of each reporting period.

(h) Provisions

(i) Provisions and Contingencies

Provisions are recognized when the Company has a present obligation (legal or constructive) as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation. Where the Company expects some or all of a provision to be reimbursed, for example, under an insurance contract, the reimbursement is recognized as a separate asset but only when the reimbursement is virtually certain. The expenses relating to provisions are generally presented in the consolidated statements of loss net of any reimbursement except for decommissioning liabilities. If the effect of the time value of money is material, provisions are discounted using a current discount rate that reflects, where appropriate, the risks specific to the liability. Where discounting is used, the increase in the provision due to the passage of time is recognized as a finance cost.

A contingency is disclosed where the existence of an obligation will only be confirmed by future events, or where the amount of a present obligation cannot be measured reliably or will likely not result in an economic outflow. Contingent assets are only disclosed when the inflow of economic benefits is probable.

(ii) Decommissioning Liabilities

PPR recognizes decommissioning liabilities related to its obligations to dismantle, retire and reclaim its oil and gas properties. Decommissioning obligations are measured at the present value of management's best estimate of expenditures required to settle the present obligation at the balance sheet date. The present value of the estimated obligation is recorded as a liability with a corresponding increase in the carrying amount of the related asset. The obligation is subsequently adjusted at the end period to reflect the passage of time and changes in the estimated future cash flows underlying the obligation. The increase in the provision due to the passage of time is recognized as accretion costs whereas increases or decreases due to changes in the estimated future cash flows or changes in the discount rate are capitalized. Actual costs incurred upon settlement or towards the settlement of the decommissioning obligations are charged against the provision to the extent the provision was established.

(i) Share-Based Compensation

PPR has not offered any awards that are classified as cash-settled awards. For equity settled share-based awards granted to officers, directors and employees, the grant date fair value of such awards is recognized as compensation costs within operating and general and administrative expenses, with a corresponding increase in contributed surplus over the vesting period. The Company also capitalizes a portion of the share-based compensation that is directly attributable to capital projects, with a corresponding decrease to compensation expense.

The fair value of option-based awards is measured using Black-Scholes option pricing model. Non-option based awards are valued based on the fair value of the underlying share units at grant date. A forfeiture rate is estimated on the grant date and is adjusted to reflect the actual number of awards that vest. Upon the exercise of the share-based awards, any consideration paid together with the amount previously recognized in contributed surplus is recorded as an increase in share capital. In the event that vested awards expire, previously recognized compensation expense associated with such awards is not reversed. In the event that awards are forfeited, previously recognized compensation expense associated with the unvested portion of such awards is reversed.

(j) Employee Benefits and Post-Retirement Obligation

PPR sponsors a group savings plan for its employees. Contributions made under the plan are expensed as the plan benefits are earned by the employees.

The Company also sponsors an unfunded post-retirement benefits plan to certain retirees, which is closed to new entrants. Expense for the post-retirement benefits plan includes the interest cost on post-retirement benefits obligations.

The liability of the post-retirement benefits plan is actuarially determined using the projected unit credit actuarial cost method prorated on service and reflects the Company's best estimate of future health care costs and retiree longevity. The accrued benefit obligation is discounted using the market interest rate on high-quality corporate debt instruments as at the measurement date. The Company accounts for its post-retirement benefits plan by recognizing the underfunded status of the plan as a liability in its consolidated statements of financial position. Interest costs on the unfunded obligation are recorded in Finance Costs. Any actuarial gains or losses are recognized in the year in which the changes occur through other comprehensive income.

(k) Flow-through Shares

Pursuant to the terms of the flow-through share agreements, the resource expenditure deductions for income tax purposes related to exploratory and development activities funded by flow-through shares are renounced to investors in accordance with tax legislation. Share capital is stated at the market value of shares without the flow-through feature at the time of issue, with a liability recognized representing the difference between cash received and market value. The premium paid for flow-through shares in excess of that market value of the shares is drawn down and deferred tax is recognized at the time the qualifying exploration and development expenditures are renounced and incurred.

(l) Income Tax

Income tax expense comprises current and deferred tax. Income tax expense is recognized in profit or loss except to the extent that it relates to items recognized directly in equity, in which case it is recognized in equity.

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted at the reporting date, and any adjustment to tax payable in respect of previous years.

Deferred tax is recognized on the temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is not recognized on the initial recognition of assets or liabilities in a transaction that is not a business combination.

Deferred tax is measured at the tax rates that are expected to be applied to temporary differences when they are reversed, based on the laws that have been enacted or substantively enacted by the reporting date. Deferred tax assets and liabilities are offset if there is a legally enforceable right to do so, and they relate to income taxes levied by the same tax authority on the same taxable entity, or on different taxable entities, but they intend to settle current tax liabilities and assets on a net basis or their tax assets and liabilities will be realized simultaneously.

A deferred tax asset is recognized to the extent that it is probable that future taxable profits will be available against which the temporary difference can be utilized. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realized.

(m) Reorganization Costs

Reorganization costs are non-recurring costs related to corporate restructuring activities. Reorganization costs include employment termination payments, accelerated share-based compensation expense, office closure costs and professional fees.

(n) Cash Equivalents

Cash equivalents include market deposits and similar type instruments, with an original maturity of three months or less when purchased.

(o) Inventory

Inventories are stated at the lower of cost and net realizable value. The cost of materials is the purchase cost, determined on first-in, first-out basis. The net realizable value is based on the estimated selling price in the ordinary course of business, less estimated costs necessary to sell.

(p) Foreign Currency

Transactions in foreign currencies are translated to Canadian dollars at exchange rates in effect to the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies are translated to Canadian dollars at the period end exchange rate. Non-monetary assets and liabilities denominated in foreign currencies that are measured at historical cost are not subsequently re-translated. Foreign currency differences arising on translation are recognized in profit or loss.

(q) Leases

The determination of whether an arrangement is, or contains a lease is based on the substance of the arrangement at the inception date of the contract. Leases, which transfer substantially all of the risks and rewards of ownership to the Company, are classified as finance leases. Finance leases are recognized at the lower of the fair value of the leased property or the present value of the minimum lease payments and are depreciated over the shorter of the estimated useful life of the asset and the lease term. As at December 31, 2017 PPR did not have any finance leases. Other leases are classified as operating leases and payments are recognized as an expense in the period incurred. Lease inducement costs are initially capitalized and amortized to net income over the lease terms.

(r) Adoption of New Accounting Standards and New Accounting Pronouncements

New and Amended Accounting Standards and Interpretations Adopted

There were no new or amended accounting standards or interpretations adopted during the year ended December 31, 2017.

New Accounting Pronouncements

- In April 2016, the IASB issued its final amendments to IFRS 15 – Revenue from Contracts with Customers (“IFRS 15”) which replaces IAS 11 – Construction Contracts, IAS 18 – Revenue and several revenue-related interpretations. The new standard establishes a single revenue recognition framework that applies to contracts with customers and requires an entity to recognize revenue to reflect the transfer of goods and services for the amount it expects to receive, when control is transferred to the purchaser. IFRS 15 is effective for annual periods beginning on or after January 1, 2018, with earlier adoption permitted. The standard may be applied retrospectively or using a modified retrospective approach. The Company has reviewed its revenue streams and underlying contracts with customers and has completed its documentation of such contracts. PPR will adopt IFRS 15 using the modified retrospective approach and has concluded that the adoption will not have a material impact on the consolidated financial statements. The Company will expand the disclosures in the notes to its financial statements as outlined in IFRS 15 including disaggregating revenue streams by product type;

- In July 2014, the IASB completed the final elements of IFRS 9 - Financial Instruments. The Standard supersedes earlier versions of IFRS 9 and completes the IASB's project to replace IAS 39 - Financial Instruments: Recognition and Measurement. IFRS 9, as amended, includes a principle-based approach for classification and measurement of financial assets, a single 'expected loss' impairment model and a substantially-reformed approach to hedge accounting. The Standard will come into effect for annual periods beginning on or after January 1, 2018, with earlier adoption permitted. The Company will adopt IFRS 9 on January 1, 2018 and has concluded that the 'expected loss' impairment model will not have a material impact on its consolidated financial statements. The Company does not currently apply hedge accounting to its derivative financial instruments and will not apply hedge accounting upon initial adoption of IFRS 9; and
- In January 2016, In January 2016, the IASB issued IFRS 16 - Leases, which replaces IAS 17 – Leases. For lessees, IFRS 16 removes the classification of leases as financing or operating leases, effectively treating all leases as finance leases which requires the recognition of lease assets and lease obligations. Certain short-term leases (less than 12 months) and leases of low-value assets are exempt from the requirements and may continue to be treated as operating leases. The standard will come into effect for annual periods beginning on or after January 1, 2019, with earlier adoption permitted if the entity is also applying IFRS 15 Revenue from Contracts with Customers. The Company intends to adopt IFRS 16 on January 1, 2019 and is in the process of identifying and reviewing contracts that fall within the scope of the new standard. The extent of the impact on the adoption of the standard has not yet been determined.

4. BUSINESS COMBINATION

(a) Red Earth Acquisition

On March 22, 2017, PPR acquired oil and natural gas properties in the Greater Red Earth area (“Red Earth Acquisition”) of Northern Alberta for cash consideration of \$40.9 million. The assets acquired include high quality and low decline oil production, which is complementary to PPR's existing operations at Evi in the Peace River Arch area of Northern Alberta.

PPR's oil and natural gas revenue and oil and natural gas revenue less royalties and operating expenses for the year ended December 31, 2017 included approximately \$13.6 million and \$5.6 million, respectively, attributable to the Red Earth Acquisition. Had the Red Earth Acquisition closed on January 1, 2017, PPR's oil and natural gas revenue and oil and natural gas revenue less royalties and operating expenses for the year ended December 31, 2017 would have been approximately \$84.4 million and \$32.7 million, respectively. This is not necessarily representative of future revenues and operations. The effect on net income is not determinable.

The acquisition has been accounted for as a business combination using the acquisition method of accounting. The following table summarizes preliminary purchase price allocation:

(\$000s)

Allocation:	
Property and equipment	50,500
Decommissioning liabilities	(5,263)
Other liabilities	(450)
Net assets acquired	44,787
Consideration:	
Cash	40,894
Gain on business combination	3,893

The recognized amounts of identifiable assets, liabilities and consideration issued are preliminary estimates and are subject to change. The fair value of the assets and liabilities included the use of certain key assumptions as described under Note 2(d) to the Financial Statements. The gain on business combination arose as the result of acquiring the assets for proceeds below the fair value of the assets acquired.

Transaction costs incurred in the year ended December 31, 2017 of \$0.7 million (2016 – \$nil), were expensed in the consolidated statement of earnings. Transaction costs included primarily legal fees and professional fees.

(b) Arsenal Energy Inc.

On September 12, 2016, the Arrangement was completed whereby PPR acquired all of the issued and outstanding common shares of Arsenal through the issuance of PPR common shares. Arsenal was a public oil and natural gas exploration, development and production company, listed on the TSX, with reserves, producing properties and prospects primarily located in Alberta.

The acquisition of Arsenal has been accounted for as a business combination using the acquisition method of accounting whereby PPR is deemed to be the acquirer of the Arsenal business. The following table summarizes the acquisition date fair value of consideration paid and the preliminary purchase price allocation:

(\$000s)

Allocation:	
Property and equipment	67,065
Exploration and evaluation assets	3,573
Cash	249
Accounts receivable	3,035
Other current assets	511
Current liabilities	(10,615)
Derivative liability	(286)
Decommissioning obligations	(21,487)
Other liabilities	(3,310)
Net assets acquired	38,735
Consideration:	
Shares issued (22,678,817 common shares at \$1.71 per share)	38,735

The fair values of cash and working capital including accounts receivable, other current assets and accounts payable approximate their carrying values due to their short-term maturities. The fair value of the remaining assets and liabilities included the use of certain key assumptions as described under Note 2(d) to the Financial Statements.

The fair value of consideration issued was calculated with reference to the enterprise value of PPR, based on the underlying consolidated assets and liabilities and confirmed through observable market trading multiples for similar entities.

Transaction costs incurred to effect the Arrangement with Arsenal incurred in the year ended December 31, 2017 of \$0.4 million (2016 – \$2.3 million) were recognized as Transaction Expense in the statement of loss. Transaction costs included primarily legal fees, professional fees, and change of control settlements.

5. ASSET ACQUISITIONS AND DISPOSITIONS

During 2017, PPR acquired properties in the Wheatland area comprised of undeveloped land and wellbores without associated reserves for cash consideration of \$1.0 million. The transactions resulted in \$2.1 million addition to exploration and evaluation assets and \$1.1 million addition to decommissioning liabilities.

The Company disposed of certain non-core properties and undeveloped land in 2017 in the provinces of Alberta and British Columbia for proceeds of \$1.4 million. The associated property and equipment, exploration and evaluation assets and decommissioning liabilities were derecognized, resulted in gains of \$0.9 million which were recognized in the consolidated statement of loss in 2017.

6. EXPLORATION AND EVALUATION ASSETS

<i>(\$000s)</i>	December 31, 2017	December 31, 2016
Cost Balance – beginning of year	81,374	77,384
Additions	13,756	30,632
Acquisitions (Notes 4 and 5)	2,131	3,573
Transfers to oil and gas property and equipment (Note 7)	(11,044)	(30,157)
Exploration and evaluation expense	(4,877)	(58)
Disposal (Note 5)	(4,069)	—
Cost Balance – end of year	77,271	81,374
Provision for impairment – beginning of year	(54,937)	(29,070)
Impairment (loss) recovery	17	(25,867)
Disposal (Note 5)	4,069	—
Provision for impairment – end of year	(50,851)	(54,937)
Net book value – beginning of the year	26,437	48,314
Net book value – end of the year	26,420	26,437

During 2017, PPR recognized \$4.9 million of exploration and evaluation expense related to surrendered leases primarily in the Wheatland area associated with the extension of the Lease Acquisition Capital Commitment (see “Contractual Obligations and Commitments” below). In addition to the surrendered leases, 2017 annual exploration and evaluation expenses included costs related to a dry exploration well drilled in the third quarter of 2017 in the Wheatland area and undeveloped land expiries. The exploratory well was drilled in conjunction with the satisfaction of the flow-through share commitment (see “Contractual Obligations and Commitments” section below for further explanation) and the related expenditures qualify as CEE. The nominal impairment recovery incurred in 2017 related to the change in estimates of decommissioning liabilities for properties with zero carrying value.

During the year ended December 31, 2016, the Company recognized an impairment loss related to leases that were due to expire within twelve months in the Evi CGU of \$0.9 million to an estimated recoverable amount of \$0.4 million based on its FVLCD. The FVLCD was determined using a market approach based on the estimated selling price of land in the related area considering recent transactions completed on similar assets. Key assumptions include the estimated selling prices of assets held considering the geographic location and related risk profile. The fair value measurement is non-recurring and is classified as level 3 in the fair value hierarchy (see Note 3(g) for information on the fair value hierarchy).

Additionally, during 2016, due to successful drilling in the Wheatland area and additional development prospects from the then-proposed Arrangement with Arsenal, along with a prolonged period of political uncertainty around oil and gas development in the province of Quebec, management shifted its exploration and development priorities, which in turn triggered an impairment indicator related to E&E assets in the Quebec exploratory area as at June 30, 2016. The impairment assessment resulted in the recognition of \$25.0 million of impairment in the year ended December 31, 2016 against the Quebec exploratory area to a recoverable amount of \$13.0 million based on its value-in-use.

During the year ended December 31, 2017, \$1.2 million (2016 – \$1.3 million) of directly attributable general and administrative expenses including a nominal amount (2016 – a nominal amount) of share-based compensation, were capitalized to E&E assets.

7. PROPERTY AND EQUIPMENT

<i>(\$000s)</i>	Production and Development	Office Equipment	Year Ended December 31, 2017
Cost:			
Balance – beginning of year	460,617	4,196	464,813
Additions	22,578	399	22,977
Acquisitions (Note 4)	50,500	—	50,500
Disposals (Note 5)	(13,276)	—	(13,276)
Transfer from E&E assets (Note 6)	11,044	—	11,044
Balance – end of year	531,463	4,595	536,058
Accumulated impairment, depletion and depreciation:			
Balance- beginning of year	(258,718)	(2,714)	(261,432)
Depletion and depreciation	(34,534)	(430)	(34,964)
Impairment loss (b)	(34,215)	—	(34,215)
Disposals	11,588	—	11,588
Balance – end of year	(315,879)	(3,144)	(319,023)
Net book value:			
At beginning of year	201,899	1,482	203,381
At end of year	215,584	1,451	217,035

(\$000s)	Production and Development	Office Equipment	Year Ended December 31, 2016
Cost:			
Balance – beginning of year	350,735	3,833	354,568
Additions	12,848	363	13,211
Acquisitions (Note 4)	67,065	—	67,065
Disposals	(188)	—	(188)
Transfer from E&E assets (Note 6)	30,157		
Balance – end of year	460,617	4,196	464,813
Accumulated impairment, depletion and depreciation:			
Balance- beginning of year	(237,149)	(2,147)	(239,296)
Depletion and depreciation	(20,641)	(567)	(21,208)
Impairment loss (b)	(1,023)	—	(1,023)
Disposals	95	—	95
Balance – end of year	(258,718)	(2,714)	(261,432)
Net book value:			
At beginning of year	113,586	1,686	115,272
At end of year	201,899	1,482	203,381

As at December 31, 2017, an estimated \$151.2 million in future development costs associated with proved plus probable undeveloped reserves were included in the calculation of depletion (December 31, 2016 - \$83.7 million).

(a) Capitalization of General and Administrative and Share-Based Compensation Expenses

During the year ended December 31, 2017, \$0.9 million (2016 – \$0.1 million) of directly attributable general and administrative expenses, including \$0.1 million (2016 – a nominal amount) of share-based compensation expenses, were capitalized to property and equipment.

(b) Impairment Loss

The Company conducted impairment tests on its Wheatland and Princess CGUs as at December 31, 2017, as a result of continued and prolonged declines in forecasted crude oil and natural gas prices. The impairment tests resulted in the recognition of \$30.7 million of impairment loss, comprised of \$16.6 million against the Wheatland CGU and \$14.1 million against the Princess CGU. These CGUs were written down to their respective recoverable amounts of \$28.0 million and \$26.1 million based on FVLCD for the Wheatland and Princess CGUs. This fair value measurement is non-recurring and is classified as level 3 in the fair value hierarchy (see Note 3(g) for information on fair value hierarchy). The FVLCD was estimated using an after-tax discount rate of 11%. An increase of 1% in the discount rate would have increased the impairment loss by \$2.0 million. A 5% decrease in forward commodity prices would have increased the impairment loss by \$4.1 million. The following estimated commodity prices were used in the Company's impairment calculation as at December 31, 2017:

December 31, 2017 ⁽¹⁾⁽²⁾	Edmonton Light Oil	AECO Natural Gas Price	Heavy Oil 25 API Hardisty
	(\$/bbl)	(\$/Mcf)	(\$/bbl)
2018	68.89	2.50	44.34
2019	71.07	2.78	48.32
2020	73.98	3.16	52.39
2021	78.47	3.43	56.93
2022	81.91	3.66	60.30
2023	84.01	3.80	62.15
2024	86.18	3.92	64.07
2025	88.40	4.05	66.00
2026	90.27	4.15	67.60
2027	92.03	4.24	69.08
2028	93.80	4.34	70.50
2029	95.60	4.43	71.96
2030	97.46	4.52	73.47
2031	99.33	4.60	74.97
2032 ⁽³⁾	101.25	4.69	76.52

- (1) The forecast benchmark prices listed above are adjusted for quality differentials, heat content and distance to market in performing the Company's impairment tests.
- (2) The forecast benchmark prices above are the consensus pricing from the following engineering firms: GLJ, McDaniel, Ryder Scott, Sproule, Timble and Deloitte.
- (3) Thereafter, annual increase of approximately 2 percent.

The remaining \$3.5 million of impairment loss recognized in 2017 included a \$3.4 million write down of assets classified as held for sale to their FVLCD and \$0.1 million of impairment related to changes in decommissioning liability estimates of certain properties with zero carrying value. Assets that were classified as held for sale as at September 30, 2017 were sold in the fourth quarter of 2017(note 5).

During the year ended December 31, 2016, the Company recorded impairment of \$0.8 million for changes in estimated decommissioning liabilities of certain properties with zero carrying value, write-down of \$0.2 million of surplus equipment and a recovery of inventory write-down of \$0.2 million.

8. LONG-TERM DEBT

(\$000s)	December 31, 2017	December 31, 2016
Revolving Facility (USD \$21.0 million and CAD \$12.9 million)	39,233	—
Senior Notes (USD \$16.0 million)	20,072	—
Amended Credit Facility	—	15,500
Deferred Financing Fees (net of amortization)	(2,979)	(453)
Value Allocated to Warrant Liability (net of accumulated interest)	(566)	—
Balance – end of year	55,760	15,047

Revolving Facility

On October 31, 2017, the Company entered into a USD \$40 million (CAD \$50.2 million using the year end exchange rate of \$1.0000 USD to \$1.2545 CAD) borrowing base senior secured revolving note facility (“the Revolving Facility”) with a maturity date of October 31, 2020. The Company can make further draws on the facility on or before October 31, 2019. The Revolving Facility is denominated in USD, but accommodates CAD advances up to the lesser of CAD \$18 million or USD \$10 million. As at December 31, 2017, the Company has drawn US\$21 million (CDN\$26.3 million equivalent) of USD denominated notes and CDN\$12.9 million of CAD denominated notes under the Revolving

Facility. All notes were issued at par by PPR Canada and are guaranteed by Prairie Provident Resources Inc. and certain of its other subsidiaries and secured by a USD \$200 million debenture.

The determination of the borrowing base is made by the lenders, in their sole discretion, taking into consideration the estimated value of PPR's oil and natural gas properties in accordance with the lenders' customary practices for oil and gas loans. The borrowing base is subject to a semi-annual redetermination, with the next redetermination scheduled for April 2018.

Amounts borrowed under the Revolving Facility can be drawn in the form of USD or CAD prime advances bearing interest based on reference bank USD and CAD prime lending rates announced from time to time, or LIBOR advances (in the case of USD amounts) or CDOR advances (in the case of CAD amounts) bearing interest based on LIBOR and CDOR rates in effect from time to time, plus an applicable margin. Applicable margins per annum are as follows:

- (i) for CDOR advances and Canadian dollar prime advances, the margins are between 350 and 500 basis points ("bps");
- (ii) for LIBOR advances and US dollar prime advances, the margins range from 325 to 475 bps; and
- (iii) standby fees on any undrawn borrowing capacity are between 50 to 87.5 bps per annum.

As at December 31, 2017, \$2.0 million of deferred costs related to the Revolving Facility was netted against its carrying value (December 31, 2016 – \$0.4 million related to the Amended Credit Facility).

Subordinated Senior Notes

On October 31, 2017, the Company obtained four-year USD \$16 million (CAD \$20.1 million using the year end exchange rate of \$1.0000 USD to \$1.2545 CAD) subordinated senior notes ("Senior Notes") with a maturity date of October 31, 2021. They bear interest at 15% per annum, payable quarterly in arrears, with up to 5% per annum deferrable at the election of PPR. The amount of any such deferred payment will become additional principal owing in respect of the Senior Notes payable at the maturity date. The terms of the Revolving Facility require that PPR Canada make the maximum deferred payment election. In conjunction with the Senior Notes, the Company issued 2,318,000 warrants with an exercise price of \$0.549 with a 5 year term expiring October 31, 2022. The warrants issued were classified as a financial liability as a result of a cashless exercise provision and were measured at fair value upon issuance using the Black-Scholes option pricing model (Note 9). The fair value of the warrant liability at the date of issuance of \$0.6 million was recorded as warrant liability and as a reduction to the carrying value of the Senior Notes. As at December 31, 2017, \$0.9 million of deferred costs related to its Senior Notes was netted against its carrying value (December 31, 2016 – \$nil).

Covenants

The note purchase agreement for the Revolving Facility, the Senior Note agreement and related parent and subsidiary guarantees contain various covenants on the part of the Company and its subsidiaries including covenants that place limitations on certain types of activities, including restrictions or requirements with respect to additional debt, liens, asset sales, hedging activities, investments, dividends and mergers and acquisitions. The Senior Note purchase agreement for the Revolving Facility and the subordinated note purchase agreement include the same financial covenants, with less restrictive thresholds under the subordinated note agreement for certain covenants. The financial covenants are as follows:

- total leverage, pursuant to which the ratio of adjusted indebtedness to EBITDAX (as defined below) for the four quarters most recently ended cannot exceed 3.5 to 1.0 (Senior Notes – 3.75 to 1.00) (as at December 31, 2017— 2.0 to 1.0);
- senior leverage, pursuant to which the ratio of senior adjusted indebtedness to EBITDAX (as defined below) for the four quarters most recently ended cannot exceed 3.0 to 1.0 (Senior Notes – 3.25 to 1.00) (as at December 31, 2017 — 2.0 to 1.0);

- asset coverage, pursuant to which the ratio of adjusted net present value of estimated future net revenue from proved reserves (discounted at 10% per annum) to adjusted indebtedness as of the date of any reserves report cannot be less than 1.3 to 1.0 (Senior Notes – 1.3 to 1.00) (as at December 31, 2017 – 2.1 to 1.0); and
- current ratio, pursuant to which the ratio of consolidated current assets, plus any undrawn capacity under the Revolving Facility, to consolidated current liabilities at the end of any fiscal quarter cannot be less than 1.0 to 1.0 (Senior Notes – 0.85 to 1.00) (as at December 31, 2017 – 1.5 to 1.0). Under the agreements, current assets excludes derivative assets while current liabilities excludes the current portion of long-term debt, the decommissioning obligations, derivative liabilities and non-cash liabilities.

The Company was in compliance with all covenants as at December 31, 2017.

Letters of Credit

As at December 31, 2017, PPR had outstanding letters of credit of \$4.8 million. The letters of credit are issued by a financial institution at which PPR has a \$4.9 million cash deposit to cover letters of credit. The related deposit is classified as restricted cash on the statement of financial position and the balance is guaranteed investment certificates with maturity dates of one year or less when purchased.

Amended Credit Facility

On October 31, 2017, the Company used proceeds from the Revolving Facility and Subordinated Notes to repay and retire the its previously outstanding credit facility with a syndicate of banks (the “Amended Credit Facility”). Under the Amended Credit Facility, PPR had a \$55 million syndicated revolving term facility and a \$10 million operating facility. The Amended Credit Facility was collateralized by a demand debenture from PPR and each of its restricted subsidiaries in the amount of \$500 million granting a first priority security interest over all present and after-acquired personal property and a first floating charge over all other present and after-acquired property, together with a fixed charge and mortgage over its existing borrowing base assets. A fixed charge and mortgage over after-acquired borrowing base assets will only be granted under certain circumstances.

As at December 31, 2016, under the Company’s credit facility PPR had outstanding long-term debt of \$15.0 million and had issued \$5.4 million of letters of credit.

9. WARRANT LIABILITY

	Number of Warrants (000s)	Amount (\$000s)
Warrant liability		
PPR Warrant Liability, December 31, 2015 & 2016	—	—
Issued	2,318	533
PPR Warrant Liability, December 31, 2017	2,318	533

In conjunction with the Subordinated Notes (Note 8), the Company issued 2,318,000 warrants with an exercise price of \$0.549 with a 5 year term expiring October 31, 2022. The warrants issued were classified as a financial liability as a result of a cashless exercise provision. As such, the warrant liability will be measured at fair value upon issuance and at each subsequent reporting period, with the changes in fair value recorded in the consolidated statement of loss. The fair value of these warrants is determined using the Black-Scholes option pricing model. The value of the warrant liability as at December 31, 2017 was \$0.5 million. These warrants are exercisable any time and thus the value of these warrants is presented as current liability in the consolidated statement of financial position.

The fair value of the warrants as at December 31, 2017 was estimated using the following assumptions:

	December 31, 2017
Fair value of options	\$0.23
Risk free interest rate	1.8%
Expected life of options (years)	4.8
Expected volatility ⁽¹⁾	65.5%
Stock price	0.46
Dividends per share	—

10. DECOMMISSIONING LIABILITIES

(\$000s)	December 31, 2017	December 31, 2016
Balance – beginning of year	97,720	70,502
Liabilities incurred	1,074	1,859
Liabilities acquired – business combination (Note 4)	5,263	21,487
Liabilities acquired – asset acquisition (Note 5)	1,141	—
Dispositions (Note 5)	(1,208)	—
Settlements	(5,136)	(4,540)
Change in estimates	11,973	7,086
Accretion of decommissioning liabilities	2,007	1,326
Sub total	112,834	97,720
Current portion – end of year	2,300	3,500
Long-term portion – end of year	110,534	94,220

The Company's decommissioning liabilities result from its ownership interests in oil and natural gas assets and are estimated based on the Company's net ownership interests in wells and facilities, the estimated costs to abandon and reclaim such properties and the estimated timing of these costs to be incurred in future years. At December 31, 2017, risk-free rates of 1.7% - 2.2% (December 31, 2016 – 0.7% - 2.2%) and an inflation rate of 1.7% (December 31, 2016 – 1.7%) were used to calculate the net present value of the decommissioning liabilities.

Decommissioning obligations assumed from acquisitions were initially measured at fair value using a credit-adjusted risk free rate of 5.7% to discount estimated future cash flows. In accordance with PPR's accounting policy, decommissioning obligations are estimated and carried on the financial statements using risk-free discount rates. As such, acquired decommissioning obligations were revalued immediately after their initial recognition using the corresponding risk-free rates. The revaluation of the decommissioning liabilities acquired during the first quarter of 2017 (Notes 4 and 5) resulted in an increase to the carrying values of decommissioning liabilities of \$11.5 million, which was included in changes in estimates. Partially offsetting the increase was a \$1.2 million decrease due to changes in discount rates that were recognized as of December 31, 2017. The remaining increase of \$1.7 million during 2017 resulted from changes in various underlying assumptions. Changes in estimates in 2016 resulted in an increase in the decommissioning liabilities of \$7.1 million, which included \$15.2 million related to revaluation of acquired liabilities less an \$8.1 million decrease primarily due to changes in cost assumptions.

The Company has estimated the undiscounted total future liabilities of approximately \$171.5 million spanning over the next 55 years, based on an inflation rate of 1.7% (December 31, 2016 – \$141.1 million). Of the estimated undiscounted total future liabilities, \$10.1 million is estimated to be incurred over the next five years.

11. SHARE CAPITAL

(a) Authorized

The Company is authorized to issue an unlimited number of common shares.

(b) Units Outstanding

	Number of Shares (000s)	Amount (\$000s)
Common shares:		
PPR Shares, inception	—	—
Lone Pine Resources common shares, December 31, 2015	99,986	—
LPR Canada common shares, December 31, 2015	24,986	73,912
Lone Pine combined and consolidated common shares	124,972	73,912
Cancellation of Lone Pine Resources common shares (Note 1)	(99,986)	—
Exchange of PPR shares for LPR Canada common shares ⁽¹⁾	(11,134)	—
PPR Shares outstanding upon the exchange for Lone Pine common shares (Note 1)	13,852	73,912
PPR Shares issued in exchange for the Preferred Shares	60,878	193,851
PPR Shares outstanding prior to Arsenal acquisition (Notes 1 & 4)	74,730	267,763
PPR Shares issued in exchange for Arsenal shares (Notes 1 & 4)	22,679	38,735
Reduction of consolidated share capital (Note 1)	—	(198,570)
Issued for cash	5,840	4,556
Share issuance costs	—	(519)
Issued on settlement of RSUs	904	3,382
Withholding taxes on settlement of RSUs	—	(285)
PPR Shares, December 31, 2016	104,153	115,062
Issued	11,651	7,204
Share issuance costs	—	(1,065)
Issued on settlement of restricted share units	84	389
Withholding taxes on settlement of restricted share units	—	(44)
PPR Shares, December 31, 2017	115,888	121,546
	Number of	Amount
	Warrants	(\$000s)
	(000s)	
Warrants:		
PPR Warrants, December 31, 2015 & 2016	—	—
Issued	3,155	337
PPR Warrants, December 31, 2017	3,155	337

On March 16, 2017, the Company closed a bought-deal financing under which, the Company issued 5,195,000 flow-through common shares with respect to Canadian Exploration Expenses (“CEE”) at \$0.77 per share and 5,971,000 subscription receipts (“Subscription Receipts”) at \$0.67 per unit for total gross proceeds of \$8.0 million (net proceeds of \$7.0 million). The proceeds from the sale of Subscription Receipts were held in escrow until the closing of the Red Earth Acquisition, upon which, the purchasers of the Subscription Receipts automatically received, for every Subscription Receipt held, one PPR common share and one-half of one common share purchase warrant (each whole warrant, a “Warrant”). Each Warrant entitles the holder to acquire one common share at an exercise price of \$0.87 per share until March 16, 2019. The fair value of warrants was determined as the difference between the trading price of common shares on the date of closing of \$0.62 and the price for Subscription Receipts of \$0.67 per unit, resulting in a value of \$0.05 per half warrant or \$0.10 per Warrant. Pursuant to the bought deal financing, the

underwriters' had an over-allotment option to purchase, at any time prior to April 15, 2017, up to an additional 15% of the number of flow-through common shares and Subscription Receipts initially offered. On April 12, 2017, the over-allotment option was partially exercised, resulting in the issuance of an additional 146,170 CEE flow-through common shares at \$0.77 per share and 338,650 Subscription Receipts at \$0.67 per share for total gross proceeds of \$0.3 million (net proceeds of \$0.3 million). The fair value of the common shares and warrants issued pursuant to the over-allotment Subscription Receipts was determined on a pro-rata basis with reference to the trading prices of common shares and warrants on the date the over-allotment closed.

As defined by the Income Tax Act, the Company has until December 31, 2018 to incur \$4.1 million of CEE costs related to the flow-through common share issuances in 2017. The difference between cash received from the issuance of flow-through shares and the market value of common shares issued of \$0.7 million was recognized as a flow-through premium liability. As of December 31, 2017, the Company incurred \$0.4 million of related CEE expenditures.

On November 28, 2017, the Toronto Stock Exchange ("TSX") accepted the Company's notice to make a normal course issuer bid ("NCIB") to purchase its outstanding common shares on the open market. The TSX authorized the Company to purchase up to 4,900,000 common shares during the period from December 1, 2017 to November 30, 2018. Shares purchased under the bid will be cancelled. There were no shares purchased under the bid as at December 31, 2017. Subsequent to December 31, 2017, the Company purchased and cancelled 15,000 shares under the NCIB.

On December 16, 2016, the Company issued 5,465,000 flow-through common shares with respect to CEE at \$0.85 per share and 375,000 flow-through common shares with respect to Canadian Development Expenses ("CDE") at \$0.80 per common share for total gross proceeds of \$4.9 million (net proceeds of \$4.4 million). The difference between cash received from the issuance and the market value of shares issued of \$0.4 million was recognized as a flow-through premium liability. The requirement, as defined by the Income Tax Act, for the Company to incur \$4.6 million of CEE costs and \$0.3 million of CDE costs by December 31, 2017 has been fully met.

Arsenal Arrangement

The Arrangement with Arsenal involved the following key steps:

- Issuance of 13.9 million PPR common shares to the shareholders of LPR Canada in exchange for all LPR Canada common shares;
- Issuance of 60.9 million PPR common shares in exchange for all LPR Canada preferred shares;
- Amalgamation of Lone Pine Resources with a wholly-owned subsidiary of PPR, whereby PPR became the sole owner of the amalgamated company. The outstanding Lone Pine Resources common shares were cancelled without any consideration; and
- The acquisition of all of the issued and outstanding common voting shares of Arsenal with 22.7 million PPR common shares pursuant to the Arrangement in accordance with the terms and conditions of the arrangement agreement dated June 23, 2016 as amended on August 2, 2016.

The exchange of PPR common shares for LPR Canada preferred shares and LPR Canada common shares, and the amalgamation of PPR's wholly owned subsidiary with Lone Pine Resources were not considered business combinations as there was no change to the controlling shareholder group resulting from the Transaction. Accordingly, the consolidated financial statements of PPR have been prepared as a continuation of LPR Canada and Lone Pine Resources' combined and consolidated financial statements. Subsequently, on November 1, 2016, LPR Canada changed its name to Prairie Provident Canada Resources Ltd.

Preferred Shares

Prior to the Arrangement, LPR Canada had outstanding preferred shares (“Preferred Shares”) that were classified as financial liabilities due to the holder’s put option. Further, the Preferred Shares were denominated in United States currency, resulting in the conversion option classified as an embedded derivative (the “Preferred Share – Conversion Liability”).

Pursuant to the Arrangement, outstanding Preferred Shares were exchanged for PPR common shares at an exchange ratio of 0.81, whereby 60.9 million PPR common shares were issued. As the preferred shareholders were also common shareholders of PPR, the transaction was in substance an equity contribution to the Company. Upon the exchange, PPR derecognized the Preferred Shares liability and the Preferred Share - Conversion Liability (collectively, “Preferred Share Liabilities”) and recorded the PPR common shares at the carrying value of the Preferred Share Liabilities, resulting in an increase to the share capital of \$193.9 million without any recognition of gains or losses.

During the year ended December 31, 2016, a \$9.8 million unrealized foreign exchange gain was recognized related to the translation of the US dollar denominated Preferred Shares at prevailing rates, and a \$11.0 million of amortization recognized (note 17).

(c) Loss per Share

Years Ended (\$000s)	December 31, 2017	December 31, 2016
Net loss for the year	(47,802)	(60,396)
Weighted average number of common shares ⁽¹⁾		
Basic & diluted	113,350	97,868
Basic & diluted net loss per share	(0.42)	(0.62)

⁽¹⁾ As the historical financial statements were prepared on a combined and consolidated basis it was not possible to measure loss per share in accordance with IAS 33 until subsequent to the closing of the Arrangement on September 12, 2016 when Lone Pine and Arsenal were brought under a common parent. The Company calculated loss per share for the historical period by assuming that the shares issued upon the closing of the Arrangement at September 12, 2016 were outstanding since the beginning of the period.

12. SHARE-BASED COMPENSATION

(a) Long-term incentive plans subsequent to the Arrangement

In conjunction with the closing of the Arrangement, the Company adopted new long-term incentive plans for employees and directors pursuant to which share-based incentive awards may be granted.

Stock Options

Under the Company’s stock option plan, options granted vest evenly over a three year period and expire 5 years after the grant date, except for the initial options granted upon the completion of the Arrangement, where those options will vest in three tranches on January 1, 2017, January 1, 2018 and January 1, 2019. Each option entitles the holder to purchase one common share at the specified exercise price. The following table summarizes the stock options outstanding and exercisable under the plan:

	Number of Options	Weighted Average Exercise Price
Balance, January 1, 2016	—	—
Granted	752,174	0.96
Balance, December 31, 2016	752,174	0.96
Granted	1,969,795	0.75
Cancelled	(37,500)	0.80
Balance, December 31, 2017	2,684,469	0.81
Exercisable at December 31, 2017	250,724	0.96

The weighted average remaining contractual life of options outstanding as at December 31, 2017 was 4.0 years (December 31, 2016 – 4.7 years).

The fair value of options granted was estimated on the date of grant using the Black-Scholes option-pricing model with the following weighted average assumptions and resulting values for the grants made:

	December 31, 2017	December 31, 2016
Fair value of options	\$0.37	\$0.41
Risk free interest rate	1.0%	0.7%
Expected life of options (years)	3.0	3.1
Expected volatility ⁽¹⁾	70.0%	70.0%
Estimated forfeiture rate	3.2%	2.0%
Dividends per share	—	—

⁽¹⁾ The expected volatility was calculated with reference to the volatilities of peer companies over a time period consistent with the expected life of the options upon grant due to the limited trading history of PPR at the date of grant.

Performance Share Units

Under the Company's incentive security plan, performance share units ("PSUs") granted vest on a date specified under the grant agreement, no more than 3 years after the grant date. The number of common shares issued for each PSU is subject to a performance multiplier ranging from 0 to 2 based on share performance relative to a selected peer group. PSUs may be settled in common shares or cash at the discretion of the Company, however, it is PPR's intention to settle the PSUs in common shares and the plan has accounted for as equity settled.

The following table summarizes the PSUs outstanding under the plan:

	PSUs
Balance, January 1, 2016	—
Granted	116,427
Balance, December 31, 2016	116,427
Granted	354,905
Balance, December 31, 2017	471,332
Weighted average fair value per PSU at grant date	0.83

The fair value of PSUs issued is determined at the date of the grant using the closing price of common shares, multiplied by the estimated performance multiplier. For the purposes of share-based compensation expense, a performance multiplier of 1 has been estimated for units granted in 2017. The weighted average fair value of units awarded in 2017 was \$0.80 and will vest on December 15, 2019.

Deferred Restricted Share Units

Deferred restricted share units (“DSUs”) are granted under the Company’s incentive security plan to non-management directors of the Company. DSUs vest in their entirety on the grant date and will be settled when a director ceases to be a member of the board of directors. DSUs may be settled in common shares or cash at the discretion of the Company; however, it is PPR’s intention to settle the DSUs in common shares and the plan has been accounted for as equity settled.

The following table summarizes the PSUs outstanding under the plan:

	DSUs
Balance, December 31, 2016	—
Granted	243,368
Balance, December 31, 2017	243,368

The fair value of DSUs issued is determined at the date of the grant using the closing price of common shares. The weighted average fair value of units granted in 2017 is \$0.50.

Restricted Share Units

Subsequent to December 31, 2017, the Company granted 1,922,274 restricted share units (“RSUs”) under the Company’s incentive security plan. RSUs vest evenly over a three-year period and will be settled in common shares or cash at the discretion of the Company; however, it is PPR’s intention to settle the RSUs in common shares.

(b) Long-term incentive plans prior to the Arrangement

Restricted shares units were issued in 2014 pursuant to the Company’s previous Equity Incentive Plan (“Prior RSUs”). On February 10, 2017, the entity issued 84,086 common shares related to the settlement of 142,812 Prior RSUs. The difference between the number of Prior RSUs settled and the number of common shares issued relates to shares withheld to cover the withholding tax obligations of certain unit holders. The Company settled the withholding tax obligation with the related tax authority in cash rather than through the issuance of shares.

The number of Prior RSUs outstanding is as follows:

	Prior RSUs Issued to Officers and Employees
Outstanding – December 31, 2016	142,812
Settled	(142,812)
Outstanding – December 31, 2017	—
Weighted average fair value per RSU at grant date:	\$1.57

(c) Share-based compensation expense

For the year ended December 31, 2017, share-based compensation of \$0.8 million (2016 – \$0.4 million) was included in general and administrative expense net of \$0.1 million of capitalized share based compensation (2016 – a nominal amount). A nominal amount of share-based compensation was included in operating expense for the years ended December 31, 2017 and December 31, 2016.

13. INCOME TAX

The tax provision differs from the amount computed by applying the combined Canadian federal and provincial statutory income tax rates to income before income tax expense as follows:

Years ended

(\$000s)	December 31, 2017	December 31, 2016
Net loss before taxes	(48,272)	(60,410)
Statutory income tax rate	26.92%	27.00%
Expected income tax recovery	(12,995)	(16,313)
Add (deduct):		
Accretion and foreign exchange on preferred shares	—	332
Change in unrecognized deferred tax asset	12,467	15,018
Foreign currency translation gains	(174)	—
Accounting gain on business combination	(1,051)	—
Effect of future US statutory rate reduction	896	—
Non-deductible share-based compensation	222	116
Non-deductible costs	—	186
Flow-through share renunciations	1,335	347
Flow-through share premium adjustments	(477)	—
Other	(693)	300
Tax expenses	(470)	(14)

The movements in deferred tax balances during the year ended December 31, 2017 are as follows:

(\$000s)	Balance December 31, 2016	Recognized in Net Loss	Recognized in OCI	Recognized in Equity	Recognized in Other	Business Combination	Balance December 31, 2017
Deferred tax liabilities:							
Unrealized translation gains	—	(174)	—	—	—	—	(174)
Total deferred tax liabilities	—	(174)	—	—	—	—	(174)
Deferred tax assets:							
Petroleum and natural gas assets	35,379	152	—	—	—	13,077	48,608
Decommissioning liabilities	26,385	2,659	—	—	—	1,421	30,465
Net operating loss carry forwards	2,218	(969)	—	—	—	—	1,249
Unrealized gains on financial instrument	1,650	(212)	—	—	—	—	1,438
Flow-through share premium	—	(477)	—	—	477	—	—
Financing and restructuring fees	1,796	(579)	—	—	—	—	1,217
Non-capital losses	41,429	7,480	—	—	—	—	48,909
Accruals and other items, net	899	(227)	(40)	286	—	122	1,040
Total deferred tax assets	109,756	7,827	(40)	286	477	14,620	132,926
Net deferred tax asset	109,756	7,653	(40)	286	477	14,620	132,752
Less: Unrecognized deferred tax asset	(109,756)	(8,130)	40	(286)	—	(14,620)	(132,752)
Deferred taxes	—	(477)	—	—	477	—	—

The movements in deferred tax balances during the year ended December 31, 2016 are as follows:

<i>(\$000s)</i>	Balance December 31, 2015	Recognized in Net Loss	Recognized in OCI	Recognized in Equity	Arsenal Acquisition	Balance December 31, 2016
Deferred tax liabilities:						
Unrealized gains on financial instruments	(3,631)	5,204	—	—	77	1,650
Total deferred tax liabilities	(3,631)	5,204	—	—	77	1,650
Deferred tax assets:						
Petroleum and natural gas assets	4,127	40,482	—	—	(9,230)	35,379
Decommissioning liabilities	19,036	1,547	—	—	5,802	26,385
Net operating loss carry forwards	2,286	(68)	—	—	—	2,218
Financing and restructuring fees	2,480	(684)	—	—	—	1,796
Non-capital losses	64,109	(31,928)	—	—	9,248	41,429
Accruals and other items, net	550	(84)	(74)	139	368	899
Total deferred tax assets	92,588	9,265	(74)	139	6,188	108,106
Net deferred tax asset	88,957	14,469	(74)	139	6,265	109,756
Less: Unrecognized deferred tax asset	(88,957)	(14,469)	74	(139)	(6,265)	(109,756)
Deferred taxes	—	—	—	—	—	—

At December 31, 2017, the Company had \$403.6 million (December 31, 2016 – \$325.7 million) of federal tax pools in Canada related to the exploration, development and production of oil and gas available for deduction against future Canadian taxable income. In addition, the Company had Canadian tax loss carry-forwards in the amount of \$179.9 million (December 31, 2016 – \$153.1 million), scheduled to expire in the years 2026 to 2037.

As of December 31, 2017 and 2016, the Company did not recognize any deferred tax assets in the consolidated statements of financial position for deductible temporary differences and unused tax losses as there was insufficient evidence to indicate that it was probable that future taxable profits in excess of profits arising from the reversal of existing temporary difference would be generated to utilize the existing deferred tax assets.

14. SUPPLEMENTAL INFORMATION

Cash Flow Presentation

Changes in non-cash working capital and interest paid are summarized:

Years Ended (\$000s)	December 31, 2017	December 31, 2016
Source (use) of cash:		
Accounts receivable	(119)	(1,953)
Prepaid expenses and other current assets	(516)	532
Accounts payable and accrued liabilities	(1,025)	12,974
Working capital acquired (Note 4)	—	(7,069)
	(1,660)	4,484
Related to operating activities	(501)	2,539
Related to investing activities	(1,159)	1,945
	(1,660)	4,484
Other:		
Interest paid during the year	5,026	623

Changes in liabilities arising from financing activities:

	Amended Credit Facility	Revolving Facility	Senior Notes
Balance as of December 31, 2016	15,047	—	—
Changes in cash flows	(15,458)	39,963	20,049
Debt issuance costs	(56)	(2,149)	(974)
Non-cash changes			
Unrealized foreign exchange gain	—	(730)	(557)
Amortization of debt issuance costs	467	119	39
Balance as of December 31, 2017	—	37,203	18,557

15. OPERATING EXPENSE

Years Ended (\$000s)	December 31, 2017	December 31, 2016
Lease operating expense	27,535	16,515
Transportation and processing	7,251	5,128
Production and property taxes	3,864	1,774
Total operating expense	38,650	23,417

16. GENERAL AND ADMINISTRATIVE COSTS

Years Ended (\$000s)	December 31, 2017	December 31, 2016
Salaries and benefits	5,930	5,442
Share-based compensation	772	392
Office rents and leases	1,412	1,457
Professional fees	2,960	2,853
Other – office and administration	1,227	2,120
	12,301	12,264
Amounts capitalized to property and equipment and E&E assets (Notes 6 & 7)	(2,083)	(1,434)
General and administrative expense	10,218	10,830

17. FINANCE COST

Years Ended (\$000s)	December 31, 2017	December 31, 2016
Interest expense	3,028	730
Accretion – preferred shares (Note 11)	—	11,024
Accretion – decommissioning liability (Note 10)	2,007	1,326
Accretion – other liabilities	125	39
Gain on warrant liability	(46)	—
Finance cost	5,114	13,119

18. FINANCIAL INSTRUMENTS, FAIR VALUES AND RISK MANAGEMENT

The financial instruments of PPR consist of cash and cash equivalents, restricted cash, accounts receivable, accounts payable, borrowings under its Revolving Facility and Senior Notes, derivative contracts and warrant liability.

Cash and cash equivalents, restricted cash and derivative contracts are classified as held for trading. Accounts receivable are classified as loans and receivables. Warrant liability is classified as held for trading. The remaining instruments are considered other financial liabilities.

(a) Fair Value

The fair value of the borrowings under PPR's Revolving Facility and Senior Notes approximates their carrying values (excluding deferred financing charges and the value assigned to the warrant liability) due to their recent issuance. Additionally, the Revolving Facility bears floating market rates.

The Company's finance department is responsible for performing the valuation of financial instruments. The valuation process and results are reviewed and approved by management at least once every quarter, in line with the Company's quarterly reporting dates.

Cash and cash equivalents and derivative instruments are measured and recorded on PPR's statement of financial position at fair value through profit and loss. Cash and cash equivalents, restricted cash, derivative contracts and the warrant liability have been assessed on the fair value hierarchy described in Note 3(g). Cash is classified as Level 1, while cash equivalents, restricted cash, derivative contracts and warrant liability are

classified as Level 2. During the years ended December 31, 2017 and 2016, there were no transfers among Levels 1, 2 and 3.

Derivative contracts are valued using valuation techniques with observable market inputs. The most frequently applied valuation techniques include forward pricing and swap models using present value calculations and third-party option valuation models. The models incorporate various inputs including the credit quality of counterparties, foreign exchange spot and forward rates, and forward rate curves and volatilities of the underlying commodity. The fair values of the derivative contracts are net of a credit valuation adjustment attributable to derivative counterparty default risk or the Company's own default risk.

(b) Risk Management

The Company's activities expose it to a variety of financial risks that arise as result of its exploration, development production and financing activities such as:

- Credit risk;
- Liquidity risk; and
- Market risk

This note presents information about the Company's exposure to each of the above risks, the Company's objectives, policies and processes for measuring and managing risk and the Company's management of capital. The Board of Directors oversees management's establishment and execution of the Company's risk management framework. Management has implemented, and monitors compliance with, risk management policies. The Company's risk management policies are established to identify and analyze the risks faced by the Company, to set appropriate risk limits and controls, and to monitor risks and adherence to market conditions and the Company's activities.

(i) Credit Risk

Credit risk is the risk of financial loss to the Company if a customer or counterparty to a financial instrument fails to meet its contractual obligations, and arises principally from the Company's accounts receivable from joint operators and oil and natural gas marketers.

Cash, Cash Equivalents and Restricted Cash

The Company limits its exposure to credit risk related to cash by depositing its excess cash only with financial institutions that have investment grade credit ratings. As of December 31, 2017, restricted cash included \$4.9 million of guaranteed investment certificates with maturity dates of one year or less (December 31, 2016 – no cash equivalents or restricted cash held).

Accounts Receivable

All of the Company's operations are conducted in Canada. The Company's exposure to credit risk is influenced mainly by the individual characteristics of each customer. All of the Company's petroleum and natural gas production is marketed under standard industry terms. Accounts receivable from oil and natural gas marketers are normally collected on the 25th day of the month following production. The Company's policy to mitigate credit risk associated with these balances is to establish marketing relationships with a number of large purchasers. The Company historically has not experienced any collection issues with its oil and natural gas marketers.

Receivable from joint operators are typically collected within one to three months of the joint venture bill being issued. The Company attempts to mitigate the risk from joint venture receivables by obtaining the

partners' pre-approval of significant capital expenditures. However, the receivables are from participants in the oil and natural gas sector, and collection of the balances is dependent on industry factors such as commodity price fluctuations, escalating costs and the risk of unsuccessful drilling. In addition, further risks exist with joint operators as disagreements occasionally arise that may increase the potential for non-collection. The Company does not typically obtain collateral from oil and natural gas marketers or joint operators; however, the Company can withhold its production from joint operators in the event of non-payment.

As at December 31, the maximum exposure to credit risk for loans and receivables at the reporting date by type of customer was:

(\$000s)	2017	2016
Oil and natural gas marketing companies	6,276	5,619
Joint operators	1,878	1,766
Government agencies	31	118
Counterparties – derivative instruments	67	399
Other	402	633
Total accounts receivable	8,654	8,535

As at December 31, the Company's accounts receivable are aged as follows:

(\$000s)	2017	2016
Current (less than 90 days)	7,871	7,616
Past due (more than 90 days)	783	919
Total	8,654	8,535

PPR's allowance for doubtful accounts was \$0.6 million as at December 31, 2017 (December 31, 2016 – \$0.7 million). When determining whether amounts that are past due are collectible, management assesses the creditworthiness and past payment history of the counterparty, as well as the nature of the past due amount.

Derivatives

PPR executes with each of its derivative counterparties an International Swap and Derivatives Association, Inc. ("ISDA") Master Agreement, which is a standard industry form contract containing general terms and conditions applicable to many types of derivative transactions. As of December 31, 2017, all of the derivative counterparties have entered inter-creditor agreements with the Company's lender to eliminate the need to post any collateral. PPR's derivative counterparties are all financial institutions that are engaged in similar activities and have similar economic characteristics that, in general, could cause their ability to meet contractual obligations to be similarly affected by changes in economic or other conditions. PPR does not require the posting of collateral for its benefit under its derivative agreements. However, PPR's ISDA Master Agreements generally contain netting provisions whereby if on any date amounts would otherwise be payable by each party to the other, then on such date the party that owes the larger amount will pay the excess of that amount over the smaller amount owed by the other party, thus satisfying each party's obligations. These provisions generally apply to all derivative transactions, or all derivative transactions of the same type (e.g., commodity, interest rate, etc.), with the particular counterparty.

The following is a summary of PPR's financial assets and financial liabilities that were subject to offsetting as at December 31, 2017 and 2016. The net asset amounts represented the maximum exposure to credit risks for derivative instruments at each applicable reporting date:

December 31, 2017 (\$000s)	Gross Assets (Liabilities)	Amounts Offset Gross Assets (Liabilities)	Net Amount Presented
Current:			
Derivative instruments assets	1,072	(177)	895
Derivative instruments liabilities	(4,333)	177	(4,156)
Long-term:			
Derivative instruments assets – long-term	1,736	(1,544)	192
Derivative instruments liabilities – long-term	(3,802)	1,544	(2,258)

December 31, 2016 (\$000s)	Gross Assets (Liabilities)	Amounts Offset Gross Assets (Liabilities)	Net Amount Presented
Current:			
Derivative instruments assets	2,944	(2,944)	—
Derivative instruments liabilities	(5,255)	2,944	(2,311)
Long-term:			
Derivative instruments assets – long-term	940	(940)	—
Derivative instruments liabilities – long-term	(4,740)	940	(3,800)

(ii) Liquidity Risk

Liquidity risk is the risk that the Company will encounter difficulty in meeting obligations associated with financial liabilities. The Company addresses its liquidity risk through its capital management of cash, committed credit capacity along with its planned capital expenditure program. As outlined in Note 8, at December 31, 2017, the Company had USD \$9.0 million borrowing capacity under the Revolving Facility. In March 2017, PPR acquired assets in the Greater Red Earth area (“Red Earth Acquisition”) for cash consideration of \$41.0 million, prior to closing adjustments (Note 4). In conjunction with the closing of this acquisition, PPR issued flow-through common shares and common shares through a bought deal financing that raised gross proceeds of \$8.0 million, which was used to fund the Red Earth Acquisition. The balance of the purchase price was funded with borrowings under long-term debt facilities. Though PPR has increased its debt leverage significantly during 2017, PPR also expects its future funds flow to increase as a result of the Red Earth Acquisition. PPR anticipates its future development to be funded primarily with cash flows from operations, while maintaining a balanced leverage ratio. The Company has determined that its current financial obligations, including current commitments (Note 20), are adequately funded from the available borrowing capacity and from working capital derived from operations. Except for the long-term portion of derivative financial instruments and long-term debt, all of the Company’s financial liabilities are due within one year.

(iii) Market Risk

Market risk is the risk that changes in market prices, such as commodity prices, foreign exchange rates and interest rates will affect the Company’s income or the value of the financial instruments. The objective of market risk management is to manage and control market risk exposure within acceptable parameters, while optimizing the return.

The Company may use financial derivative contracts to manage market risks as disclosed below. All such transactions are conducted within risk management tolerances that are reviewed by the Board of Directors.

Currency Risk

Currency risk is the risk that the fair value of future cash flows will fluctuate as a result of changes in foreign exchange rates. Substantially all of the Company's petroleum and natural gas sales are conducted in Canada and are denominated in Canadian dollars. Canadian commodity prices are influenced by fluctuations in the Canada to United States dollar exchange rate. Prices for oil are determined in global markets and generally denominated in United States dollars. The Company is exposed to currency risk in relation to its US dollar denominated long-term debt. A 10% strengthening or weakening of the US dollar will contribute a \$4.6 million increase or decrease to the Company's net loss before tax (2016 – nil). The exposure of realized prices fluctuations of the US dollar and Canadian dollar exchange rate, serves as natural hedges to the US dollar denominated debt. Therefore, the Company has entered into commodity hedges in US dollars to maintain such natural economic hedges.

Interest Rate Risk

Interest rate risk is the risk that future cash flows will fluctuate as a result of changes in market interest rates. The interest charged on the Revolving Facility fluctuates with the interest rates posted by the lenders. The Company is exposed to interest rate risk related to borrowings are drawn under the Revolving Facility.

A change in prime interest rates by 1% would have changed net loss by approximately \$0.5 million in 2017 (2016 – \$0.1 million) assuming all other variables remain constant.

Commodity Price Risk

Commodity price risk is the risk that the fair value of future cash flows will fluctuate as a result of changes in commodity prices. Commodity prices for oil and natural gas are impacted not only by the relationship between the Canadian and United States dollars but also worldwide economic events that influence supply and demand.

PPR enters into derivative instruments to manage its exposure to commodity price risk caused by fluctuations in commodity prices, which have served to protect and provide certainty on a portion of the Company's cash flows. The following table summarizes commodity derivative transactions as at December 31, 2017:

Crude Oil Commodity Risk Management Contracts						
Commodity Contract	Notional Quantity	Remaining Term	Reference	Weighted Average Price	Contract Type	
Oil	1,200 bbls/d	January 1, 2018 – March 31, 2018	USD\$ WTI	\$ 57.13	Swap	
Oil	1,100 bbls/d	April 1, 2018 – June 30, 2018	USD\$ WTI	\$ 56.63	Swap	
Oil	1,000 bbls/d	July 1, 2018 – September 30, 2018	USD\$ WTI	\$ 55.65	Swap	
Oil	900 bbls/d	October 1, 2018 – December 31, 2018	USD\$ WTI	\$ 54.55	Swap	
Oil	500 bbls/d	January 1, 2018 – December 31, 2018	USD\$ WTI	\$ 65.00	Sold Call Option	
Oil	800 bbls/d	January 1, 2018 – December 31, 2018	CDN\$ WTI	\$ 58.00/ 67.50	Collar	
Oil	600 bbls/d	January 1, 2019 – March 31, 2019	USD\$ WTI	\$ 53.53	Swap	
Oil	250 bbls/d	April 1, 2019 – May 31, 2019	USD\$ WTI	\$ 52.65	Swap	
Oil	325 bbls/d	April 1, 2019 – June 30, 2019	USD\$ WTI	\$ 52.75	Swap	
Oil	500 bbls/d	July 1, 2019 – September 30, 2019	USD\$ WTI	\$ 52.50	Swap	
Oil	450 bbls/d	October 1, 2019 – December 31, 2019	USD\$ WTI	\$ 52.00	Swap	
Oil	400 bbls/d	January 1, 2019 – December 31, 2019	CDN\$ WTI	\$ 85.00	Sold Call Option	
Oil	400 bbls/d	January 1, 2019 – December 31, 2019	USD\$ WTI	\$ 52.50/60.00	Collar	
Oil	275 bbls/d	January 1, 2019 – December 31, 2019	USD\$ WTI	\$ 50.00/57.00	Collar	
Oil	450 bbls/d	January 1, 2020 – March 31, 2020	USD\$ WTI	\$ 51.50	Swap	
Oil	425 bbls/d	April 1, 2020 – June 30, 2020	USD\$ WTI	\$ 51.00	Swap	
Oil	400 bbls/d	July 1, 2020 – September 30, 2020	USD\$ WTI	\$ 50.75	Swap	
Oil	400 bbls/d	October 1, 2020 – December 31, 2020	USD\$ WTI	\$ 50.50	Swap	
Oil	275 bbls/d	January 1, 2020 – December 31, 2020	USD\$ WTI	\$ 60.50	Swap	
Oil	175 bbls/d	January 1, 2020 – December 31, 2020	USD\$ WTI	\$ 49.00/ 54.75	Collar	

Natural Gas Commodity Risk Management Contracts						
Commodity Contract	Notional Quantity	Remaining Term	Reference	Weighted Average Price	Contract Type	
Natural Gas	2,500 GJ/d	January 1, 2018 – March 31, 2018	AECO 7A Monthly Index	\$ 3.12	Swap	
Natural Gas	1,500 GJ/d	January 1, 2018 – December 31, 2018	AECO 7A Monthly Index	\$ 2.76	Swap	
Natural Gas	1,500 GJ/d	January 1, 2018 – December 31, 2018	AECO 7A Monthly Index	\$ 2.76	Sold Call Option	
Natural Gas	3,000 GJ/d	January 1, 2019 – March 31, 2019	AECO 7A Monthly Index	\$ 2.73	Swap	

The following lists the fair value of all derivative contracts by commodity type in place at the following balance sheet dates:

December 31, 2017	Crude Oil	Natural Gas	Total
<i>(\$000s)</i>			
Derivative instruments – current assets	—	895	895
Derivative instruments – current liability	(4,156)	—	(4,156)
Derivative instruments – long-term assets	—	192	192
Derivative instruments – long-term liability	(2,258)	—	(2,258)
Total	(6,414)	1,087	(5,327)

December 31, 2016	Crude Oil	Natural Gas	Total
<i>(\$000s)</i>			
Derivative instruments – current liability	(1,536)	(775)	(2,311)
Derivative instruments – long-term liability	(3,800)	—	(3,800)
Total	(5,336)	(775)	(6,111)

The following shows the breakdown of realized and unrealized gains and losses recognized by commodity type in the fiscal years 2017 and 2016:

Year ended December 31, 2017	Crude Oil	Natural Gas	Total
<i>(\$000s)</i>			
Unrealized gain (loss) on derivative instruments	(1,079)	1,862	783
Realized gain on derivative instruments	3,776	1,150	4,926
Total gain	2,697	3,012	5,709

Year ended December 31, 2016	Crude Oil	Natural Gas	Total
<i>(\$000s)</i>			
Unrealized loss on derivative instruments	(18,499)	(775)	(19,274)
Realized gain on derivative instruments	9,352	391	9,743
Total loss	(9,147)	(384)	(9,531)

An increase of Canadian dollar WTI by \$1.00 per bbl from the expected forward prices as at December 31, 2017 would result in a decrease in the unrealized gain on derivative instruments of approximately \$1.3 million, assuming all other variables, including the Canadian/United States dollar exchange rate, remain constant. An increase of Canadian dollar AECO by \$0.25 per Mcf from the expected forward prices as at December 31, 2017 would result in a decrease in the unrealized gain on derivative instruments of approximately \$0.2 million, assuming all other variables remain constant.

(c) Capital Management

PPR's objectives when managing capital are to maintain a flexible capital structure in order to meet its financial obligations and allow it to execute on its planned capital expenditure program. The Company's long-term goal is to fund current period capital expenditures necessary for the replacement of production declines and decommissioning expenditures using only funds from operations. Value-creating activities may be financed with a combination of funds from operations and other sources of capital. The Company considers its capital structure to include shareholders' equity, the available borrowing under outstanding debt agreements and working capital. PPR intends to manage the capital structure of the Company to provide a strong financial position that is capable of funding the future growth of the Company. The Company monitors its current and forecasted capital structure and makes adjustments on an ongoing basis in order to maintain the liquidity

needed to satisfy its funding requirements. Modifications to PPR's capital structure can be accomplished through issuing common shares, issuing new debt or replacing existing debt, adjusting capital spending and acquiring or disposing of assets.

PPR anticipates its future development to be funded primarily with cash flows from operations, while maintaining a balanced capital structure. PPR monitors its capital structure based on the ratio of total debt to trailing twelve months Adjusted EBITDAX (as defined below). Total debt to Adjusted EBITDAX provides a measure of the Company's ability to manage its debt levels under current operating conditions. The Company's goal is to manage this ratio well within the financial covenants imposed on it under its outstanding debt agreements. Total debt to Adjusted EBITDAX at December 31, 2017 was 2.0 to 1.0 (2016 – 1.2 to 1.0), which was well below the financial covenant requirement of 3.5 to 1.0 under the Revolving Facility. The Company plans to maintain a prudent financial position by actively managing its capital program with careful consideration of the commodity pricing environment to optimize leverage, liquidity and cash flows.

Total debt excludes borrowing drawn from cash collateral against letters of credits. Adjusted EBITDAX corresponds to defined terms in the Company's Revolving Facility Agreement and means net earnings before financing charges, foreign exchange gain (loss), E&E expense, income taxes, depreciation, depletion, amortization, other non-cash items of expense and non-recurring items, adjusted for major acquisitions and material dispositions assuming that such transactions had occurred on the first day of the applicable calculation period. As transaction costs related to the Arrangement and Red Earth Acquisition are non-recurring costs, Adjusted EBITDAX has been calculated, excluding transaction costs, as a meaningful measure of continuing operating cash flows. For purposes of calculating covenants under the credit facility, Adjusted EBITDAX is determined using financial information from the most recent four consecutive fiscal quarters.

The following is a reconciliation of Adjusted EBITDAX to the nearest IFRS measure, net loss before income tax:

	Year Ended December 31,	
(\$000s)	2017	2016
Net loss before income tax	(48,272)	(60,410)
Add (deduct):		
Interest	3,028	730
Depletion and depreciation	34,875	21,344
Exploration and evaluation expense	4,877	58
EBITDAX	(5,492)	(38,278)
Unrealized (gain) loss on derivative instruments	(783)	19,274
Impairment loss	34,177	26,723
Accretion	2,132	12,389
Loss (gain) on foreign exchange	(1,621)	(9,510)
Reorganization costs ¹	—	392
Share-based compensation	687	366
Loss on sale of properties	(853)	73
Gain on business combination	(3,893)	—
Gain on warrant liability	(46)	—
Transaction costs	1,075	2,288
Pro-forma impact of acquisition (note 4)	2,394	3,206
Adjusted EBITDAX	27,777	16,923

¹ Reorganization cost includes share-based compensation related to terminations.

19. KEY MANAGEMENT COMPENSATION

The aggregate payroll expense of directors and executive management is summarized as follows:

<i>Years ended</i> <i>(\$000s)</i>	December 31, 2017	December 31, 2016
Salary, bonus and fees	2,532	2,312
Termination payments	—	628
Share based compensation	499	316
Share based compensation – terminations	—	10
Total remuneration	3,031	3,266

Share based compensation included in key management compensation is non-cash compensation.

20. COMMITMENTS AND CONTINGENCIES

The Company has non-cancellable contractual obligations summarized as follows:

	2018	2019	2020	2021	2022	Thereafter	Total
Debt	4,259	4,364	43,341	26,471	—	—	78,435
Operating Leases – net	1,511	1,680	2,153	2,187	182	—	7,713
Firm transportation agreements	2,271	2,264	114	38	16	—	4,703
Capital commitments	250	23,733	1,000	—	—	—	24,983
Flow-through share commitment	3,665	—	—	—	—	—	3,665
Other agreements	219	188	80	29	30	293	839
Total	12,175	32,229	46,688	28,725	228	293	120,338

Included in ‘Operating Leases – net’ are sublease recoveries in amount of \$1.9 million over the contractual period.

The flow-through share commitment relates to flow-through shares issued by PPR in 2017 and will be met by incurring CEE as defined in the *Income Tax Act* and renouncing the related income tax deductions to investors.

The 2019 capital commitments are pursuant to a lease acquisition agreement as described below. The capital commitments and flow-through share commitment may be fulfilled by the same exploration expenditures. The 2020 capital commitment relates to land acquired in 2017 and is comprised of a four well drilling commitment. The costs included in the schedule about represent estimated drilling costs in the area.

In addition, the Company has estimated future decommissioning liabilities on its interests in wells and facilities in the total amount of \$171.5 million on an undiscounted basis, inflated at 1.7%, of which, \$10.1 million is estimated to be incurred over the next five years.

(a) Lease Acquisition Capital Commitment

Under the lease acquisition capital commitment, the Company had committed to annual capital expenditures for three years ending July 1, 2018 pursuant to the acquisition of approximately 73,500 net undeveloped acres in the Wheatland area. In the fourth quarter of 2017, the agreement was amended whereby certain leases totaling approximately 20,500 acres were surrendered, and the term of remaining leases, along with the related remaining capital commitment were extended to March 31, 2019. Under the amending agreement, the lease term and capital commitment may be further extended to September 30, 2019, should PPR incur at least \$37.5 million of the \$45.0

million total commitment by March 31, 2019. In the event PPR does not incur the minimum capital expenditures by the end of the given commitment period, the shortfall may be payable to the vendor.

As of December 31, 2017, the Company had incurred a total of \$21.3 million towards the total capital commitment of \$45.0 million. PPR expects to fulfill the remaining capital commitment through its capital program at the Wheatland area (see Note 18(b)(ii)).

(b) Contingencies

PPR is involved in litigation and claims arising in the normal course of operations. Such claims are not expected to have a material impact on the Company's results of operations or cash flows.