

# STATEMENTS OF FINANCIAL POSITION

(Unaudited)

As at	June 30, 2016	December 31, 2015
(000s)	(\$)	(\$)
<b>ASSETS</b>		
<b>Current assets</b>		
Accounts receivable	8,400	10,927
Deposits and prepaid expenses	1,092	753
Derivative financial instruments (note 12)	–	7,615
	9,492	19,295
<b>Non-current assets</b>		
Exploration and evaluation assets (note 5)	37,496	37,463
Property and equipment (note 6)	244,066	241,940
<b>Total assets</b>	<b>291,054</b>	<b>298,698</b>
<b>LIABILITIES</b>		
<b>Current liabilities</b>		
Bank debt (note 7)	24,199	37,012
Accounts payable and accrued liabilities	9,814	13,218
Dividend payable	1,176	1,062
Derivative financial instruments (note 12)	728	–
	35,917	51,292
<b>Non-current liabilities</b>		
Decommissioning liabilities (note 8)	14,098	13,349
Flow-through share premium liability (note 9)	578	–
Derivative financial instruments (note 12)	104	–
Deferred tax liability	20,765	22,764
<b>Total liabilities</b>	<b>71,462</b>	<b>87,405</b>
<b>SHAREHOLDERS' EQUITY</b>		
Share capital (note 9)	410,697	388,949
Contributed surplus	14,800	14,479
Deficit	(205,905)	(192,135)
<b>Total shareholders' equity</b>	<b>219,592</b>	<b>211,293</b>
<b>Total liabilities and shareholders' equity</b>	<b>291,054</b>	<b>298,698</b>

See accompanying notes to the condensed interim financial statements.

# STATEMENTS OF OPERATIONS AND COMPREHENSIVE INCOME (LOSS)

(Unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2016	2015	2016	2015
(000s, except per share amounts)	(\$)	(\$)	(\$)	(\$)
<b>REVENUE</b>				
Oil and natural gas revenues	11,837	33,989	19,854	80,066
Royalties	(3,479)	(9,226)	(5,338)	(19,197)
Oil and natural gas revenues, net of royalties	8,358	24,763	14,516	60,869
Unrealized (loss) on financial instruments	(5,810)	(11,143)	(8,473)	(13,905)
Realized gain on financial instruments	941	4,746	3,856	11,662
	3,489	18,366	9,899	58,626
<b>EXPENSES</b>				
Operating and transportation	2,066	6,277	4,138	18,030
General and administrative	799	1,334	1,552	3,328
Transaction costs – general and administrative (note 4)	–	3,287	–	3,661
Depletion and depreciation (note 6)	4,473	11,902	9,069	32,926
Share-based compensation (note 10)	1,369	440	2,475	1,092
Transaction costs – share-based compensation (note 4)	–	4,027	–	4,027
Exploration and evaluation expense (note 5)	604	–	771	344
Gain on disposition to Boulder (note 4)	–	(154,034)	–	(154,034)
Accretion and finance expenses	491	1,504	858	3,019
	9,802	(125,263)	18,863	(87,607)
Income (loss) before income tax	(6,313)	143,629	(8,964)	146,233
<b>TAXES</b>				
Deferred income tax expense (recovery)	(1,303)	(6)	(1,696)	837
<b>Net income (loss) and comprehensive income (loss) for the period</b>	<b>(5,010)</b>	<b>143,635</b>	<b>(7,268)</b>	<b>145,396</b>
Net income (loss) per share (note 9)				
Basic	(0.16)	4.78	(0.23)	4.87
Diluted	(0.16)	4.77	(0.23)	4.86

See accompanying notes to the condensed interim financial statements.

# STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY

(Unaudited)

	Share Capital	Contributed Surplus	Retained Earnings (Deficit)	Total Equity
(000s)	(\$)	(\$)	(\$)	(\$)
<b>Balance – January 1, 2016</b>	<b>388,949</b>	<b>14,479</b>	<b>(192,135)</b>	<b>211,293</b>
Share-based compensation	–	<b>3,819</b>	–	<b>3,819</b>
Common shares issued	<b>15,384</b>	–	–	<b>15,384</b>
Flow-through shares issued	<b>3,003</b>	–	–	<b>3,003</b>
Premium on flow-through shares	<b>(578)</b>	–	–	<b>(578)</b>
Tax benefit of share issuance costs	<b>302</b>	–	–	<b>302</b>
Issued on vesting of share incentives	<b>3,478</b>	<b>(3,478)</b>	–	–
Exercise of options	<b>159</b>	<b>(20)</b>	–	<b>139</b>
Dividends	–	–	<b>(6,502)</b>	<b>(6,502)</b>
Net loss	–	–	<b>(7,268)</b>	<b>(7,268)</b>
<b>Balance – June 30, 2016</b>	<b>410,697</b>	<b>14,800</b>	<b>(205,905)</b>	<b>219,592</b>
Balance – January 1, 2015	381,540	12,591	69,378	463,509
Share-based compensation	–	5,888	–	5,888
Exercise of options	7,344	(5,932)	–	1,412
Distribution of non-cash assets (note 4)	–	–	(404,825)	(404,825)
Dividends	–	–	(910)	(910)
Net income	–	–	145,396	145,396
Balance – June 30, 2015	388,884	12,547	(190,961)	210,470

See accompanying notes to the condensed interim financial statements.

# STATEMENTS OF CASH FLOWS

(Unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2016	2015	2016	2015
(000s)	(\$)	(\$)	(\$)	(\$)
<b>Cash flow from (used in):</b>				
<b>Operating activities</b>				
Net income (loss) for the period	(5,010)	143,635	(7,268)	145,396
Adjustments for:				
Depletion and depreciation expense (note 6)	4,473	11,902	9,069	32,926
Deferred income tax expense (recovery)	(1,303)	(6)	(1,696)	837
Share-based compensation (note 10)	1,369	454	2,475	1,147
Transaction costs – share-based compensation (note 4)	–	4,027	–	4,027
Accretion (note 8)	71	126	148	327
Unrealized loss on financial instruments (note 12)	5,810	11,143	8,473	13,905
Exploration and evaluation expense (note 5)	604	–	771	344
Gain on disposition of Boulder (note 4)	–	(154,034)	–	(154,034)
Abandonment and reclamation costs (note 8)	–	(56)	–	(61)
	6,014	17,191	11,972	44,814
Change in non-cash working capital (note 11)	(842)	5,335	(686)	(4,681)
	5,172	22,526	11,286	40,133
<b>Financing activities</b>				
Change in bank debt	(14,815)	(143,470)	(12,813)	(111,044)
Assumption of debt from Boulder transaction (note 4)	–	130,000	–	130,000
Dividends	(3,313)	(910)	(6,502)	(910)
Issuance of share capital	19,573	1,412	19,645	1,412
Share issuance costs	(1,119)	–	(1,119)	–
Change in non-cash working capital (note 11)	113	910	113	910
	439	(12,058)	(676)	20,368
<b>Investing activities</b>				
Property and equipment expenditures	(5,519)	(11,979)	(9,467)	(46,804)
Exploration and evaluation expenditures	(212)	23	(586)	(2,212)
Changes in non-cash working capital (note 11)	115	1,488	(529)	(11,485)
	(5,616)	(10,468)	(10,582)	(60,501)
<b>Foreign exchange gain on cash and cash equivalents held in foreign currency</b>	5	–	(28)	–
<b>Change in cash and cash equivalents</b>	–	–	–	–
<b>Cash and cash equivalents – beginning of period</b>	–	–	–	–
<b>Cash and cash equivalents – end of period</b>	–	–	–	–

See accompanying notes to the condensed interim financial statements.

# NOTES TO THE FINANCIAL STATEMENTS

As at and for the three and six month periods ended June 30, 2016  
(Unaudited)

## 1 REPORTING ENTITY

Granite Oil Corp. ("Granite" or the "Company") is a publicly traded company incorporated under the laws of Alberta. The Company is a dividend-paying, junior oil producer based in Calgary, Alberta that is principally engaged in the exploration for and exploitation, development and production of oil and natural gas, and conducts some of its activities jointly with others. These financial statements reflect only the Company's interests in such activities. Granite is registered and domiciled in Canada. Its main office is at 432, 222 Third Avenue S.W., Calgary, Alberta, T2P 0B4.

## 2 BASIS OF PRESENTATION

### (a) Statement of Compliance

These condensed interim financial statements for the three and six months ended June 30, 2016 were prepared in accordance with International Financial Reporting Standard 34 "Interim Financial Reporting" as issued by the International Accounting Standards Board (IASB).

The condensed interim financial statements should be read in conjunction with the Company's audited financial statements for the year ended December 31, 2015.

These financial statements were authorized for issuance by the Board of Directors on August 11, 2016.

### (b) Basis of Measurement

The financial statements of Granite were prepared on the historical cost basis, except for derivative financial instruments, which are measured at fair value. The methods used to measure fair values are discussed in note 12.

### (c) Use of Estimates and Judgements

Significant estimates and judgements made by management in the preparation of these condensed interim financial statements remain unchanged and are outlined in Note 2 of the December 31, 2015 audited annual financial statements.

## 3 SIGNIFICANT ACCOUNTING POLICIES

### (a) Current Accounting Policies

The Company's accounting policies are described in Note 3 of the December 31, 2015 audited annual financial statements. Those accounting policies have been applied consistently to all periods presented in these condensed interim financial statements.

### (b) Future Accounting Policy Changes

In July 2014, IFRS 9 "Financial Instruments" was issued as a complete standard, including the requirements previously issued related to classification and measurement of financial assets and liabilities, and additional amendments to introduce a new expected loss impairment model for financial assets, including credit losses. Retrospective application of this standard with certain exemptions is effective for fiscal years beginning on or after January 1, 2018, with earlier application permitted. The full impact of the standard on the Company's financial statements is currently being assessed by the Company.

In May 2014, the IASB issued IFRS 15 “Revenue from Contracts with Customers”. It replaces existing revenue recognition guidance and provides a single, principles based five-step model to be applied to all contracts with customers. Retrospective application of this standard is currently effective for fiscal years beginning on or after January 1, 2018, with earlier application permitted. The Company is currently assessing the impact of this standard.

In January 2016, IFRS 16 “Leases” was issued and replaces IAS 17. The standard is required to be adopted either retrospectively or by recognizing the cumulative effect of initially applying IFRS 16 as an adjustment to opening equity at the date of initial application. IFRS 16 is effective for fiscal years beginning on or after January 1, 2019 with earlier adoption permitted if IFRS 15 “Revenue from Contracts with Customers” has also been adopted. The Company is currently evaluating the impact of the standard.

## 4 PLAN OF ARRANGEMENT

On April 7, 2015, DeeThree Exploration Ltd. (“DeeThree”), as the Company was then called, and Boulder Energy Ltd. (“Boulder”) entered into a Plan of Arrangement (the “POA”) whereby DeeThree transferred its oil and natural gas properties located in the Brazeau Belly River and Peace River Arch areas of Northern Alberta, Canada (collectively “Northern Assets”) to Boulder and each DeeThree shareholder received one third (0.3333) of one share of New DeeThree shares and one half (0.5) of one share of Boulder. On May 14, 2015, the holders of common shares of DeeThree approved the POA. The POA was completed on May 15, 2015.

In addition to the Northern Assets being transferred from DeeThree to Boulder, debt of \$130 million as well as decommissioning liabilities, derivative financial instruments and a deferred tax liability were also transferred pursuant to the POA.

Year ended December 31, 2015

### Fair market value of Boulder Assets given up:

Fair market value of Boulder shares issued	(404,825)
Carrying value of Boulder net assets given up	252,829
Gain on disposition of assets	(151,996)

### Assets and liabilities transferred to Boulder:

Assumption of debt by Boulder	(130,000)
Property and equipment	403,802
Exploration and evaluation assets	26,988
Decommissioning liabilities	(24,284)
Derivative financial instruments	(512)
Deferred income taxes	(24,400)
Working capital	1,235
Carrying value of Boulder net assets given up	252,829

This transaction was considered to be a distribution of non-cash assets and was recorded at the fair market value of the Northern Assets at May 15, 2015. The weighted average trading price of Boulder shares after they commenced trading was used to determine the fair value of the net assets given up or \$8.89 per common share. The carrying value was determined using the historical costs as recorded by DeeThree. The \$152.0 million difference between Boulder’s fair value of \$404.8 million and carrying value of \$252.8 million was recognized on the statement of operations and comprehensive income as a gain on disposition of assets and reflects adjustments to the carrying value of Boulder net assets given up recorded subsequent to June 30, 2015.

The Company incurred \$3.7 million in cash transaction costs related to the POA during the six months ended June 30, 2016, including financial advisory accounting, legal and consulting fees recognized as “transaction costs – general and administrative” in the statement of operations and comprehensive income. For the options that were cancelled in relation to the POA, the remaining share based compensation of \$4.0 million for the six months ended June 30, 2016, was immediately recognized and expensed in the statement of operations and comprehensive income as “transaction costs – share-based compensation”.

## 5 EXPLORATION AND EVALUATION ASSETS

	Six Months Ended June 30, 2016	Year Ended December 31, 2015
<i>(\$000s)</i>		
Balance – beginning of period	<b>37,463</b>	62,784
Additions	<b>835</b>	6,600
Disposition to Boulder (note 4)	–	(26,988)
Transfers to property and equipment	<b>(31)</b>	(742)
E&E expenses	<b>(104)</b>	(2,891)
Lease expiries	<b>(667)</b>	(1,300)
Balance – end of period	<b>37,496</b>	37,463

During the six month period ended June 30, 2016, the Company expensed \$0.1 million of preliminary drilling costs incurred related to the preparation of contingent locations (year ended December 31, 2015 - \$2.9 million on two vertical stratigraphic test wells in the Alberta Bakken) and \$0.7 million related to lease expiries on undeveloped land (year ended December 31, 2015 – \$1.3 million).

During the six month period ended June 30, 2016, approximately \$0.1 million of directly attributable general and administrative expense and \$0.2 million of directly attributable share-based compensation expense were capitalized as expenditures on exploration and evaluation assets (year ended December 31, 2015 – \$0.1 million and \$0.2 million, respectively).

## 6 PROPERTY AND EQUIPMENT

	Oil and Natural Gas Properties	Office Equipment	Total
(\$000s)			
<b>Cost</b>			
Balance – January 1, 2015	824,725	474	825,199
Additions	62,813	49	62,862
Dispositions to Boulder (note 4)	(584,791)	–	(584,791)
Transfers from E&E assets	742	–	742
<b>Balance – December 31, 2015</b>	<b>303,489</b>	<b>523</b>	<b>304,012</b>
<b>Additions</b>	<b>11,158</b>	<b>6</b>	<b>11,164</b>
<b>Transfers from exploration and evaluation assets</b>	<b>31</b>	<b>–</b>	<b>31</b>
<b>Balance – June 30, 2016</b>	<b>314,678</b>	<b>529</b>	<b>315,207</b>
<b>Accumulated depletion and depreciation</b>			
Balance – January 1, 2015	198,035	222	198,257
Depletion and depreciation for the year	44,743	61	44,804
Dispositions to Boulder (note 4)	(180,989)	–	(180,989)
<b>Balance – December 31, 2015</b>	<b>61,789</b>	<b>283</b>	<b>62,072</b>
<b>Depletion and depreciation for the period</b>	<b>9,038</b>	<b>31</b>	<b>9,069</b>
<b>Balance – June 30, 2016</b>	<b>70,827</b>	<b>314</b>	<b>71,141</b>
<b>Net book value</b>			
December 31, 2015	241,700	240	241,940
<b>June 30, 2016</b>	<b>243,851</b>	<b>215</b>	<b>244,066</b>

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

During the period ended June 30, 2016, approximately \$0.2 million of directly attributable general and administrative expense and \$1.1 million of directly attributable share-based compensation expense were capitalized as expenditures on property and equipment (year ended December 31, 2015 – \$1.0 million and \$1.2 million, respectively).

### (b) Future Development Costs and Salvage Value

During the six months ended June 30, 2016, an estimated \$69.3 million of future development costs associated with proved plus probable undeveloped reserves were included in the calculation of depletion and depreciation expense and an estimated \$10.0 million of salvage value of production equipment was excluded (December 31, 2015 – \$73.4 million and \$10.0 million, respectively).

## 7 BANK DEBT

At June 30, 2016 the Company had a revolving demand credit facility (the “Credit Facility”) with an authorized borrowing base of \$60 million, including a \$45 million extendible revolving facility and a \$15 million operating facility (December 31, 2015, an authorized borrowing base of \$80 million, including a \$60 million extendible revolving facility and a \$20 million operating facility). The Credit Facility is considered a current liability due to its demand term.

Interest is charged at a rate per annum equal to the Canadian prime rate during the period plus the applicable margin, being



a range of 0.50 percent to 2.50 percent, depending on the Company's debt to cash flow ratio as determined by its lender. Standby fees associated with the facility are charged based on an applicable margin, being a range of 0.2 percent to 0.45 percent per annum on the undrawn portion of the facility, again based on the Company's debt to cash flow ratio. Under the Credit Facility, the Company is required to maintain a current ratio of not less than 1:1. The current ratio is calculated as current assets (excluding derivative financial instruments) plus any undrawn availability in the Credit Facility versus current liabilities (excluding derivative financial instruments and any amounts drawn on the Credit Facility). At June 30, 2016, the Company was in compliance with the current ratio requirement.

At June 30, 2016, \$24.2 million was drawn against this facility (December 31, 2015 – \$37.0 million). The amount of the facility is subject to a borrowing base test performed on a periodic basis by the lenders, based primarily on reserves and using commodity prices estimated by the lenders as well as other factors. The borrowing base of the credit facility is subject to review at least semi-annually with the next review to take place by October 2016. A decrease in the borrowing base could result in a reduction to the credit facility. Collateral for this facility consists of a general security agreement, providing a security interest over all present and subsequently acquired personal property and a floating charge on all present and subsequently acquired land interests of the Company.

## 8 DECOMMISSIONING LIABILITIES

The Company has estimated the net present value of decommissioning obligations to be \$14.1 million as at June 30, 2016 (December 31, 2015 – \$13.3 million) based on an undiscounted total future liability of \$18.0 million (December 31, 2015 – \$17.6 million). These payments are expected to be incurred over a period of two to 20 years with the majority of costs to be incurred between 2018 and 2028. At June 30, 2016, a risk-free rate of 2.00 percent (December 31, 2015 – 2.25 percent) and an inflation rate of 2.00 percent (December 31, 2015 – 2.00 percent) were used to calculate the net present value of the decommissioning liabilities.

	Six Months Ended June 30, 2016	Year Ended December 31, 2015
(\$000s)		
Balance – beginning of period	13,349	34,165
Liabilities incurred	235	1,272
Liabilities disposed to Boulder (note 4)	—	(24,284)
Revisions	366	1,941
Settlements	—	(216)
Accretion of decommissioning liabilities	148	471
Balance – end of period	14,098	13,349

## 9 SHARE CAPITAL

### (a) Authorized

Unlimited number of common voting shares, no par value.

Unlimited number of preferred shares, no par value, issuable in series.

## (b) Issued – Common Shares

	Six Months Ended June 30, 2016		Year Ended December 31, 2015	
	Shares	Amount	Shares	Amount
	(#)	(\$000s)	(#)	(\$000s)
Balance – beginning of period	30,355,024	388,949	29,655,187	381,540
Common shares issued (ii)	2,324,300	16,503	–	–
Exercise of options (iv)	36,925	159	699,837	7,409
Flow-through shares issued (iii)	330,000	3,003	–	–
Premium on flow-through shares (iii)	–	(578)	–	–
Issued on vesting of share incentives	542,196	3,478	–	–
Share issuance costs	–	(1,119)	–	–
Tax benefit of share issuance costs	–	302	–	–
Balance – end of period	33,588,445	410,697	30,355,024	388,949

### i) Plan of Arrangement

In May 2015, in connection with the POA, the Company's outstanding common shares were exchanged whereby each previous DeeThree shareholder received one third (0.3333) of a Granite share and one-half (0.5) a share of Boulder for each DeeThree share previously held. This adjustment in shares has been retrospectively applied to all current and comparative periods within these financial statements.

### ii) Common Share Issuance

In June 2016, the Company issued 2,324,300 common shares pursuant to a public offering for total gross proceeds of \$16.5 million (\$15.4 million net of estimated share issuance costs), including 211,300 common shares issued pursuant to the exercise of an over-allotment held by the underwriters.

### iii) Flow-through Share Issuance

In May 2016, the Company issued 330,000 flow-through shares for total gross proceeds of \$3.0 million. The implied premium on the flow-through shares of \$1.75 per share or \$0.6 million was recorded as a liability on the statement of financial position and remains at June 30, 2016. To date, the Company has incurred \$nil of the total \$3.0 million qualifying expenditures, with the entire amount to be incurred by December 31, 2017.

### iv) Exercising of Options

During the six months ended June 30, 2016, 36,925 options were exercised at a weighted-average price of \$3.77 per share for total cash proceeds of \$0.1 million and previously recognized share-based compensation expense of \$0.02 million.

The presentation of the number of DeeThree options below does not reflect the share adjustment of 0.3333 in connection with the POA.

During the year ended December 31, 2015 the Company issued 686,506 common shares in Granite as a result of 3,631,260 DeeThree options exercised. These included 465,101 DeeThree options exercised for total cash proceeds of \$1.4 million and previously recognized share-based compensation expense of \$0.8 million. It also included 3,166,159 DeeThree options exercised on a cashless basis in connection with the POA, with previously recognized share-based compensation expense of \$5.1 million. In addition to the DeeThree options exercised, 13,331 Granite options were exercised during the year ended December 31, 2015, for total cash proceeds of \$0.06 million and previously recognized share-based compensation expense of \$0.01 million.

### (c) Per Share Amounts

Per share amounts were calculated on the weighted-average number of shares outstanding. The basic and diluted shares outstanding were as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2016	2015	2016	2015
<i>(000s, except per share amounts)</i>	<i>(\$)</i>	<i>(\$)</i>	<i>(\$)</i>	<i>(\$)</i>
Net income (loss) for the period	<b>(5,010)</b>	143,635	<b>(7,268)</b>	145,396
Weighted-average number of common shares	<i>(#)</i>	<i>(#)</i>	<i>(#)</i>	<i>(#)</i>
– basic	<b>31,846</b>	30,044	<b>31,095</b>	29,850
– diluted	<b>31,846</b>	30,118	<b>31,095</b>	29,914
Net income per weighted average common share	<i>(\$)</i>	<i>(\$)</i>	<i>(\$)</i>	<i>(\$)</i>
– basic	<b>(0.16)</b>	4.78	<b>(0.23)</b>	4.87
– diluted	<b>(0.16)</b>	4.77	<b>(0.23)</b>	4.86

## 10 SHARE- BASED COMPENSATION

### (a) Replacement Options

DeeThree's stock option plan was terminated in connection with the POA. Unvested in-the-money DeeThree options that were outstanding at the time of the completion of the POA were replaced with options to acquire shares of Granite and Boulder respectively. Replacement options were issued based on the exercise price proportion of the fraction A/B, where A is the volume weighted average price of the Boulder common shares on the first five trading days on the TSX and B is the aggregate of (i) the volume weighted average price of Boulder common shares for the first five trading days on the TSX and (ii) the volume weighted average price of the Granite common shares on the first five trading days on the TSX. All Granite replacement options granted under the POA maintain the same vesting and expiry dates as the original DeeThree options that were previously issued.

The number and weighted-average exercise prices of replacement stock options are as follows:

	Six Months Ended June 30, 2016		Year Ended December 31, 2015	
	Options	Weighted-Average Exercise Price	Options	Weighted-Average Exercise Price
	(#)	(\$)	(#)	(\$)
Outstanding – January 1	194,486	3.96	–	–
Issued	–	–	207,817	3.96
Exercised	(36,925)	3.77	(13,331)	4.05
Outstanding – end of period	157,561	4.00	194,486	3.96
Exercisable – end of period	148,563	3.84	82,646	3.13

  

Exercise Price	Weighted-Average Contractual Outstanding	Options Life	Weighted-Average Exercisable
(\$)	(#)	(years)	(#)
<b>As at June 30, 2016</b>			
<b>2.00 – 4.99</b>	<b>139,564</b>	<b>0.53</b>	<b>139,564</b>
<b>5.00 – 6.80</b>	<b>17,997</b>	<b>1.31</b>	<b>8,999</b>
	<b>157,561</b>	<b>0.62</b>	<b>148,563</b>

Gross share-based compensation for the options was \$0.03 million for the six month period ended June 30, 2016 (year ended December 31, 2015 - \$1.7million). Of this amount, \$nil was capitalized (year ended December 31, 2015 – \$0.7 million), resulting in total net share-based compensation expense related to options of \$0.03 million for the period (year ended December 31, 2015 - \$1.0 million).

### (b) Share Incentive Plan

On May 15, 2015, Granite adopted a Share Incentive Plan ("SIP") for directors, officers, certain employees and eligible consultants. The SIP consists of performance based awards and time based awards. Both the TBAs and the PBAs vest one third on each of the first, second and third anniversaries of the grant date. The PBAs granted are subject to a

performance multiplier ranging from 0 to 2. The payout multiplier is dependent on the performance of Granite at the end of the vesting period relative to corporate performance measures determined at the discretion of Granite's Board of Directors. The number of common shares issued for each PBA and TBA granted is adjusted for the payments of dividends from the date of the grant to the payment date. On the payment date, Granite has sole and absolute discretion to settle the awards in the form of either cash or common shares, or some combination thereof.

The number of PBAs is as follows:

	<b>Six Months Ended June 30, 2016</b>	<b>Year Ended December 31, 2015</b>
	PBAs	PBAs
	(#)	(#)
Outstanding – January 1	<b>829,103</b>	–
Issued	–	829,103
Redeemed	<b>(276,367)</b>	–
Outstanding – end of period	<b>552,736</b>	829,103

The fair value of the PBAs is determined at the grant date using the binomial option-pricing model, multiplied by the estimated performance multiplier. During the six months ended June 30, 2016, 276,367 PBAs were redeemed for 503,565 common shares reflecting a performance multiplier of 1.75 and adjustment for dividends from the date of the original grant to the payment date. A performance multiplier of 1.5 has been assumed for the remaining PBAs outstanding at June 30, 2016 (December 31, 2015 – 1.0). Fluctuations in share based compensation expense may occur due to changes in estimates of performance outcomes.

Gross share-based compensation related to PBAs was \$3.4 million for the six months ended June 30, 2016 (year ended December 31, 2015 - \$1.8 million). Of this amount, \$1.2 million was capitalized (year ended December 31, 2015 – \$0.6 million), resulting in total net share-based compensation expense related to PBAs of \$2.2 million for the year (year ended December 31, 2015 - \$1.2 million).

The number of TBAs is as follows:

	<b>Six Months Ended June 30, 2016</b>	<b>Year Ended December 31, 2015</b>
	TBAs	TBAs
	(#)	(#)
Outstanding – January 1	<b>115,892</b>	–
Issued	–	115,892
Redeemed	<b>(38,631)</b>	–
Outstanding – end of period	<b>77,261</b>	115,892

The fair value of the TBAs is determined at the grant date using the binomial option-pricing model. Fluctuations in share based compensation expense may occur due to changes in estimates of performance outcomes. During the six months ended June 30, 2016, 38,631 TBAs were redeemed for 38,631 common shares.

Gross share-based compensation related to TBAs was \$0.3 million for the six months ended June 30, 2016 (year ended December 31, 2015 - \$0.2 million). Of this amount, \$0.1 million was capitalized (year ended December 31, 2015 – \$0.1 million), resulting in total net share-based compensation expense related to TBAs of \$0.2 million for the year (year ended December 31, 2015 - \$0.1 million).

## 11 SUPPLEMENTAL CASH FLOW INFORMATION

Changes in non-cash working capital are comprised of:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2016	2015	2016	2015
(\$000s)				
Accounts receivable	(1,891)	10,637	2,527	16,745
Deposits and prepaid expenses	(295)	(629)	(339)	(1,165)
Accounts payable and accrued liabilities	1,572	(2,275)	(3,290)	(30,836)
	(614)	7,733	(1,102)	(15,256)
Related to operating activities	(842)	5,335	(686)	(4,681)
Related to financing activities	113	910	113	910
Related to investing activities	115	1,488	(529)	(11,485)
	(614)	7,733	(1,102)	(15,256)

## 12 DETERMINATION OF FAIR VALUES

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

Granite classifies the fair value of these transactions according to the following hierarchy based on the nature of the observable inputs used to value the instrument.

- 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 volume to provide continuous pricing information.
- Level 2 – Pricing inputs are other than quoted prices in active markets included in Level 1. Prices 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 are derived from inputs that are not based on observable market data.

The carrying value of accounts receivable, accounts payable and accrued liabilities and dividend payable included in the statement of financial position approximate fair value due to the short-term nature of those instruments. The fair value measurement of the derivative financial instruments has a fair value classification of Level 2.

### (a) Property and Equipment and E&E Assets

The fair value of property and equipment recognized in a business combination is based on market values. The market value of property and equipment is the estimated amount for which property 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 market value of petroleum and natural gas properties (included in property and equipment) and E&E 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.

The market value of other items of property and equipment is based on the quoted market prices for similar items.

**(b) Accounts Receivable, Accounts Payable and Accrued Liabilities and Dividend Payable**

The fair value of accounts receivable, accounts payable and accrued liabilities and dividend payable is estimated as the present value of future cash flows, discounted at the market rate of interest at the reporting date. The fair value of these balances approximated their carrying value at June 30, 2016 due to their short term to maturity.

**(c) Stock Options**

The fair value of stock options is measured using the Black-Scholes option-pricing model. Measurement inputs include share price on measurement date, exercise price of the instrument, expected volatility (based on weighted- average historical volatility adjusted for changes expected due to publicly available information), weighted-average expected life of the instruments (based on historical experience and general option-holder behaviour) and the risk- free interest rate (based on Government of Canada bonds).

**(d) Performance Based Awards and Time Based Awards**

The fair value of awards granted under the SIP is measured using the binomial model. Measurement inputs include share price on measurement date, expected volatility (based on weighted-average historical volatility adjusted for changes expected due to publicly available information), weighted-average expected life of the instruments (based on the terms of the agreement) and the risk-free interest rate (based on Government of Canada bonds).

**(e) Derivative Financial Instruments**

The fair value measurement of the derivative financial instruments has a fair value hierarchy of Level 2.

As at June 30, 2016, the Company had the following crude oil risk management contracts, with a total mark-to-market liability of \$0.8 million (December 31, 2015 – \$7.6 million asset):

**CRUDE OIL CONTRACTS**

Remaining Period	Commodity	Type of Contract	Quantity	Pricing Point	Contract Price	Fair Value Asset (Liability) (\$ (000s)
Jul. 1/16 – Dec 31/16	Crude Oil	Fixed	250 bbls/d	WTI-NYMEX	Cdn \$78.00/bbl	CAD 731
Jul. 1/16 – Dec. 31/16	Crude Oil	Fixed	250 bbls/d	WTI-NYMEX	US \$62.75/bbl	USD 692
Jul. 1/16 – Dec. 31/16	Crude Oil	Fixed	250 bbls/d	WTI-NYMEX	Cdn \$80.00/bbl	CAD 838
Jul. 1/16 – Dec. 31/16	Crude Oil	Fixed	250 bbls/d	WTI-NYMEX	US \$32.02/bbl	USD (949)
Jul. 1/16 – Dec. 31/16	Crude Oil	Fixed	250 bbls/d	WTI-NYMEX	US \$40.00/bbl	USD (457)
Jul. 1/16 – Jun. 30/17	Crude Oil	Fixed	250 bbls/d	WTI-NYMEX	US \$41.00/bbl	USD (903)
Jan. 1/17 – Jun. 30/17	Crude Oil	Fixed	250 bbls/d	WTI-NYMEX	US \$47.00/bbl	USD (222)
Jan. 1/17 – Dec. 31/17	Crude Oil	Fixed	250 bbls/d	WTI-NYMEX	US \$53.00/bbl	USD 54
Jan. 1/17 – Dec.31/17 <sup>(1)</sup>	Crude Oil	Fixed	250 bbls/d	WTI-NYMEX	US \$52.50/bbl	USD 8

(1) Subsequent to June 30, 2016, this crude oil contract was unwound and terminated.