Consolidated Financial Statements of

ARSENAL ENERGY INC.

Years ended December 31, 2015 and 2014

MANAGEMENT'S REPORT

Management, in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board, has prepared the accompanying consolidated financial statements of Arsenal Energy Inc. (the "Company"). Financial and operating information presented throughout this report is consistent with that shown in the consolidated financial statements. The consolidated financial statements have been prepared in accordance with the accounting policies detailed in the notes thereto.

Management is responsible for the integrity of the financial statements by selecting and training qualified personnel and by ensuring that the organizational structure provides appropriate delegation of authority and segregation and division of responsibilities and authority. Internal control systems are designed and maintained to provide reasonable assurance that assets are safeguarded from loss or unauthorized use and to produce reliable accounting records for financial reporting purposes.

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

The Board of Directors is responsible for ensuring that management fulfills its responsibilities for financial reporting and internal control. The Board exercises this responsibility through the Audit Committee, with assistance from the Reserve Committee regarding the annual evaluation of our petroleum and natural gas reserves. The Audit Committee, which is composed of completely independent directors all of which have financial expertise, meets regularly with management and the independent auditors to ensure that management's responsibilities are properly discharged, to review the consolidated financial statements and recommend that the consolidated financial statements be presented to the Board of Directors for approval. The Audit Committee also considers the independence of the external auditors and reviews their fees. The external auditors have access to the Audit Committee without the presence of management.

"Signed" Tony van Winkoop	*"Signed" J. Paul Lawrence*
President and Chief Executive Officer	Vice President Finance and Chief Financial Officer

March 8, 2016

INDEPENDENT AUDITORS' REPORT

To the Shareholders of Arsenal Energy Inc.

We have audited the accompanying consolidated financial statements of Arsenal Energy Inc. which comprise the consolidated statements of financial position as at December 31, 2015 and December 31, 2014, the consolidated statements of income (loss) and comprehensive income (loss), changes in shareholders' equity and cash flows for the years then ended, and notes, comprising 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 our 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, we 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 consolidated financial position of Arsenal Energy Inc. as at December 31, 2015 and December 31, 2014, and its consolidated financial performance and its consolidated cash flows for the years then ended in accordance with International Financial Reporting Standards.

Emphasis of Matter

Without modifying our opinion, we draw attention to Note 2 (b) in the financial statements which indicates that Arsenal Energy Inc. has material uncertainties relating to liquidity and the ability to meet the terms of the credit facility agreement as at December 31, 2015. These conditions, along with other matters as set forth in Note 2 in the financial statements, indicate the existence of a material uncertainty that may cast significant doubt about Arsenal Energy Inc.'s ability to continue as a going concern.

KPMG LLP

Chartered Professional Accountants

March 8, 2016
Calgary, Canada

Arsenal Energy Inc.

Consolidated Statements of Financial Position
As at December 31,

(thousands of $Cdn)	2015	2014
Assets		
Current assets:		
Cash	$ 2,561	$ 2,573
Accounts receivable (note 11)	5,453	10,553
Inventory	488	570
Risk management contracts (note 11)	-	11,946
Prepaid expenses and deposits	668	649
	9,170	26,291
Reclamation deposit	208	174
Exploration and evaluation assets (note 6)	1,114	3,639
Property, plant and equipment (note 7)	153,641	206,320
	$ 164,133	$ 236,424
Liabilities and Shareholders' Equity		
Current liabilities:		
Accounts payable and accrued liabilities	$ 10,143	$ 16,700
Bank loan (note 8)	15,000	-
Current tax payable	-	522
Current portion of decommissioning obligations (note 9)	300	750
Incentive compensation liability (note 10(b))	79	1,571
Risk management contracts (note 11)	296	57
	25,818	19,600
Bank loan (note 8)	37,464	60,000
Flow-through share premium (note 10(a))	315	1,628
Risk management contracts (note 11)	320	139
Decommissioning obligations (note 9)	40,050	43,979
Deferred taxes (note 13)	4,434	20,386
	108,401	145,732
Shareholders' Equity:		
Common shares (note 10(a))	155,988	151,434
Contributed surplus	11,668	11,388
Accumulated other comprehensive income	9,036	3,182
Deficit	(120,960)	(75,312)
	55,732	90,692
	$ 164,133	$ 236,424

Going concern (note 2(b))
Subsequent event (note 8)
Segmented information (note 15)
Commitments and contingencies (note 16)

Approved by the Board of Directors:

"Signed" R. Neil MacKay
Director and Chairman of the Board of Directors

"Signed" William Hews
Director and Chair of the Audit Committee

The notes are an integral part of these consolidated financial statements.

Arsenal Energy Inc.

Consolidated Statements of Income (Loss) and Comprehensive Income (Loss)
For the years ended December 31,

(thousands of $Cdn, except per share amounts)		**2015**		**2014**
Revenue				
Oil and natural gas	$	55,082	$	117,114
Royalties		(11,501)		(25,317)
Net revenue		43,581		91,797
Realized gain on risk management contracts (note 11)		14,825		1,227
Unrealized gain (loss) on risk management contracts (note 11)		(12,366)		15,654
Net revenue after risk management		46,040		108,678
Expenses				
Operating and transportation		21,893		30,767
General and administrative		4,096		4,026
Exploration and evaluation expenses		3,409		4,010
Depletion and depreciation		26,707		30,853
Exploration and evaluation impairment (note 6)		2,025		5,199
Property, plant and equipment impairment (note 7)		55,816		-
Interest and other financing charges		2,159		2,775
Accretion (note 9)		1,108		1,753
Share-based compensation (recovery) (note 10(b))		(691)		1,797
Loss on sale of property (note 7)		1,467		-
Foreign exchange gain		(6,698)		(2,770)
		111,291		78,410
Income (loss) before income tax		(65,251)		30,268
Provision for (recovery of) income taxes (note 13)				
Current		(168)		969
Deferred		(21,103)		3,658
		(21,271)		4,627
Net income (loss) for the year	**$**	**(43,980)**	**$**	**25,641**
Other comprehensive income				
Translation gain on foreign operations		5,854		2,380
Comprehensive income (loss)	**$**	**(38,126)**	**$**	**28,021**
Net income (loss) per share (note 10(c))				
Basic	$	(2.37)	$	1.55
Diluted	$	(2.37)	$	1.54

The notes are an integral part of these consolidated financial statements.

Arsenal Energy Inc.

Consolidated Statements of Changes in Shareholders' Equity

(thousands)	Number of Shares	Share capital	Contributed surplus	Accumulated other comprehensive income (loss)	Deficit	Total Shareholders' equity
Balance December 31, 2013	16,080	$137,705	$10,940	$802	$(96,575)	$52,872
Net income for the year	-	-	-	-	25,641	25,641
Issue of shares, net of costs and premium	1,712	12,843	-	-	-	12,843
Issued on exercise of options (note 10(b))	101	877	-	-	-	877
Share-based compensation expensed	-	-	395	-	-	395
Repurchase of shares (note 10(d))	(41)	(349)	53	-	-	(296)
Dividends	42	358	-	-	(4,378)	(4,020)
Cancelled on expiration of amalgamation exchange provision	(17)	-	-	-	-	-
Translation gain on foreign operations	-	-	-	2,380	-	2,380
Balance December 31, 2014	17,877	$151,434	$11,388	$3,182	$(75,312)	$90,692
Balance December 31, 2014	17,877	$151,434	$11,388	$3,182	$(75,312)	$90,692
Net loss for the year	-	-	-	-	(43,980)	(43,980)
Issue of shares, net of costs and premium	1,364	3,906	-	-	-	3,906
Issued on vesting of awards (note 10(b))	60	398	(398)	-	-	-
Share-based compensation expensed	-	-	678	-	-	678
Dividends	122	250	-	-	(1,668)	(1,418)
Translation gain on foreign operations	-	-	-	5,854	-	5,854
Balance December 31, 2015	19,423	$155,988	$11,668	$9,036	$(120,960)	$55,732

The notes are an integral part of these consolidated financial statements.

Arsenal Energy Inc.

Consolidated Statements of Cash flows

For the years ended December 31,

(thousands of $Cdn)		**2015**		**2014**
Operating Activities:				
Net income (loss) for the year	$	(43,980)	$	25,641
Items not affecting cash:				
Unrealized (gain) loss on risk management contracts		12,366		(15,654)
Depletion and depreciation		26,707		30,853
Accretion (note 9)		1,108		1,753
Deferred tax expense (recovery)		(21,103)		3,658
Exploration and evaluation impairment (note 6)		2,025		5,199
Property, plant and equipment impairment (note 7)		55,816		-
Share-based compensation expense (recovery) (note 10(b))		(816)		1,797
Unrealized foreign exchange gain		(6,645)		(2,694)
Loss on sale of property		1,467		-
Decommissioning obligations settled (note 9)		(1,587)		(1,987)
Net change in non-cash working capital (note 14)		2,039		(291)
Net cash from operating activities		27,397		48,275
Financing Activities:				
Bank loan payments		(7,908)		(9,100)
Issue of shares, net of share issue costs		4,229		15,025
Dividends paid		(1,418)		(4,020)
Issue of shares on exercise of stock options		-		583
Purchase of put options		-		(343)
Repurchase of shares		-		(296)
Net change in non-cash working capital items (note 14)		(116)		153
Net cash from (used in) financing activities		(5,213)		2,002
Investing Activities:				
Property, plant and equipment		(20,302)		(53,047)
Exploration and evaluation asset expenditures		-		(487)
Acquisition of properties		-		(152)
Disposition of exploration and evaluation asset		500		-
Disposition of property, plant and equipment		1,382		100
Net change in non-cash working capital items (note 14)		(4,195)		4,616
Net cash used in investing activities		(22,615)		(48,970)
Foreign exchange gain on cash held in foreign currency		419		47
Change in cash during the year		(12)		1,354
Cash, beginning of year		2,573		1,219
Cash, end of year	$	2,561	$	2,573
The following are included in cash flow from operating activities:				
Interest paid in cash	$	2,098	$	2,603
Income taxes paid in cash	$	424	$	818

The notes are an integral part of these consolidated financial statements.

1. Reporting entity:

Arsenal Energy Inc. (“Arsenal” or the “Company”) is an oil and gas exploration, development and production Company based in Calgary, Alberta, Canada. The Company conducts its operations in the Western Canadian Sedimentary basin in Canada and the Williston basin in the United States. The consolidated financial statements of the Company as at December 31, 2015 comprise the Company and its wholly owned subsidiaries, Arsenal Energy USA Inc. and Arsenal Energy Holdings Ltd.; which were incorporated in the USA and Canada respectively. Arsenal’s principle place of business is located at Suite 1900, 639 – 5th Avenue SW, Calgary Alberta, Canada, T2P 0M9.

2. Basis of preparation:

(a) Statement of compliance:

These consolidated financial statements have been prepared by management in accordance with International Financial Reporting Standards (“IFRS”) as issued by the International Accounting Standards Board (“IASB”) and were prepared using accounting policies consistent with IFRS.

The consolidated financial statements were authorized for issue by the Board of Directors on March 7, 2016.

(b) Going concern:

The Company’s credit facility is based on the bank’s determination of the Company’s borrowing base utilizing the Company’s risked reserves and the lenders assessment of future commodity prices. The facility was scheduled for review on November 30, 2015 which concluded subsequent to year-end on January 8, 2016. As a result of the review, the Company’s credit facility was reduced to a borrowing base of $40 million and a supplemental facility of $15 million (from $60 million - $55 million extendible facility and $5 million supplemental). The supplemental facility of $15 million has a maturity date of May 26, 2016. The extendible credit facility has a revolving period of 364 days plus one year and therefore has been classified as long-term. On review, the extendible facility can be increased or reduced. If increased it can be utilized to reduce the supplemental facility. If decreased the Company has 60 days to repay any shortfall. The next review of the credit facility is scheduled to be completed by May 26, 2016.

As the Company’s forecast of funds from operations is estimated to be insufficient to fully retire the supplemental facility by the maturity date, the Company has taken steps to sell all or a portion of its US properties and various non-core properties in Canada. In addition, the Company has deferred capital spending and initiated addition reductions in costs and expenses. While these steps have been initiated, there is no certainty that they will be successful, or that the funds generated will be sufficient to reduce the bank debt to an amount the Company can support with its retained assets.

Uncertainties as to the Company’s ability to continue as a going concern exist due to:

- A $15 million scheduled repayment of the supplemental facility on May 26, 2016. The Company does not currently have sufficient funds to repay this amount;
- There is uncertainty as to the determination of the borrowing base that will be provided by the lenders in May 2016;
- There is risk that the Company will not be able to comply with the financial covenant in 2016. Compliance is impacted by the undrawn debt which is at risk. In the event the Company has a covenant violation, this would represent an event of default under the credit facility which could result in all outstanding amounts being payable on demand; and
- The Company is required to expend $2.1 million in 2016 on qualifying expenditures by December 31, 2016 to satisfy the requirements of the flow-through share issuance completed in 2015.

As a result of the above matters, there is a material uncertainty as to the Company’s ability to continue as a going concern.

These consolidated financial statements do not reflect any adjustments to the carrying amounts of the Company's assets, liabilities, revenues, expenses and balance sheet classifications that would be necessary if the going concern assumption is not appropriate. Therefore the Company may be required to realize its assets and discharge its liabilities in other than the normal course of business at amounts different from those reflected in these financial statements.

(c) Basis of measurement:

The consolidated financial statements have been prepared on the historical cost basis except for the derivative financial instruments, short term incentive compensation liability and decommissioning obligations which are measured at fair value. The methods used to measure fair value are discussed in notes 5 and 12.

(d) Functional and presentation currency:

These consolidated financial statements are presented in Canadian dollars, which is the parent company's functional currency. Arsenal's subsidiary Arsenal Energy USA Ltd. has a U.S. dollar functional currency.

(e) Use of estimates, judgments and assumptions:

The preparation of financial statements in conformity with IFRS requires management to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amounts regarding assets, liabilities, revenue, and expenses. Actual results may differ from estimated amounts as future confirming events occur.

Reserve estimates including production profiles, future development costs, and discount rates are a critical part of many of the estimated amounts and calculations contained in the financial statements. These estimates are verified by third party professional engineers, who work with information provided by the Company to establish reserve determinations. These determinations are updated at least on an annual basis.

Significant areas of estimation, uncertainty and critical judgments in applying accounting policies that have the most significant effect on the amount recognized in the consolidated financial statements include:

- Impairment testing – estimates of reserves, future commodity prices, future costs, production profiles, discount rates, market value of land.
- Depletion and depreciation - oil and natural gas reserves, including future prices, costs and reserve base to use on calculation of depletion.
- Decommissioning obligations – estimates relating to amounts, likelihood, timing, inflation and discount rates.
- Long-term incentive compensation – forfeiture rates, volatility and multiplier rate.
- Risk management contracts – expected future oil and natural gas prices and interest rates, and expected volatility in these prices and rates.
- Deferred tax – estimates of reversal of temporary differences, tax rates substantively enacted, and likelihood of assets being realized.
- Determinations of cash generating units ("CGU's").
- Determining the status and viability of exploration and evaluation assets.

3. Significant accounting policies:

The accounting policies set out below have been applied consistently to all periods presented in these consolidated financial statements, and have been applied consistently by the Company and its subsidiaries. Certain comparative amounts have been reclassified to conform with the current year's presentation.

(a) Basis of consolidation:

(i) *Subsidiaries:*
Subsidiaries are entities controlled by the Company. Control exists when the Company has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. In assessing control, potential voting rights that currently are exercisable are taken into account. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases.

(ii) *Jointly controlled operations and jointly controlled assets:*
Many of the Company's oil and natural gas activities involve jointly controlled assets. The consolidated financial statements include the Company's share of these jointly controlled assets and a proportionate share of the relevant revenue and related costs.

(iii) *Transactions eliminated on consolidation:*
Intercompany balances and transactions, and any unrealized income and expenses arising from intercompany transactions, are eliminated in preparing the consolidated financial statements.

(b) Foreign currency:

(i) Transactions in foreign currencies are generally translated to Canadian dollars at the average exchange rate for the period. Monetary assets and liabilities denominated in foreign currencies are translated to Canadian dollars at the period end exchange rate. Foreign currency differences arising on translation are recognized in earnings in the period in which they arise.

(ii) Assets and liabilities of Arsenal's U.S. operations are translated into Canadian dollars at period end exchange rates while revenues and expenses are translated using average rates for the period. Gains and losses from the translation are deferred and included in accumulated other comprehensive income (''AOCI'').

(c) Financial instruments:

(i) Non-derivative financial instruments:

Non-derivative financial instruments comprise account receivable, cash and cash equivalents, bank loans, and accounts payables and accrued liabilities. Non-derivative financial instruments are recognized initially at fair value less, for instruments not at fair value through profit or loss, any directly attributable transaction costs. Subsequent to initial recognition non-derivative financial instruments are measured as described below.

Cash and cash equivalents comprise cash on hand, term deposits held with banks, other short-term highly liquid investments with original maturities of three months or less.

Financial assets at fair value through profit or loss:

An instrument is classified at fair value through profit or loss if it is held for trading or is designated as such upon initial recognition. Financial instruments are designated at fair value through profit or loss if the Company manages such investments and makes purchase and sale decisions based on their fair value in accordance with the Company's risk management or investment strategy. Upon initial recognition attributable transaction costs are recognized in profit or loss when incurred. Financial instruments are measured at fair value and changes therein are recognized in profit or loss.

Other non-derivative financial instruments, such as cash and cash equivalents, accounts receivable, bank loans, accounts payables and accrued liabilities, are measured at amortized cost using the effective interest method, less any impairment losses.

(ii) Derivative financial instruments:

The Company has entered into certain financial derivative contracts in order to manage the exposure to market risks from fluctuations in commodity prices. These instruments are not used for trading or speculative purposes. The Company has not designated its financial derivative contracts as effective accounting hedges, and thus not applied hedge accounting, even though the Company considers all commodity contracts to be economic hedges. As a result, all financial derivative contracts are classified as fair value through profit or loss and are recorded on the balance sheet at fair value. Transaction costs are recognized in earnings when incurred.

The Company accounts for any forward physical delivery sales contracts, which are entered into and continue to be held for the purpose of receipt or delivery of non-financial items in accordance with its expected purchase, sale or usage requirements as executory contracts. As such, these contracts are not considered to be derivative financial instruments and are not recorded at fair value on the balance sheet. Settlements on these physical sales contracts are recognized in oil and natural gas revenue.

Embedded derivatives are separated from the host contract and are accounted for separately if the economic characteristics and risks of the host contract and the embedded derivative are not closely related, a separate instrument with the same terms as the embedded derivative would meet the definition of a derivative, and the combined instrument is not measured at fair value through profit or loss. Changes in the fair value of separable embedded derivatives are recognized immediately in earnings.

(iii) Share capital:

Common shares are classified as equity. Incremental costs directly attributable to the issue of common shares and share options are recognized as a deduction from equity, net of any deferred taxes.

(d) Property, plant and equipment and intangible exploration and evaluation assets:

(i) Recognition and measurement:

Exploration and evaluation expenditures:

Pre-license costs, dry holes, seismic and lease rentals are recognized as operating expenses as incurred.

Exploration and evaluation costs, include costs of land and exploratory drilling and testing, are capitalized as exploration and evaluation assets according to the expenditure. Tangible assets acquired which are consumed in developing an intangible exploration and evaluation asset are recorded as part of the costs of the exploration and evaluation asset.

Exploration and evaluation assets are assessed for impairment if (i) sufficient data exists to determine technical feasibility and commercial viability, and (ii) facts and circumstances suggest that the carrying amount exceeds the recoverable amount. For purposes of impairment testing, exploration and evaluation assets are allocated to cash-generating units.

The technical feasibility and commercial viability is considered to be determinable when proved and or probable reserves are determined to exist. A review 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, exploration and evaluation assets attributable to those reserves are first tested for impairment and then reclassified from exploration and evaluation assets to a separate category within tangible assets referred to as property, plant and equipment.

Development and production costs:

Items of property, plant and equipment, which include oil and gas development and production assets, are measured at cost less accumulated depletion and depreciation and accumulated impairment. Development and production assets are grouped into Cash Generating Units ("CGU's") for impairment testing. When significant parts of an item of property, plant and equipment, including oil and natural gas interests, have different useful lives, they are accounted for as separate items (major components).

Gains and losses on disposal of an item of property, plant and equipment, including oil and natural gas interests, are determined by comparing the proceeds from disposal with the carrying amount of property, plant and equipment and are recognized in profit or loss.

(ii) Subsequent costs:

Costs incurred subsequent to the determination of technical feasibility and commercial viability and the costs of replacing parts of property, plant and equipment are recognized as oil and natural gas interests only when they increase the future economic benefits embodied in the specific asset to which they relate. All other expenditures are recognized in earnings as incurred. Such capitalized oil and natural gas interests generally represent costs incurred in developing proved and/or probable reserves and bringing in or enhancing production from such reserves, and are accumulated on a field or geotechnical area basis. The carrying amount of any replaced or sold component is derecognized. The costs of the periodic servicing of property, plant and equipment are recognized in earnings as incurred.

(iii) Depletion and depreciation:

The net carrying value of development or production assets is depleted using the unit of production method by reference to the ratio of production in the period to the related proved and probable reserves, taking into account estimated future development and decommissioning costs necessary to bring those reserves into production. Future development and decommissioning costs are estimated taking into account the level of development required to produce the reserves. These estimates are reviewed by independent reserve engineers at least annually.

Proved and probable reserves are estimated using independent reserve engineer reports, in accordance with Canadian Securities Regulation National Instrument 51-101, and represent the estimated quantities of crude oil, natural gas and natural gas liquids 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.

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.

The estimated useful lives for certain production assets for the current and comparative years are as follows:

Pipeline facilities	Unit of production
Turnaround and work over costs	Expensed as incurred

For other assets, depreciation is recognized in profit or loss on a straight-line basis over the estimated useful lives of each part of an item of property, plant and equipment.

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. Land is not depreciated.

The estimated useful lives for other assets for the current and comparative years are as follows:

Office equipment	5 years

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

(e) Leased assets:

Leases where the Company assumes substantially all the risks and rewards of ownership are classified as finance leases. Upon initial recognition the leased asset is measured at an amount equal to the lower of its fair value and the present value of the minimum lease payments. Subsequent to initial recognition, the asset is accounted for in accordance with the accounting policy applicable to that asset.

Minimum lease payments made under finance leases are apportioned between the finance expenses and the reduction of the outstanding liability. The finance expenses are allocated to each year during the lease term so as to produce a constant periodic rate of interest on the remaining balance of the liability.

Other leases are operating leases, which are not recognized on the Company’s statement of financial position.

Payments made under operating leases are recognized in earnings on a straight-line basis over the term of the lease. Lease incentives received are recognized as an integral part of the total lease expense, over the term of the lease.

(f) Business combinations:

The acquisition method of accounting is used to account for acquisitions of subsidiaries and assets that meet the definition of a business under IFRS. The cost of an acquisition is measured as the fair value of the assets given, equity instruments issued and liabilities incurred or assumed at the date of exchange. The recognized amount of identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured mostly at fair value at the acquisition date. The excess of the cost of acquisition over the recognized amount of identifiable assets, liabilities and contingent liabilities acquired is recorded as goodwill. If the cost of acquisition is less than the recognized amount of the net assets of the subsidiary acquired, the difference is recognized immediately in earnings.

(g) Inventory:

Crude oil inventory consists of amounts produced and in storage tanks or in transit, and is recorded at the lower of the average cost of production and estimated net realizable value. Net realizable value is the estimated selling price in the normal course of business less applicable selling expenses.

(h) Impairment:

(i) *Financial assets:*

A financial asset is assessed at each reporting date to determine whether there is any objective evidence that it is impaired. A financial asset is considered to be impaired if objective evidence indicates that one or more events have had a negative effect on the estimated future cash flows of that asset.

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

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

All impairment losses are recognized in earnings.

An impairment loss is reversed if the reversal can be related objectively to an event occurring after the impairment loss was recognized. For financial assets measured at amortized cost the reversal is recognized in earnings.

(ii) *Non-financial assets:*

The carrying amounts of the Company's non-financial assets net of decommissioning obligations, other than E&E assets and deferred tax assets, are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists, then the asset's recoverable amount is estimated. E&E assets are assessed for impairment when they are reclassified to property, plant and equipment, as oil and natural gas interests, and also if facts and circumstances suggest that the carrying amount exceeds the recoverable amount.

For the purpose of impairment testing, assets are grouped together into the smallest group of assets that generates cash inflows from continuing use that are largely independent of the cash inflows of other assets or groups of assets. Geological formation, product type, geography and internal management are key factors considered when grouping the Company's oil and natural gas assets into CGU's. The recoverable amount of an asset or a CGU is the greater of its value in use and its fair value less costs to sell.

In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. Value in use is generally computed by reference to the present value of the future cash flows expected to be derived from production of proved and probable reserves.

E&E assets are allocated to related CGU's when they are assessed for impairment, both at the time of any triggering facts and circumstances as well as upon their eventual reclassification to property, plant and equipment.

An impairment loss is recognized if the carrying amount of an asset or its CGU net of decommissioning obligations exceeds its estimated recoverable amount. Impairment losses are recognized in earnings.

An impairment loss in respect of property, plant and equipment and E&E assets recognized in prior years are assessed at each reporting date for any indications that the loss has decreased or no longer exists. An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depletion and depreciation or amortization, if no impairment loss had been recognized.

(i) Share based payments:

The Company has the right, but not the obligation to settle options in cash upon the exercise of options, and, as a result, uses liability accounting for its share options. Obligations are accrued over the vesting period and the share-based compensation liability is remeasured at fair value, which is estimated using the closing price of the Company's common shares at the end of each reporting period. Changes in fair value are recognized in earnings. When options are surrendered for cash, the share-based compensation liability is reduced. When options are exercised for shares, the accrued liability is transferred to share capital.

In 2014 the Company cancelled any further issuances under the stock option plan and initiated the share award incentive plan ("Awards"). The portion of the Awards related to the taxable portion of the payment is recorded as a liability and is estimated using the closing price of the Company's common shares at the end of each reporting period. The portion of the Awards to be settled in common shares of the Company is accounted for as equity settled and is valued at the closing price immediately preceding the time of grant and are not revalued.

In the liability portion the amount of the liability for Awards is adjusted for cancellations and forfeitures. For the equity settled Awards a forfeiture rate is estimated on grant date and is not subsequently adjusted.

(j) Provisions:

Decommissioning obligations:

The Company's activities give rise to dismantling, decommissioning and site disturbance re-mediation activities. A provision is made for the estimated cost of site restoration and capitalized in the relevant asset category.

Decommissioning obligations are measured at the present value of the expected expenditures required to settle the present obligation at the balance sheet date. Subsequent to the initial measurement, the obligation is adjusted at the end of each period to reflect the passage of time and changes in the estimated future cash flows and discount rate underlying the obligation. The increase in the provision due to the passage of time is recognized as finance expense whereas increases/decreases due to changes in the estimated future cash flows and discount rate are capitalized. Actual costs incurred upon settlement of the decommissioning obligations are charged against the provision to the extent the provision was established.

(k) Revenue:

Revenue from the sale of oil and natural gas is recorded when the significant risks and rewards of ownership of the product is transferred to the buyer which is usually when legal title passes to the external party. This is generally at the time the product enters the pipeline.

Royalty income is recognized as it accrues in accordance with the terms of the overriding royalty agreements.

(l) Finance income and expenses:

Finance expense comprises interest expense on borrowings, accretion of the discount on provisions and transaction costs.

Borrowing costs incurred for the construction of qualifying assets are capitalized during the period of time that is required to complete and prepare the assets for their intended use or sale. All other borrowing costs are recognized in profit or loss using the effective interest method.

Finance income is recognized as it accrues in profit or loss, using the effective interest method.

(m) Income tax:

Income tax expense comprises current and deferred tax. Deferred tax expense is recognized in earnings 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 using the balance sheet method, providing for 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 reverse, 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 offset, and they relate to income taxes levied by the same tax authority on the same taxable entity, or on different tax 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.

(n) Per share amounts:

Basic earnings per share is calculated by dividing the profit or loss attributable to common shareholders of the Company by the weighted average number of common shares outstanding during the period. Diluted earnings per share is determined by adjusting the profit or loss attributable to common shareholders and the weighted average number of common shares outstanding for the effects of dilutive instruments such as options and awards granted to employees. The calculation assumes that the proceeds on exercise of options and awards are used to repurchase shares at the current market price.

(o) Flow-through shares:

The resource expenditure deductions for income tax purposes related to exploration and development activities funded by flow-through share arrangements are renounced to investors in accordance with tax legislation. On issuance the premium received on the flow-through shares, being the difference in price over a common share with no tax attributes is recognized on the statement of financial position. As expenditures are incurred the deferred tax liability associated with the renounced tax deductions are recognized through profit and loss along with a pro-rata portion of the deferred premium.

4. Future accounting policies:

(a) IFRS 15 – Revenue from Contracts and Customers

The standard contains a single model that applies to contracts with customers and two approaches to recognising revenue: at a point in time or over time. The Company intends to adopt IFRS 15 in its financial statements for the annual period beginning on January 1, 2017. The Company does not expect the standard to have a material impact on its consolidated financial statements.

(b) IFRS 9 – Financial Instruments

IFRS 9 (2014) introduces new requirements for the classification and measurement of financial assets. Under IFRS 9 (2014), financial assets are classified and measured based on the business model in which they are held and the characteristics of their contractual cash flows.

The standard introduces additional changes relating to financial liabilities. It also amends the impairment model by introducing a new 'expected credit loss' model for calculating impairments. IFRS 9 (2014) also includes a new general hedge accounting standard which aligns hedge accounting more closely with risk management. This new standard does not fundamentally change the types of hedging relationships or the requirement to measure and recognize ineffectiveness, however it will provide more hedging strategies that are used for risk management to qualify for hedge accounting and introduce more judgment to assess the effectiveness of a hedging relationship. Special transitional requirements have been set for the application of the new general hedging model. The Company is currently evaluating the impact of adopting IFRS 9 on its consolidated financial statements.

(c) IFRS 16 - Leases

IFRS 16, which replaces IFRS 17, Leases, is effective for annual periods beginning on or after January 1, 2019. Early adoption is permitted provided IFRS 15, Revenue from Contracts and Customers, has been applied or is applied at the same time. The Company is currently evaluating the impact of adopting IFRS 16 on its consolidated financial statements.

5. Determination of fair values:

A number of the Company's accounting policies and disclosures require the determination of fair value, for both financial and non-financial assets and liabilities. Fair values have been determined for measurement and/or disclosure purposes based on the following methods. When applicable, further information about the assumptions made in determining fair values is disclosed in the notes specific to that asset or liability.

(i) Property, plant and equipment and exploration and evaluation assets:

The fair value of property, plant and equipment recognized in a business combination, is based on fair values. The fair value of property, plant and equipment is the estimated amount for which property, plant and equipment could be exchanged on the acquisition date between a willing buyer and a willing seller in an arm's length transaction after proper marketing wherein the parties had each acted knowledgeably, prudently and without compulsion. The fair value of oil and natural gas interests (included in property, plant and equipment) and exploration and evaluation assets is estimated with reference to the discounted cash flows expected to be derived from oil and natural gas production based on externally prepared reserve reports. The risk-adjusted discount rate is specific to the asset with reference to general market conditions.

(ii) Cash and cash equivalents, accounts receivables, bank loans and accounts payables:

The fair value of cash and cash equivalents, accounts receivables, bank loans and accounts payable is estimated as the present value of future cash flows, discounted at the market rate of interest at the reporting date. At December 31, 2015 and December 31, 2014, the fair value of these balances approximated their carrying value due to their short term to maturity. Bank loans bear a floating rate of interest therefore carrying value approximates fair value.

(iii) Derivatives:

The fair value of forward contracts and swaps is determined by discounting the difference between the contracted prices and published forward price curves as at the statement of financial position date, using the remaining contracted oil and natural gas volumes and a risk-free interest rate (based on published government rates). The fair value of options and costless collars is based on option models that use published information with respect to volatility, prices and interest rates.

(iv) Stock options:

The fair value of employee stock options and share awards classified as a liability are measured using a fair value based on the closing share price of the Company at the reporting date. The fair value of share awards classified as equity are measured at the share price immediately prior to the date of issue of the share awards.

6. Exploration and evaluation assets:

Cost or deemed cost		Total
Balance at December 31, 2013	$	10,259
Additions		487
Impairment		(5,199)
Transfer to property, plant and equipment		(1,908)
Balance at December 31, 2014	$	3,639
Divestitures		(500)
Impairment		(2,025)
Balance at December 31, 2015	$	1,114

The Company's exploration and evaluation assets are located in Canada.

At September 30, 2015 the Company recognized an impairment of $1.2 million related to exploratory lands in the Columbia area. At December 31, 2015, due to further declines in land and commodity prices, the Company determined that development of exploratory lands other than Princess would be curtailed. Accordingly the Company further impaired exploratory assets in the Columbia and Provost areas totaling $844,000.

The $1.1 million remaining in exploration and evaluation assets is for undeveloped land in the Princess area.

7. Property, plant and equipment:

Cost or deemed cost		Total
Balance at December 31, 2013	$	255,778
Additions (including capitalized G&A of $860,000)		52,187
Capitalized general and administration		860
Acquisitions		152
Transfer from exploration and evaluation assets		1,908
Divestitures		(259)
Decommissioning obligations acquired and incurred		646
Change in decommissioning obligations		7,601
Foreign currency translation		10,520
Balance at December 31, 2014	$	329,393
Additions		19,587
Capitalized general and administration		715
Divestitures		(4,931)
Decommissioning obligations incurred		619
Change in decommissioning obligations		(5,328)
Foreign currency translation		27,429
Balance at December 31, 2015	$	367,484

Accumulated depreciation		Total
Balance at December 31, 2013	$	89,116
Depletion and depreciation provision		31,003
Divestitures		(100)
Foreign currency translation		3,054
Balance at December 31, 2014	$	123,073
Depletion and depreciation provision		26,632
Divestitures		(1,620)
Impairment		55,816
Foreign currency translation		9,942
Balance at December 31, 2015	$	213,843

NBV		Total
Balance, at December 31, 2014	$	206,320
Balance, at December 31, 2015	$	153,641

The calculation of depletion for the year ended December 31, 2015 included estimated future development and decommissioning costs of $100.4 million (December 31, 2014 - $100.3 million) associated with the development and decommissioning of the Company's proved plus probable reserves and excludes salvage value of $8.6 million (December 31, 2014 - $8.4 million).

During 2015, the Company disposed of certain non-core properties for proceeds of $1.4 million resulting in a loss on disposition of $1.5 million.

Impairment loss:

As a result of a significant decline in the price of oil and gas commodities during 2015, The Company determined that indicators of impairment were evident and, accordingly, impairment calculations were required at both September 30, 2015 and December 31, 2015.

The Company recognized impairments of $20.2 million at September 30, 2015 based on a value in use model utilizing discount rates ranging from 10% to 15% on proved plus probable reserves. The impairment tests conducted at December 31, 2015 was based on a value in use model, with the exception of the Desan CGU, at a 15% discount rate applied to proved developed producing reserves, and a discount rate of 20% to proved undeveloped and probable reserves. This resulted in a further impairment of $35.6 million at December 31, 2015 and a total impairment of $55.8 million for the year then ended. The Company believes that the current price structures and the possibility of restricted access to necessary development capital may constrain the ability of the Company to allocate proper funds to the development of its resources.

The application of the impairment tests resulted in the following impairments:

- For the U.S. CGU, located in the Northwestern portion of North Dakota, USA, the Company recorded impairments of $15.0 million ($11.2 million US) at September 30, 2015 and $30.4 million ($22.0 million U.S.) at December 31, 2015. The recoverable amount of this CGU was $55.8 million ($40.3 million U.S.) at December 31, 2015.
- For the Medium Oil CGU, primarily in the Princess and Provost areas of Alberta, the Company recorded impairments of $4.2 million at September 30, 2015 and $3.9 million at December 31, 2015. The recoverable amount of this CGU was $53.8 million at December 31, 2015.
- For the Gas CGU, primarily in Central Eastern areas of Alberta, the Company recorded impairments of $1.0 million at September 30, 2015 and $271,000 at December 31, 2015. The recoverable amount of this CGU was effectively nil at December 31, 2015.
- For the Heavy Oil CGU, located near the Lloydminister area of Saskatchewan, the Company recorded no impairment at September 30, 2015 and an impairment of $23,000 at December 31, 2015. The recoverable amount of the CGU was effectively nil at December 31, 2015.

- For the Desan CGU, located in the Northeastern area of British Columbia, the Company recorded no impairment at September 30, 2015 and an impairment of $1.0 million at December 31, 2015. The recoverable amount of the Desan CGU of $1.0 million was based on a fair value less costs of disposal at December 31, 2015. The fair value is based on a Level 1 input, being a quoted price for this area.
- There were no impairments for the Evi CGU, located in Northern Alberta.

The value in use models at December 31, 2015 were based on reserve values and pricing as utilized in the independently evaluated reserve report. Commodity pricing utilized in preparation of the reserve report and the impairment tests were as follows:

Year	WTI oil (U.S. $/bbl)	Foreign exchange rate (U.S.$/Cdn$)	Bow River 25 Deg. API Hardisty Cdn$/bbl	Alberta AECO Cdn$/mcf
2016	42.00	0.74	38.35	2.45
2017	48.45	0.77	44.35	2.85
2018	57.20	0.80	52.80	3.10
2019	66.35	0.80	63.85	3.40
2020	75.75	0.80	75.25	3.75
2021	82.80	0.80	83.65	4.15
2022	90.10	0.80	92.35	4.40
2023	91.90	0.80	94.20	4.55
2024	93.75	0.80	96.10	4.90
2025	95.60	0.80	98.00	5.15
Thereafter	+2.0%/year	0.80	+2.0%/year	+2.0%/year

At December 31, 2014, there were no impairments recorded.

8. Bank loan:

At December 31, 2014 the Company's credit facility consisted of an extendible credit facility of $90 million. In May, 2015 the credit facility was reviewed and revised to provide, to the maximum, an extendible credit of $55 million and a supplemental facility ("Supplemental") of $15 million. The Company utilized $12 million of the Supplemental. The revised agreement provided for a semi-annual redetermination of the borrowing base by November 30th. At November 30th the Company had reduced the outstanding balance of the Supplemental to $5 million.

At December 31, 2015, debt under the credit facility amounted to $52.4 million (December 31, 2014 – $60.0 million). As at December 31, 2015 the debt under the extendible facility was $47.4 million and under the Supplemental was $5.0 million.

The semi-annual redetermination date, due by November 30, 2015, was extended and completed subsequent to the year end on January 8, 2016. The credit agreement was amended to reduce the extendible facility to $40 million and adjusted the Supplemental to $15 million, for a total available credit facility of $55 million. The amending agreement placed a restriction on distributions of the Company without the pre-approval of the lenders. On January 8, 2016 the Company increased its Supplemental to $15 million. The Supplemental has a maturity date of May 26, 2016 and accordingly has been classified as a current liability.

The extendible credit facility has a revolving period of 364 days and is extendible annually at the option of the lenders for a further 364 days. If the extendible facility is increased it can be utilized to reduce the Supplemental, if it is reduced the Company has 60 days to repay the shortfall, if any. If the facility is not extended, the amount outstanding under the credit facility will automatically convert to a one year non-revolving term loan and all obligations under the credit facility shall be repaid or paid at the end of the one year period.

Under the Company's extendible credit facility the rates for bankers' acceptances and Libor's are subject to additional stamping fees from 2.00% to 4.50% and prime, U.S. based and operating loans are subject to margins from 1.00% to 3.50% over the Lender's base rate. The stamping fees and margins for the

Supplemental are at a rate of 2.00% higher than the corresponding rate for the extendible facility. The stamping fees and margins are dependent on the debt to cash flow ratio, as defined, and as calculated based on the Company's two most recent quarter ends.

The credit facility is secured by an unlimited liability guarantee to the lenders, an ISDA Master Agreement, a demand debenture in the amount of $300 million granting a first priority security interest over all present and after acquired personal property and a first floating charge over all present and after acquired petroleum and natural gas interests and mortgages creating specific fixed charges on some of the oil and gas properties of the Company in North Dakota. The credit facility is also subject to certain positive and negative covenants including a covenant not to dispose of assets or property having an aggregate fair value exceeding 5% of the borrowing base without the review of the borrowing base and to not make distributions, as defined in the agreement, without the prior written consent of the lenders. The credit facility is subject to a semi-annual borrowing base review based on an independent reserve evaluation in May and on an internally generated engineering evaluation and operational update in November or in the event of a material adverse effect.

At December 31, 2015 there were $5.0 million of US dollar ($6.9 million Canadian $ equivalent) denominated borrowings under the extendible credit facility (December 31, 2014 – nil).

The Company's credit facility has a financial covenant that, without the written consent of the lenders, would result in a breach of the agreement. The Company cannot permit:

> The adjusted working capital ratio (as defined in the agreement to include the unutilized portion of the extendible facility and to exclude the value of any risk management contracts) to fall to below 1:1.

At December 31, 2015, the Company's adjusted working capital ratio was 1.11:1.

9. Decommissioning obligations:

	Year ended December 31, 2015	Year ended December 31, 2014
Beginning of year	$ 44,729	$ 36,321
Obligations settled	(1,587)	(1,987)
Obligations disposed	(462)	(36)
Obligations incurred	619	646
Change in estimates	(5,328)	7,601
Foreign currency translation	1,271	431
Accretion expense	1,108	1,753
End of year	$ 40,350	$ 44,729

Expected to be incurred within one year	$ 300	$ 750
Expected to be incurred beyond one year	$ 40,050	$ 43,979

The Company's decommissioning obligations result from its ownership interest in oil and natural gas assets including well sites, facilities and gathering systems. The total decommissioning obligations are estimated based on the Company's net ownership interest in all wells, facilities and pipelines, estimated costs to reclaim and abandon these wells, facilities and pipelines and the estimated timing of the costs to be incurred in future years. The Company has used an inflation rate of 1.5% (2014 – 1.5%) and a discount factor, being the risk free rate related to the liability, of 2.5% (2014 – 2.5%).

The change in estimates in 2015 is due primarily to a reduction in the estimated costs of decommissioning. The Company has estimated the net present value of the decommissioning obligations to be $40.3 million as at December 31, 2015 (December 31, 2014 - $44.7 million) based on an undiscounted inflation adjusted total future liability of $59.4 million (December 31, 2014 - $65.2 million).

10. Share capital:

At December 31, 2015, the Company was authorized to issue an unlimited number of common shares with the holders of common shares being entitled to one vote per share.

(a) Issued:

	Year ended December 31, 2015		Year ended December 31, 2014	
	Number of Shares	Share capital	Number of Shares	Share Capital
Balance, beginning of year	17,877	$151,434	16,080	$137,705
Issue of shares, net of costs and premium	1,364	3,906	1,712	12,843
Issued on exercise of options	-	-	101	877
Issued on vesting of share awards	60	398	-	-
Issued on share dividend	122	250	42	358
Repurchase of shares	-	-	(41)	(349)
Cancelled on expiration of exchange provision	-	-	(17)	-
Balance, end of year	19,423	$155,988	17,877	$151,434

Common shares

On July 3, 2014, the Company completed a bought deal financing and issued 799,400 flow-through common shares at $9.35 per flow-through share for gross proceeds of $7.5 million and on December 8, 2014, the Company completed a bought deal financing and issued 912,950 flow-through common shares at $9.95 per flow-through share for gross proceeds of $9.1 million. Share issue costs for these deals were $1.5 million and the flow-through share premiums recognized were $2.2 million.

On July 14, 2015, the Company completed a private placement bought deal financing and issued 778,460 common shares at $3.15 per share and 585,700 flow-through common shares at $3.70 per flow-through share for gross proceeds of $4.6 million. Share issue costs for this deal were $391,000 and the flow-through share premium recognized was $322,000.

Dividends

During the year ended December 31, 2015, the Company declared quarterly dividends totaling $0.09 per share that resulted in cash dividend payments of $1.4 million and share dividends of $250,000. As at December 31, 2015, there were no dividends payable to shareholders (December 31, 2014 - $ nil).

The Company suspended further dividend payments in January 2016.

(b) Share based payments:

Share award incentive plan

During 2014 the Company implemented a share award incentive plan and discontinued any further grants under the option plan. Under the share award incentive plan the Company may issue restricted awards and/or performance awards to participants to a maximum of 4.5% of the Company's issued and outstanding common shares.

Restricted awards entitle the participant to one common share of the Company for each restricted award issued. Performance awards entitle the participant to common shares of the Company based on a payout multiplier based on pre-determined corporate performance measures of from 0 to 2 times the number of performance awards issued. For purposes of stock-based compensation a forfeiture rate of 5% on all awards and a payout multiplier of 1.0 for the performance awards were utilized.

Awards vest one-third annually on each of the first, second and third anniversaries from the date of grant. All awards are adjusted to include dividends from the date of grant to the date of vesting. The Company has the option of settling the notional value of the common shares underlying the award by payment in common shares issued from treasury or by payment in cash. The Company has determined that a portion of the settlement will be in cash and a portion of the settlement will be in common shares. The cash portion of these awards is accounted for as a liability and the common share component of these awards has been accounted for as equity.

The share award incentives are summarized in the following table:

Share awards	Number of Restricted Awards	Number of Performance Awards	Total Share Awards
Balance at December 31, 2013	-	-	-
Granted	127	115	242
Balance at December 31, 2014	127	115	242
Granted	124	117	241
Adjustment for dividends	1	1	2
Adjustment for performance factor	-	20	20
Vested and converted to common shares	(25)	(35)	(60)
Vested and paid in cash	(16)	(21)	(37)
Cancelled or forfeited	(22)	(22)	(44)
Balance at December 31, 2015	189	175	364

Share awards vest over the following years:

2016	75	70	145
2017	75	69	144
2018	39	36	75
Total	189	175	364

Stock option plan

The Company had a stock option plan under which the Company granted options to its directors, officers, employees and. The exercise price of each option granted was not less than the market price of the Company's common shares on the date the option was granted and the contractual term of each option did not exceed five years. The stock option plan was discontinued with the implementation of the share award incentive plan.

The following table summarizes changes in options outstanding under the Company's stock option plan:

	Number of options	Weighted average exercise price
Balance, December 31, 2013	1,268	$ 6.41
Exercised	(101)	5.76
Cash settled	(148)	5.48
Cancelled/forfeited	(5)	5.89
Balance, December 31, 2014	1,014	$ 6.61
Cancelled or forfeited	(396)	8.02
Balance, December 31, 2015	618	$ 5.70

The following table summarizes information about the stock options outstanding and exercisable at December 31, 2015:

	Options outstanding			Options exercisable	
Range of exercise prices	Number of options	Weighted average exercise price	Weighted average remaining life (years)	Number of options	Weighted average exercise price
$4.00 to $6.00	310	$ 4.31	2.15	230	$ 4.41
$6.01 to $8.00	258	6.54	0.51	258	6.54
$8.01 to $10.00	50	10.00	0.03	50	10.00
Total	618	$ 5.70	1.29	538	$ 5.95

As a result of the conversion of the option plan from an equity settled plan to a cash settled plan, the obligation associated with the cash settled vested options is recorded as a liability. The fair value of the liability is measured at the reporting date using the fair value based on the closing price of the Company's common shares at December 31, 2015 of $1.22 (2014 - $6.77).

(c) Income (loss) per share:

The following table shows the weighted average number of common and diluted shares.

	Year ended December 31, 2015	Year ended December 31, 2014
Income (loss) per share:		
Basic	$ (2.37)	$ 1.55
Diluted	$ (2.37)	$ 1.54
Weighted average shares outstanding:		
Basic	18,591	16,565
Diluted	18,591	16,959

In computing diluted loss per share for the year ended December 31, 2015, 982,000 (2014- 1.0 million) options and share awards were excluded from the dilution calculations as they were anti-dilutive.

(d) Normal course issuer bid:

On March 27, 2014, the Company announced its intention to make a normal course issuer bid ("NCIB") that commenced April 1, 2014 and ended March 31, 2015. To December 31, 2014, the Company purchased and cancelled 40,900 common shares at a cost of $296,164 or $7.24 per share plus expenses. The stated value of these shares exceeded the cost by $52,953 and was recorded to contributed surplus.

For the year ended December 31, 2015 there was no acquisition of common shares under the NCIB.

11. Risk management and financial instruments:

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

- market risk
- credit risk
- liquidity risk

The Board of Directors oversees managements' 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.

(a) Market Risk:

Foreign currency exchange rate risk

Foreign currency exchange rate risk is the risk that the fair value of future cash flows will fluctuate as a result of changes in foreign exchange rates. Canadian commodity prices are influenced by fluctuations in the Canadian to U.S. dollar exchange rate. As at December 31, 2015, the Company does not have any foreign currency exchange contracts in place. A $0.01 change in the CAD/US dollar exchange rate is estimated to result in a change to the 2015 net income by approximately $85,000 (2014 - $369,000).

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 Company is exposed to interest rate fluctuations on its bank loan which bears a floating rate of interest. Average bank debt outstanding during the year ended December 31, 2015 was $52.6 million (2014 - $71.6 million). For the year ended December 31, 2015, a 1.0 percent change to the effective interest rate, exclusive of the effect of the interest rate swap, would have a $526,000 impact on net income (2014 - $716,000).

The Company has attempted to mitigate the impact of future fluctuations in interest rates on its outstanding bank borrowings through an existing swap contract fixing the base interest rate on banker's acceptance borrowings ("BA's") as outlined below. In 2015 the Company entered into a swap contract fixing the base interest rate which expires in 2018. For the year ended December 31, 2015, the Company recorded a realized interest rate hedging loss of $232,000 (2014 - $55,000 loss) and an unrealized interest rate loss of $420,000 (2014 - $141,000).

Subject of Contract	Remaining Term	National Quantity	Reference	Strike Price	Option Traded	Fair Value
30 day BA rate	January 1, 2016 – February 13, 2018	$30,000,000	CAD- – BA- – CDOR	1.80%	Swap	(616)

Commodity price risk

Commodity price risk is the risk that future cash flows will fluctuate as a result of changes in commodity prices. Commodity prices for petroleum and natural gas are impacted by the relationship between the Canadian and U.S. dollar as well as global economic events that dictate the levels of supply and demand. The Company has attempted to mitigate a portion of the commodity price risk through the use of commodity price contracts.

During the year ended December 31, 2015 the Company monetized crude oil risk management contracts for proceeds of $15.1 million.

As at December 31, 2015, the Company had no commodity risk management contracts in-place.

Fair market value of risk management contracts

The summary of the total fair market value of risk management contracts is:

(thousands $Cdn.)	December 31, 2015	December 31, 2014
Total fair value consists of the following:		
Fair value, end of year – current portion	$ (296)	$ 11,889
Fair value, end of year – long-term portion	(320)	(139)
Total fair value, end of year	$ (616)	$ 11,750

The following table reconciles the changes in the fair value of risk management contracts:

(thousands $Cdn.)	December 31, 2015	December 31, 2014
Fair value, beginning of year	$ 11,750	$ (3,903)
Changes in fair value	2,459	16,878
Settlement received	(14,825)	(1,225)
Fair value, end of year	$ (616)	$ 11,750

Offsetting financial assets and liabilities:

The Company may offset assets and liabilities related to risk management contracts and present the net amount in the Statements of Financial Position when the Company has a legal right to offset the amounts and intends to settle them on a net basis. The assets and liabilities related to risk management contracts in these financial statements are shown at their gross values. The following table shows the Company's gross risk management assets and liabilities:

	December 31, 2015	December 31, 2014
Current Asset	$ -	$ 11,946
Current Liability	(296)	(57)
Long-Term Liability	(320)	(139)
Net Risk Management Asset (Liability)	$ (616)	$ 11,750

Fair value of financial instruments:

The Company's exposure under its financial instruments is limited to financial assets and liabilities, all of which are included in these financial statements. Financial instruments include cash, accounts receivable, accounts payable and accrued liabilities, risk management contracts and bank debt. The fair values of financial assets and liabilities that are included in the balance sheet approximate their carrying amounts. Certain of these financial instruments including risk management contracts are measured in the financial statements at fair value. These financial instruments require disclosure about how fair value was determined based on significant levels of inputs described in the following hierarchy:

Level 1: Quoted prices are available in active markets for identical assets or liabilities as of the reporting date. Active markets are those in which transactions occur in sufficient frequency and value to provide pricing information on an ongoing basis.

Level 2 Pricing inputs are other than quoted prices in active markets included in Level 1. Prices in Level 2 are either directly or indirectly observable as of the reporting date. Level 2 valuations are based on inputs including quoted forward prices for commodities, time value and volatility factors, which can be substantially observed or corroborated in the marketplace.

Level 3: Valuations in this level are those with inputs for the asset or liability that are not based on observable market data.

Risk management assets and liabilities are recorded at their estimated fair value based on the difference between the contracted price and the period end forward price for the same commodity, using quoted market prices (Level 2).

(b) Credit risk:

Credit risk is the risk of financial loss to the Company if a customer or counterparty to a financial instrument fails to meets its contractual obligations, and arises principally from the Company's receivables from joint interest partners and petroleum and natural gas marketers. The maximum exposure to credit risk at year end is as follows:

	December 31, 2015	December 31, 2014
Accounts and other receivables	$5,453	$ 10,553

A substantial portion of the Company's accounts receivable are with marketers, customers and joint interest partners in the oil and gas industry and are subject to normal market and industry credit risks.

As at December 31, 2015 the Company's receivables consisted of $2.6 million (2014 - $2.7 million) from joint interest partners the majority of which has either been collected or is expected to be collected within 60 days, $2.8 million (2014 - $5.8 million) of receivables from petroleum and natural gas marketers, which have been collected and $nil (2014 - $2.1 million) of receivables related to commodity hedge contracts. At December 31, 2015, Arsenal had approximately $0.2 million (2014 - $0.5 million) of receivables that are considered past due and collection efforts, including the taking of production and consideration and taking of legal action have commenced.

Receivables from petroleum and natural gas marketers are normally collected on the 20th day of the month following production in the U.S. and on the 25th day of the month following production in Canada. The Company's policy is to mitigate credit risk associated with these balances by establishing marketing relationships with large creditworthy purchasers. The Company historically has not experienced any collection issues with its petroleum and natural gas marketers. The Company currently transacts its risk management contracts with major financial institutions. Payments under these contracts are typically remitted on the 13th day of the month following. Joint interest receivables are typically collected within one to three months of the joint interest bill being issued to the partner. The Company attempts to mitigate the risk from joint interest receivables by obtaining partner approval of significant capital expenditures and payment of cash advances prior to expenditures. However, the receivables are from participants in the petroleum and natural gas sector, and collection of the outstanding balances are dependent on industry factors such as commodity price fluctuations, costs and the risk of unsuccessful drilling. In addition, further risk exists with joint interest partners as disagreements occasionally arise that increase the potential for non-collection. The Company does not typically obtain collateral from petroleum and natural gas marketers or joint interest partners; however the Company does have the ability to request deposits and to withhold production from joint interest partners in the event of non-payment.

(c) Liquidity risk:

Liquidity risk is the risk that the Company will encounter difficulty in meeting obligations associated with its financial liabilities. The Company's financial liabilities consist of accounts payable, financial instruments and the bank loan. Accounts payable consists of invoices payable to trade suppliers for office, field operating activities and capital expenditures. The Company processes invoices within a normal payment period of approximately 45 days. The Company maintains a revolving credit facility, as outlined in note 8, that is based on proved and producing reserves and is subject to review semi-annually by the lenders. The Company also maintains and monitors a certain level of cash flow which is used to partially finance all operating expenses, capital expenditures and the payment of dividends. The level of cash flow is updated regularly for updated forward strip prices and decisions on the future use of capital are adjusted to reflect changes in the commodity prices and the costs of operations, exploration and development. See further discussions in note 2(b).

12. Capital management:

The Company considers its capital structure to include working capital, its credit facility and shareholders' equity. The Company manages its capital base primarily on its net debt to annualized funds from operations ratio and its net debt to equity ratio. The Company continually monitors, through its annual budgeting and quarterly forecasting process, evaluates the risk reward profile of its exploration program and the economic returns of its development projects, its production profile and the economic indicators in the market including commodity prices, interest rates and foreign exchange rates. It then determines increases or decreases to its capital budget and what, if any, additional initiatives may need to be implemented.

Net debt includes bank borrowings, plus or minus working capital and excludes long term decommissioning obligations and risk management contracts (whether current or long term and whether an asset or an obligation). Annualized funds from operations is calculated as net cash from operating activities, before changes in non-cash working capital, decommissioning obligations settled, exploration and evaluation expenses and transaction costs from the Company's most recent quarter multiplied by four. The annualized funds from operations is further adjusted, if required, for large one-time items included in the recent quarter and significant forecasted changes to production and commodity prices.

At December 31, 2015 the Company's net debt to annualized funds from operations ratio is 5.32:1 and the net debt to equity ratio is 0.97: 1. These ratios are unacceptable and unsustainable and must be reduced through higher prices or lowering debt. Equity markets may be available to reduce debt but the dilution to existing shareholders would be significant. See further discussions in note 2(b).

The following table summarizes the Company's capital position:

Net debt		2015		2014
Cash	$	2,561	$	2,573
Accounts receivable, prepaids and inventory		6,609		11,772
Accounts payable and other liabilities [1]		(10,522)		(19,543)
Adjusted working capital deficiency [1]		(1,352)		(5,198)
Bank loan		(52,464)		(60,000)
Net debt [5]		(53,816)		(65,198)
Annualized funds from operations [2,3,4]	$	10,123	$	55,127
Net debt to annualized funds from operations ratio [6]		5.32		1.18
Shareholders' equity	$	55,732	$	90,692
Net debt to equity		0.97		0.72

1 Excludes the value of risk management contracts and the current portion of the bank loan.
2 Excludes exploration and evaluation expenses.
3 Based on the last quarter's funds from operations annualized.
4 Management uses funds from operations before changes in non-cash working capital and annualized funds from operations to analyze operating performance and leverage. Funds from operations as presented does not have any standardized meaning prescribed by IFRS and therefore it may not be comparable to the calculation of similar measures for other entities. Funds from operations as presented is not intended to represent operating cash flow or operating profits for the period nor should it be viewed as an alternative to cash flow provided by operating activities, net earnings or loss or other measures of financial performance calculated in accordance with IFRS.
5 Net debt is used by Management to analyze leverage. Net debt does not have any standardized meaning prescribed by IFRS and therefore these terms may not be comparable with the calculation of similar measures for other entities.

13. Income tax expense:

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

		2015		2014
Income (loss) before income tax	$	(65,251)	$	30,268
Combined federal and provincial tax rate		26.0%		25.0%
Expected tax provision		(16,965)		7,576
Increase (decrease) in taxes resulting from:				
Tax impact of foreign jurisdictions		(5,793)		1,437
Effect of alternative minimum tax		(158)		1,303
Share based compensation		(190)		450
Flow through shares		2,616		678
Rate change		(569)		(529)
Premium adjustment on flow through shares		(1,635)		(487)
Other		(362)		(671)
Unrecognized tax benefits		1,785		(5,130)
	$	(21,271)	$	4,627

For the year ended December 31, 2015, the Company has recorded income tax recovery of $21.3 million (December 31, 2014 expense of $4.6 million). In the US, the Company has recorded an income tax recovery of $19.6 million (December 31, 2014 expense of $5.2 million) of which a recovery of $158,000 (December 31, 2014 expense of $1.0 million) relates to Alternate Minimum Tax ("AMT" see below). In Canada, the Company has recorded income tax recovery of $1.6 million which represents a reduction of the flow through share premium (December 31, 2014 - $591,000).

The AMT attempts to ensure that corporations that benefit from certain deductions (such as intangible drilling costs, accelerated depreciation and non-capital losses) pay at least a minimum tax. In calculating the AMT, these deductions are reduced from the amounts allowed under the calculation of regular income tax. The tax credit for AMT payments can be used to offset future regular income tax liability. The Company does not recognize any asset related to the potential future recovery of AMT.

The components of the deferred income tax asset and liability are as follows:

	December 31, 2015	
	Canadian Operations	US Operations
Deferred tax assets:		
Non-capital losses	$ -	$ 11,915
Decommissioning obligation	8,446	2,568
Deferred tax liabilities:		
Property, plant and equipment	(6,616)	(18,853)
Other	(1,830)	(64)
	$ -	$ (4,434)

	December 31, 2014	
	Canadian Operations	US Operations
Deferred tax assets:		
Non-capital losses	$ 464	$ 9,371
Decommissioning obligation	9,506	2,480
Other	666	-
Deferred tax liabilities:		
Property, plant and equipment	(7,698)	(32,160)
Unrealized hedging gain	(2,938)	-
Other	-	(77)
	$ -	$ (20,386)

The Company's assets have a tax basis of $129.6 million at December 31, 2015 (December 31, 2014 - $141.0 million) available for deduction against future taxable income. The non-capital loss carry forwards in Canada of $13.7 million (December 31, 2014 - $18.5 million) expire between 2025 and 2032. The following table summarizes the estimated tax pools:

	December 31, 2015	
	Canada	US
Cumulative Canadian Oil and Gas Property Expense	$ 27,060	$ -
Cumulative Canadian Development Expense	15,527	-
Undepreciated Capital Cost	24,044	11,579
Share Issue Costs	1,362	-
Non-capital Losses	13,731	32,342
Capital Losses and Other	4,001	-
	$ 85,725	$ 43,921

The following table summarizes the unrecognized temporary differences for which no tax asset has been recorded:

	December 31, 2015	December 31, 2014
Non-capital losses	$ 13,731	$ 16,684
Capital losses	3,741	3,780
	$ 17,472	$ 20,464

The following tables provide a continuity of the deferred income tax asset (liability):

	December 31, 2013	Recognized in profit and loss	Recognized in equity and other	December 31, 2014
Decommissioning obligation	$ 9,483	$ 2,329	$ 174	$ 11,986
Non-capital losses	6,290	2,849	696	9,835
Property, plant and equipment	(30,459)	(6,922)	(2,477)	(39,858)
Other	124	(1,914)	(559)	(2,349)
	$ (14,562)	$ (3,658)	$ (2,166)	$ (20,386)

	December 31, 2014	Recognized in profit and loss	Recognized in equity and other	December 31, 2015
Decommissioning obligation	$ 11,986	$ (1,447)	$ 475	$ 11,014
Non-capital losses	9,835	236	1,844	11,915
Property, plant and equipment	(39,858)	20,210	(5,821)	(25,469)
Flow-through share premium	-	1,635	(1,635)	-
Other	(2,349)	469	(14)	(1,894)
	$ (20,386)	$ 21,103	$ (5,151)	$ (4,434)

14. Supplemental cash flow information:

	December 31, 2015	December 31, 2014
Change in non-cash working capital items:		
Accounts receivable	$ 4,445	$ 1,939
Prepaid expenses and deposits	603	(343)
Inventory	49	(26)
Accounts payable and accrued liabilities	(7,369)	2,908
	$ (2,272)	$ 4,478
Amounts relating to operating activities	$ 2,039	$ (291)
Amounts relating to financing activities	(116)	153
Amounts relating to investing activities	(4,195)	4,616
	$ (2,272)	$ 4,478

15. Segmented information:

A portion of the Company's assets and revenues are earned in the United States and Canada, and are monitored as an identifiable reporting segment by management. Business risks and economic indicators are similar across both geographical regions.

Year ended December 31, 2015 (000's Cdn. $)	Canada	U.S.	Total
Oil and gas revenue	31,623	23,459	55,082
Operating income (1)	9,257	12,431	21,688
Funds from operations (2)	24,013	6,341	30,354
Loss before income taxes	(12,992)	(52,259)	(65,251)
Loss after income taxes	(11,357)	(32,623)	(43,980)
Exploration and evaluation assets (as at December 31, 2015)	1,114	-	1,114
Property, plant and equipment (as at December 31, 2015)	90,889	62,752	153,641
Property, plant and equipment expenditures	12,765	7,537	20,302
Exploration and evaluation expenses	3,409	-	3,409
Exploration and evaluation impairment	2,025	-	2,025
Property, plant and equipment impairment	10,431	45,385	55,816
Proceeds on property dispositions	(1,882)	-	(1,882)

Year ended December 31, 2014 (000's Cdn. $)	Canada	U.S.	Total
Oil and gas revenue	66,121	50,993	117,114
Operating income (1)	29,653	31,377	61,030
Funds from operations (2)	31,589	22,974	54,563
Income (loss) before income taxes	17,924	12,344	30,268
Income (loss) after income taxes	18,516	7,125	25,641
Exploration and evaluation assets (as at December 31, 2014)	3,639	-	3,639
Property, plant and equipment (as at December 31, 2014)	109,194	97,126	206,320
Property, plant and equipment expenditures	24,183	28,864	53,047
Exploration and evaluation expenses	4,010	-	4,010
Exploration and evaluation impairment	5,199	-	5,199
Property dispositions	(100)	-	(100)
Property acquisitions	152	-	152

(1) Defined as oil and gas revenues less royalties, operating costs and transportation. Operating income does not have any standardized meaning prescribed by IFRS and therefore this term may not be comparable with the calculation of for other entities.
(2) Defined as operating income less general and administrative expenses, interest and financing, plus or minus realized foreign exchange gains or losses expenses. Funds from operations does not have any standardized meaning prescribed by IFRS and therefore this terms may not be comparable with the calculation for other entities.

16. Commitments and contingencies:

a) Office premises, equipment leases and firm service transportation:

The Company leases its office premises, computer and office equipment and field vehicles through operating leases for accounting purposes.

The total estimated operating lease commitments are summarized as follows:

(000's Cdn. $)	2016	2017	2018	2019	2020
Flow-through share commitments	2,120	-	-	-	-
Lease of office premises	550	321	-	-	-
Equipment, vehicle and computer leases and software licenses	321	144	18	1	-
Total	2,991	465	18	1	-

b) Outstanding lawsuits:

Various lawsuits have been filed against the Company for incidents which arose in the ordinary course of business. In the opinion of management, the outcome of any of the lawsuits, now pending, are not material to the Company's operations. Should any loss result from the resolution of these claims in addition to amounts provided in the financial statements, such loss will be charged to earnings in the year of resolution.

17. Personnel expenses:

The aggregate compensation expense of all employees included in operating and transportation expenses, in general and administrative expenses, and in property, plant and equipment was as follows:

	2015	2014
Salaries, wages and benefits	$ 4,742	$ 4,972
Share based compensation (recovery)	(689)	1,797
	$ 4,053	$ 6,769

Personnel expenses directly attributed to capital activities have been capitalized and included in property, plant and equipment and intangible exploration assets.

The Company has determined that the key management personnel consist of its officers and directors. Key management personnel compensation is comprised of the following:

	2015	2014
Salaries, wages, benefits and directors' fees	$ 1,876	$ 1,842
Share based compensation (recovery)	(440)	1,009
	$ 1,436	$ 2,851